SEATTLE CITY COUNCIL
CENTRAL STAFF

July 17, 2023

MEMORANDUM

To:	Finance and Housing Committee
From:	Tom Mikesell, Analyst
Subject:	Summary and Fiscal Note Template and Process Review

On Wednesday, July 19, 2023, the Finance and Housing Committee will receive a briefing and discuss potential changes to the template and process for reviewing summary and fiscal notes. This memorandum reviews the current process and format used for communicating the potential fiscal impacts of proposed legislation. Based on an assessment of best practices and recent examples, insights and alternative options for producing fiscal notes are offered and next steps are outlined at the end of the memo.

Central Staff conducted this review after discussions with the Budget Chair, other councilmembers, and the City Budget Office, who have a shared interest in improving the utility of the Summary and Fiscal Note (fiscal note) template that is a required attachment for all legislation that comes before the Council. The goal is to update the template and modify internal processes for the development and review of fiscal notes to:

- Improve information to the public and decisionmakers about fiscal and other impacts of legislation;
- Enhance the fiscal note's value as an input into budget and financial planning processes;
- Provide better oversight and accountability to foster an understanding of how policy decisions might impact short and long-term budget sustainability; and
- Clarify equity implications and resource trade-offs.

Background

A fiscal note is generally a written estimate of the potential expenditure and/or revenue changes that would occur if proposed legislation were adopted. Beyond that simple definition, however, there is a range of ways these estimates can be produced, including but not necessarily limited to the minimum standards for the information that they must contain and the staff that are responsible for preparing them. The following subsections include a history of recent legislation impacting the current template and process, a brief overview of the existing template, and an analysis of the template in the context of best practices and recent observations.

Legislative History

The *General Rules and Procedures of the Seattle City Council* require that "(a)ll Council Bills and Resolutions shall include a Summary and Fiscal Note"[1]. However, the requirements for what information to consider and include in the fiscal note are not specifically proscribed in the rules. Rather, the fiscal notes currently produced in the Council's legislative process are developed according to standards delineated in a combination of prior legislation, as follows:

- Enhanced Fiscal Notes for Capital Projects: Adopted in June 2010, Resolution (RES) 31203 updated the standards for fiscal notes for larger capital projects, particularly with regards to new public hearing procedures and information requirements for projects that involve partnership with a private organization. While specific changes to the existing Summary and Fiscal Note template were not provided for, an additional form, titled 'Additional Risk Analysis and Fiscal Analysis for Non-Utility Partner Project' was proscribed to demonstrate the financial wherewithal of these private partners, to help identify counterparty financial and implementation risks. The form to be completed and made publicly available is included as Attachment 1.
- Climate Change Impacts: Adopted in September 2020, RES 31933 updated the fiscal note template with questions related to the climate change implications of proposed legislation, including whether the proposal would impact greenhouse gas emissions and/or the City's ability to adapt to climate change. The updated template, which represents the format currently used in the legislative process[2], is included as Attachment 2.

In addition to these formal requirements added through legislation, over the years other changes to the form and process have been made by way of collaboration between legislative and executive staff in areas of clear policy alignment between branches of government. As an example, questions about how proposed legislation furthers the goals of the Race and Social Justice Initiative (RSJI) were added through this informal process.

Current Process and Template Overview

Under the current practice, using the template included for reference as Attachment 2, the City Budget Office coordinates fiscal notes for executive legislation, and Central Staff coordinates them for the council-generated legislation. Generally, for executive generated legislation, department staff complete the template and submit it with other legislative materials. The template includes four primary sections, as follows:

1. Bill Summary: Requests the legal title of the legislation, a narrative summary of the bill's effect, and any background information to add context.

2. Capital Improvement Program: Asks if the legislation affects either a new or existing capital improvement program (CIP) project, and, if answered in the affirmative, requires the inclusion of project-specific information, including the name and identification number; the physical location; the start and end dates; and the total cost through the end of the current six-year capital programming horizon. In addition, this section requests that a new or modified CIP project page be attached to the proposed legislation, and that a spending plan be included.

[1] Rule III.A.1.b of Att 1 to RES 32029

[2] Fiscal years have been updated compared to the version attached to RES 31933.

3. Summary of Financial Implications: Includes subsections with tables to display specific financial details, including:
    a. An overview section that asks if the bill amends the City budget, and if so, requests completion of a two-year (current and following year) table that shows, grouped by General Fund (GF) and Other Fund (i.e., any City fund that is not GF), a two-year display of appropriation, revenue, and position changes. Also included in this section is a question about other financial implications for the City that are not included as appropriation or revenue changes, including any long-term costs, and a question about whether there is a financial implication of not passing the legislation;
    b. A detail section that requests dollar amounts of appropriation changes, if any, that the bill would make in the current and following year, including a table to fill in details about the fund, department, and budget control level (the legal level of budget control in the City's budget) that would be impacted;
    c. A detail section that requests dollar amounts of revenues or reimbursements changes, if any, that the bill would make in the current and following year, including a table to add details about the impacted City fund and revenue source details; and,
    d. A detail section requesting information about position changes, if any, that the bill would make in the current and following year, including a table to include position-specific details. This table also includes a space to indicate if the positions sunset in the future.
4. Other Implications: Asks several specific qualitative questions about the legislation, including whether a public hearing is necessary, whether publication in a journal of record is required, whether a property parcel is impacted, and details about the measurable goals of any newly created programs. This section also asks specific questions about climate emissions and resiliency impacts, as well as perceived implications for RSJI principles, including potential impacts on vulnerable or historically disadvantaged communities and whether there is a Language Access plan for public communications.

As one or more sections of the template may not be applicable to every piece of legislation, it is often the case that the final fiscal note submitted into the legislative record will exclude one or more elements for which the drafter considers to be not applicable to the bill in question. In most cases, the fiscal note is not revised to accommodate changes that may occur due to accepted amendments in Council's deliberative process.

Best Practice Review

Fiscal notes are common in state and local legislative processes. Though centered on the practices at state legislatures, a 2015 article[3] produced by the Center for Budget and Policy Priorities (CBPP), based on a review of the processes at all 50 states, offers key practices for states to use to improve their fiscal note process. Given the similarities to the divided government inherent in the Mayor - Council form of city government, a state perspective can be a useful template for Seattle's process. Best practices noted in the CBPP materials, together with a comparison with Seattle's approach, include the following:

- Prepare Fiscal notes for all proposals: In some states, a fiscal note is only generated upon request by a legislator. The preferred practice, followed by 38 of the states surveyed, is to require a fiscal note for all proposed legislation. As noted in the previous section, the *General Rules and Procedures of the Seattle City Council* require a fiscal note for all legislation, which aligns with this best practice;

- Produce non-partisan estimates: The CBPP article suggests that embedding the responsibility for providing fiscal notes in an independent, non-partisan office insulates the results from the perception of political bias. Of the states surveyed, 33 rely on an independent, non-partisan entity or legislative office for fiscal notes. As discussed in the earlier section, in Seattle's process, the fiscal note is written by the department that submits the legislation; as such, it does not meet the CBPP-identified standard.

  Prior to submittal to the City Clerk, fiscal notes for executive-generated legislation are reviewed by the City Budget Office, which reports to the Mayor. Fiscal notes for City Council -generated legislation are usually written by Council Central Staff, which, while non-partisan, may be viewed as biased towards the legislative branch.

  That said, a potential closer fit to the CBPP best- practice would be to house the development of fiscal notes for all legislation with the Central Staff, given its non-partisan nature. However, current staffing levels would not be sufficient to support the new body of work.

  As a middle-ground approach, in the future, Central Staff will work to enhance our review of the fiscal note and Central Staff's fiscal policy team will provide a brief review of some fiscal notes and suggest enhancements when possible.

- Project long-term impacts: As legislation may take several years for the full impacts to be realized, and because some changes may be one-time versus ongoing in nature, the CBPP article suggest that fiscal notes should consider impacts beyond the current year. The City's template (see Attachment 2) includes a narrative space to reference future impacts. However, this may not be as impactful as including a multi-year table of impacts, which explicitly shows the estimated net impact in each year and allows for a display of any growth.

[3] McNichol, E. Lav, I., and Masterson, K. 2015, November 24. Better Cost Estimates, Better Budgets Improved Fiscal Notes Would Help States Make More Informed Decisions. The Center for Budget and Policy Priorities. https://www.cbpp.org/research/state-budget-and-tax/better-cost-estimates-better-budgets

As an example, Attachment 3, the form used in the Washington state legislative process, includes a table showing the impacts in the current year and five successive years. As shown in the tables, the bill's impacts are shown to grow in future years.

OPTION: Revise the summary and fiscal note form to include multiyear tables for operating, capital, and position impacts. *Note that the City Budget Office has expressed some concern that executive departments are not prepared to take a longer-term look at the financial impacts. If the Council provides directions to staff to incorporate this change, Central Staff will work with the City Budget Office to update guidance on drafting fiscal notes to assist departments.*

- <u>Revise estimates as needed</u>: Given that legislation may be amended in a manner that changes its fiscal impact, the CBPP best practice supports providing a modified fiscal note as needed during the process. Fiscal notes in Seattle's process may be modified to include the impacts of adopted amendments, though it is not a consistently applied standard.

  OPTION: Revise and reissue an as-amended fiscal note for <u>all</u> amended legislation where approved amendments impact the estimates. Though not related to the fiscal impacts, updating the bill summary section or other portions of the fiscal note unrelated to fiscal impacts, would also be useful to accurately summarize the final bill acted on by the City Council.

- <u>Post fiscal notes online</u>: Finally, the CBPP notes that posting fiscal notes online is a common practice at most states surveyed. Consistent with this standard, fiscal notes for all current Seattle legislation are available on the online posted agenda and accompany the legislation in internet search results.

While Seattle's process aligns with several of the standards, as noted above, there are areas where changes could better align with best practices. These are discussed in the Revised Summary and Fiscal Note Template section, below.

Other Observations

In addition to the best practices discussed above, there are recent examples that suggest steps could be taken to improve fiscal notes. These include:

- <u>Capital Improvement Project Reference</u>: The current template includes a table for the user to provide specific descriptive elements about any capital projects that are created, funded, or amended by the legislation. However, it does not make clear what Project Identification (Project I.D.) number should be used in this table. Given that the City's financial structure relies on both Master Project I.D.s, which are the large, public facing identifiers used in the six-year Capital Improvements Program that is adopted with the annual budget, and lower-level Detail Project I.D.s, which are used primarily by department financial managers, it may be useful to ensure that the Master Project I.D. is listed on the fiscal note template, for consistency with the public and Council-facing budget document.

  OPTION: Clarify that the details about a new, funded, or amended CIP should be at the 'Master Project I.D level.

- Aquarium Overlook project loan: In August of 2022, the City Council passed ORD 12653, which provided loan financing to the Seattle Aquarium Society (SEAS) to continue the work on the Aquarium Overlook project due to projected shortfalls. This loan was requested because, due to shortfalls in its fundraising, SEAS was unable to proceed with project work absent a cash infusion to the project. Originally added to the CIP in 2019, this project was subject to the enhanced public hearing and capital reporting requirements stipulated in RES 31203, discussed above. As required, a public hearing was held on October 23, 2018. However, it does not appear that the enhanced fiscal and risk analysis form, included as Attachment 1, was entered into the public record.

  Critical financial capacity questions excerpted from the Enhanced Fiscal and Risk Analysis form include the following:

  "Question 5. Financial Plan.

  Summarize the financial plan for the project, including:

  - *the financial responsibilities of the City and the Partner Entity,*
  - *the level of confidence in the financial information at this point in the project, the assumptions used for cost and revenue estimates, and*
  - *whether assumptions account for revenue variations due to factors such as concession revenues, competition, or the state of the future economy.*

  Also identify who developed the cost and revenue estimates and whether the estimates have been independently reviewed.

  Question 6. Risks if Partner Entity doesn't fulfill its funding responsibilities.

  Explain the risk that a Capital Commitment by the Partner Entity will not arrive at the time or in the amounts expected. If there is moderate to significant risk, show a lower level(s) of partner funding that might reasonably occur and how the project scope, timing, or other factors would be adjusted to address the shortfall. Would the City be expected to fill any resulting funding gap? Is City receipt of funds from the Partner Entity dependent on performance beyond our control? If so, what does the funder need to do to get the money?"

  These questions relate to the strength of the financial plan under varying economic assumptions and explicitly detail the risks if the private partner entity is unable to fulfill its funding responsibilities in a timely manner. While it is unknowable if having this additional information available in the fall of 2019 would have had any impact on avoiding the future emergency cash need addressed by ORD 12653 in the fall of 2022, it is possible that it may have led to a more resilient financial structure for the Aquarium Overlook project at its inception.

  OPTION: Add a question that prompts the user to complete and attach the 'Additional Risk Analysis and Fiscal Analysis for Non-Utility Partner Project' form if applicable for the legislation being proposed.

- Absorbed costs: In some cases, a fiscal note will indicate that, while the bill has an impact, those costs can be absorbed within the existing budget. Further, the amount of absorbed cost may or may not be explicitly stated in the fiscal note. From the perspective of the proposed legislation, an indication that there is no additional cost associated with a proposal is a positive indication. However, given that needs perennially outweigh resources, the identification of slack in the budget, which is implicit in a proposal wherein the budget is sized to support new work, would be useful to quantify, for at least two reasons. First, quantifying the absorbed costs would make transparent the resource choice at hand, and allow for alternative choices to be made about the resources, rather than conserving them solely within the context of the new proposal. Second, this would make explicit the assumptions about resources available for a new proposal and allow for alternative assumptions where applicable.

    OPTION: Require that all costs of legislation, whether they can be absorbed or otherwise, are clearly quantified in the fiscal note, and if not quantifiable, at least qualitatively describe the costs.

- Open ended versus binary questions: There are several areas of the existing template that provide for a 'yes/no' response, where allowing for qualitative explanation would provide more information. At times these questions are responded to with 'n/a', indicating that the question is not applicable to the subject legislation. Changes to the form would enhance opportunities to describe the nature of financial, inter-departmental, climate, and racial equity impacts, and are phrased in a manner that precludes an 'n/a' response. In other words, if a question is deemed not applicable, the way that determination was made should be explained in the fiscal note.

    OPTION: Revise binary questions to allow for responses that explain the impacts, or lack therefor, and preclude 'n/a' as a response.

- Other Implications: As described above, the existing template includes questions about climate emissions and resiliency impacts, as well as perceived implications for RSJI principles, but it does not specifically request copies of any studies or reports that may have informed the proposed legislation and the responses to those questions. Specifically, final environmental review documents (the Final Environmental Impact Statement (EIS) or Determination of Non-significant (DNS)) or a Racial Equity Toolkit (RET) are documents intended to provide input to decision-makers, but they are frequently not easily found, and internet links to these documents can be removed in the future. Attaching these types of documents to the fiscal note would be a useful addition to both the legislative process and the legislative record.

    OPTION: Add a question to the fiscal note that prompts the user to attach relevant studies or reports that may have informed the proposal and are meant to inform decision makers.

- Core Elements Not Memorialized: As noted previously, there is not a single codified source that provides clear guidance on what information to consider and include in the fiscal note. Rather, the fiscal notes currently produced in the Council's legislative process are developed according to standards delineated in a combination of prior legislation and administrative process determined by the Legislative and Executive branches.

  OPTION: Adopt by resolution or by ordinance policy that outlines the core components required for inclusion in all fiscal notes. Central Staff recommends that if this is codified, this guidance is developed in a way that retains the flexibility for the Legislative and Executive branches to work collaboratively as needed to update the template for the fiscal note administratively, provided that at minimum it requires that core components outlined in policy are included in any template revisions.

Next Steps

Following the Committee's discussion on July 19, and depending on the guidance the Committee provides to staff at that meeting, Central Staff will work with the City Budget Office to revise the fiscal note, and if requested, develop legislation to memorize the core components of a fiscal note. To provide adequate time to update written guidance and provide training to the many drafters of fiscal notes, Central Staff anticipates that any changes to the template would go into effect in 2024.

Attachments:

1. Additional Risk Analysis and Fiscal Analysis for Non-Utility Partner Projects
2. Summary & Fiscal Note Template
3. Example Washington state legislative fiscal note

cc: Esther Handy, Director
Aly Pennucci, Deputy Director

Attachment 1 to Exhibit A

ADDITIONAL RISK ANALYSIS AND FISCAL ANALYSIS FOR NON-UTILITY PARTNER PROJECTS

1. Project Identification. Describe the project identification process and how the project came to the City's attention (such as through a Request for Proposal, unsolicited proposal, or other means).

2. Need for Participation of a Partner Entity. Explain why the project is best accomplished jointly with the Partner Entity, instead of having the City (or its Partner Entity) pursue the project alone. Be sure to explain any cost implications (savings or increases) associated with the Partner Project compared to the City pursuing the project alone.

3. Selection of the Partner Entity. Describe the proposed Partner Entity. Explain the entity's internal management structure and how it plans to undertake its role in the project. Does the entity have experience with similar projects? Have those similar projects been successful (e.g. completed on time, met financial targets, etc.)? What is the City's previous experience working with the entity?

4. Public Benefits of the Partner Project. Name the specific benefits that the City and the public will receive in return for the City's participation in this project.

5. Financial Plan.
Summarize the financial plan for the project, including: - the financial responsibilities of the City and the Partner Entity, - the level of confidence in the financial information at this point in the project, the assumptions used for cost and revenue estimates, and - whether assumptions account for revenue variations due to factors such as concession revenues, competition, or the state of the future economy. Also identify who developed the cost and revenue estimates and whether the estimates have been independently reviewed.

6. Risks if Partner Entity doesn't fulfill its funding responsibilities.
Explain the risk that a Capital Commitment by the Partner Entity will not arrive at the time or in the amounts expected. If there is moderate to significant risk, show a lower level(s) of partner funding that might reasonably occur and how the project scope, timing, or other factors would be adjusted to address the shortfall. Would the City be expected to fill any resulting funding gap? Is City receipt of funds from the Partner Entity dependent on performance beyond our control? If so, what does the funder need to do to get the money?

7. Risks if Relationship with the Partner Entity is Dissolved. Explain how assets and liabilities will be distributed if and when the project ends or the relationship with the Partner Entity is dissolved. What are the risks if the project is left incomplete (such as public hazards, environmental risk, or non-functioning facility)?

8. Assurances The anticipated terms of the agreement that govern City and Partner Entity responsibilities for funding and completing the project? Explain how risks will be shared between the Partner Entity and the City and the safeguards to be incorporated into written assurances to protect City interests including: - responsibilities for managing revenues and expenditures; - the mechanism(s) to prevent/respond to cost overruns, schedule delays, and poor quality construction; - the City's recourse if the Partner Entity doesn't perform; and - the method for making payments by or to the City (paid only after completion, progress payments, payment to third party, payment pursuant to legal settlement or court action or property sale).

Attachment 2 – Summary and Fiscal Note Template

SUMMARY and FISCAL NOTE*

Department:	Dept. Contact:	CBO Contact:

** Note that the Summary and Fiscal Note describes the version of the bill or resolution as introduced; final legislation including amendments may not be fully described.*

1. BILL SUMMARY

Legislation Title:

Summary and Background of the Legislation:

2. CAPITAL IMPROVEMENT PROGRAM

Does this legislation create, fund, or amend a CIP Project? ___ Yes ___ No

If yes, please fill out the table below and attach a new (if creating a project) or marked-up (if amending) CIP Page to the Council Bill. Please include the spending plan as part of the attached CIP Page. If no, please delete the table.

Project Name:	Project I.D.:	Project Location:	Start Date:	End Date:	Total Project Cost Through 2028:

3. SUMMARY OF FINANCIAL IMPLICATIONS

Does this legislation amend the Adopted Budget? ___ Yes ___ No

If there are no changes to appropriations, revenues, or positions, please delete the table below.

	General Fund $		Other $	
Appropriation change ($):	2023	2024	2023	2024
	Revenue to General Fund		Revenue to Other Funds	
Estimated revenue change ($):	2023	2024	2023	2024
	No. of Positions		Total FTE Change	
Positions affected:	2023	2024	2023	2024

Does the legislation have other financial impacts to The City of Seattle that are not reflected in the above, including direct or indirect, short-term or long-term costs?

Are there financial costs or other impacts of *not* implementing the legislation?

Template last revised: December 13, 2022

Attachment 2 – Summary and Fiscal Note Template

If there are no changes to appropriations, revenues, or positions, please delete sections 3.a., 3.b., and 3.c. and answer the questions in Section 4.

3.a. Appropriations

___ This legislation adds, changes, or deletes appropriations.

Fund Name and Number	Dept	Budget Control Level Name/Number*	2023 Appropriation Change	2024 Estimated Appropriation Change
		TOTAL		

**See budget book to obtain the appropriate Budget Control Level for your department.*

Appropriations Notes:

3.b. Revenues/Reimbursements

___ This legislation adds, changes, or deletes revenues or reimbursements.

Anticipated Revenue/Reimbursement Resulting from This Legislation:

Fund Name and Number	Dept	Revenue Source	2023 Revenue	2024 Estimated Revenue
		TOTAL		

Revenue/Reimbursement Notes:

3.c. Positions

___ This legislation adds, changes, or deletes positions.

Total Regular Positions Created, Modified, or Abrogated through This Legislation, Including FTE Impact:

Position # for Existing Positions	Position Title & Department*	Fund Name & Number	Program & BCL	PT/FT	2023 Positions	2023 FTE	Does it sunset? (If yes, explain below in Position Notes)
			TOTAL				

** List each position separately.*

Position Notes:

4. OTHER IMPLICATIONS

a. Does this legislation affect any departments besides the originating department?

b. Is a public hearing required for this legislation?

c. Is publication of notice with *The Daily Journal of Commerce* and/or *The Seattle Times* required for this legislation?

d. Does this legislation affect a piece of property?

e. Please describe any perceived implication for the principles of the Race and Social Justice Initiative. Does this legislation impact vulnerable or historically disadvantaged communities? What is the Language Access plan for any communications to the public?

f. Climate Change Implications

1. Emissions: Is this legislation likely to increase or decrease carbon emissions in a material way?

2. Resiliency: Will the action(s) proposed by this legislation increase or decrease Seattle's resiliency (or ability to adapt) to climate change in a material way? If so, explain. If it is likely to decrease resiliency in a material way, describe what will or could be done to mitigate the effects.

g. If this legislation includes a new initiative or a major programmatic expansion: What are the specific long-term and measurable goal(s) of the program? How will this legislation help achieve the program's desired goal(s)?

Summary Attachments (if any):

Multiple Agency Fiscal Note Summary

Bill Number: 1201 HB	Title: Retirement system funding

Estimated Cash Receipts

NONE

Estimated Operating Expenditures

Agency Name	2023-25				2025-27				2027-29			
	FTEs	GF-State	NGF-Outlook	Total	FTEs	GF-State	NGF-Outlook	Total	FTEs	GF-State	NGF-Outlook	Total
Department of Retirement Systems	.0	0	0	0	.0	0	0	0	.0	0	0	0
Actuarial Fiscal Note - State Actuary	.0	(425,700,000)	(425,700,000)	(425,700,000)	.0	(371,600,000)	(371,600,000)	(683,000,000)	.0	(399,200,000)	(399,200,000)	(731,000,000)
Total $	**0.0**	**(425,700,000)**	**(425,700,000)**	**(425,700,000)**	**0.0**	**(371,600,000)**	**(371,600,000)**	**(683,000,000)**	**0.0**	**(399,200,000)**	**(399,200,000)**	**(731,000,000)**

Estimated Capital Budget Expenditures

Agency Name	2023-25			2025-27			2027-29		
	FTEs	Bonds	Total	FTEs	Bonds	Total	FTEs	Bonds	Total
Department of Retirement Systems	.0	0	0	.0	0	0	.0	0	0
Actuarial Fiscal Note - State Actuary	.0	0	0	.0	0	0	.0	0	0
Total $	**0.0**	**0**	**0**	**0.0**	**0**	**0**	**0.0**	**0**	**0**

Estimated Capital Budget Breakout

NONE

Prepared by: Marcus Ehrlander, OFM	Phone: (360) 489-4327	Date Published: Final

Individual State Agency Fiscal Note

Bill Number: 1201 HB	**Title:** Retirement system funding	**Agency:** 124-Department of Retiremen Systems

Part I: Estimates

[X] **No Fiscal Impact**

Estimated Cash Receipts to:

NONE

Estimated Operating Expenditures from:
NONE

Estimated Capital Budget Impact:

NONE

The cash receipts and expenditure estimates on this page represent the most likely fiscal impact. Factors impacting the precision of these estimates, and alternate ranges (if appropriate), are explained in Part II.

Check applicable boxes and follow corresponding instructions:

[ ] If fiscal impact is greater than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete entire fiscal note form Parts I-V.

[ ] If fiscal impact is less than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete this page only (Part I).

[ ] Capital budget impact, complete Part IV.

[ ] Requires new rule making, complete Part V.

Legislative Contact:	David Pringle	Phone: 360-786-7310	Date: 01/12/2023
Agency Preparation:	Mike Ricchio	Phone: 360-664-7227	Date: 01/17/2023
Agency Approval:	Mark Feldhausen	Phone: 360-664-7194	Date: 01/17/2023
OFM Review:	Marcus Ehrlander	Phone: (360) 489-4327	Date: 01/17/2023

Part II: Narrative Explanation

II. A - Brief Description Of What The Measure Does That Has Fiscal Impact

Significant provisions of the bill and any related workload or policy assumptions that have revenue or expenditure impact on the responding agency by section number.

This bill amends RCW 41.45.060 (Basic state and employer contribution rates—Methods used—Role of council—Role of state actuary) and 41.45.150 (Unfunded liabilities—Employer contribution rates) to “supersede” the portion of the employer contribution rate used to amortize the unfunded actuarial accrued liabilities (UAALs) in Plan 1 of the Public Employees' Retirement System (PERS) and Teachers' Retirement System (TRS). It also repeals Sec. 747 of the biennial operating budget, passed in the 2021 Session, that would have transferred $800,000,000 to TRS Plan 1 to apply to its UAAL.

These changes do not have a cost impact on the Department of Retirement Systems as implementing and communicating rate changes are normal processes for the agency.

II. B - Cash receipts Impact

Cash receipts impact of the legislation on the responding agency with the cash receipts provisions identified by section number and when appropriate, the detail of the revenue sources. Description of the factual basis of the assumptions and the method by which the cash receipts impact is derived. Explanation of how workload assumptions translate into estimates. Distinguished between one time and ongoing functions.

II. C - Expenditures

Agency expenditures necessary to implement this legislation (or savings resulting from this legislation), with the provisions of the legislation that result in the expenditures (or savings) identified by section number. Description of the factual basis of the assumptions and the method by which the expenditure impact is derived. Explanation of how workload assumptions translate into cost estimates. Distinguished between one time and ongoing functions.

Part III: Expenditure Detail

III. A - Operating Budget Expenditures

NONE

III. B - Expenditures by Object Or Purpose

NONE

III. C - Operating FTE Detail:

FTEs listed by classification and corresponding annual compensation. Totals agree with total FTEs in Part I and Part IIIA.

NONE

III. D - Expenditures By Program (optional)

NONE

Part IV: Capital Budget Impact

IV. A - Capital Budget Expenditures

NONE

IV. B - Expenditures by Object Or Purpose

NONE

IV. C - Capital Budget Breakout

Acquisition and construction costs not reflected elsewhere on the fiscal note and description of potential financing methods.

NONE

IV. D - Capital FTE Detail: *FTEs listed by classification and corresponding annual compensation. Totals agree with total FTEs in Part IVB.*

NONE

Part V: New Rule Making Required

Provisions of the bill that require the agency to adopt new administrative rules or repeal/revise existing rules.

Individual State Agency Fiscal Note

Bill Number: 1201 HB	**Title:** Retirement system funding	**Agency:** AFN-Actuarial Fiscal Note - State Actuary

Part I: Estimates

☐ **No Fiscal Impact**

Estimated Cash Receipts to:

NONE

Estimated Operating Expenditures from:

		FY 2024	FY 2025	2023-25	2025-27	2027-29
Account						
All Other Funds-State	000-1	0	0	0	(311,400,000)	(331,800,000)
General Fund-State	001-1	0	(425,700,000)	(425,700,000)	(371,600,000)	(399,200,000)
	Total $	0	(425,700,000)	(425,700,000)	(683,000,000)	(731,000,000)

Estimated Capital Budget Impact:

NONE

The cash receipts and expenditure estimates on this page represent the most likely fiscal impact. Factors impacting the precision of these estimates, and alternate ranges (if appropriate), are explained in Part II.

Check applicable boxes and follow corresponding instructions:

☒ If fiscal impact is greater than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete entire fiscal note form Parts I-V.

☐ If fiscal impact is less than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete this page only (Part I).

☐ Capital budget impact, complete Part IV.

☐ Requires new rule making, complete Part V.

Legislative Contact:	David Pringle	Phone: 360-786-7310	Date: 01/12/2023
Agency Preparation:	Aaron Gutierrez	Phone: 360-786-6152	Date: 01/18/2023
Agency Approval:	Kyle Stineman	Phone: 3607866153	Date: 01/18/2023
OFM Review:	Marcus Ehrlander	Phone: (360) 489-4327	Date: 01/18/2023

Part II: Narrative Explanation

II. A - Brief Description Of What The Measure Does That Has Fiscal Impact

Significant provisions of the bill and any related workload or policy assumptions that have revenue or expenditure impact on the responding agency by section number.

II. B - Cash receipts Impact

Cash receipts impact of the legislation on the responding agency with the cash receipts provisions identified by section number and when appropriate, the detail of the revenue sources. Description of the factual basis of the assumptions and the method by which the cash receipts impact is derived. Explanation of how workload assumptions translate into estimates. Distinguished between one time and ongoing functions.

II. C - Expenditures

Agency expenditures necessary to implement this legislation (or savings resulting from this legislation), with the provisions of the legislation that result in the expenditures (or savings) identified by section number. Description of the factual basis of the assumptions and the method by which the expenditure impact is derived. Explanation of how workload assumptions translate into cost estimates. Distinguished between one time and ongoing functions.

Part III: Expenditure Detail

III. A - Operating Budget Expenditures

Account	Account Title	Type	FY 2024	FY 2025	2023-25	2025-27	2027-29
000-1	All Other Funds	State	0	0	0	(311,400,000)	(331,800,000)
001-1	General Fund	State	0	(425,700,000)	(425,700,000)	(371,600,000)	(399,200,000)
		Total $	0	(425,700,000)	(425,700,000)	(683,000,000)	(731,000,000)

III. B - Expenditures by Object Or Purpose

	FY 2024	FY 2025	2023-25	2025-27	2027-29
FTE Staff Years					
A-Salaries and Wages					
B-Employee Benefits		(425,700,000)	(425,700,000)	(683,000,000)	(731,000,000)
C-Professional Service Contracts					
E-Goods and Other Services					
G-Travel					
J-Capital Outlays					
M-Inter Agency/Fund Transfers					
N-Grants, Benefits & Client Services					
P-Debt Service					
S-Interagency Reimbursements					
T-Intra-Agency Reimbursements					
9-					
Total $	0	(425,700,000)	(425,700,000)	(683,000,000)	(731,000,000)

III. C - Operating FTE Detail: *FTEs listed by classification and corresponding annual compensation. Totals agree with total FTEs in Part I and Part IIIA.*

NONE

III. D - Expenditures By Program (optional)

NONE

Part IV: Capital Budget Impact

IV. A - Capital Budget Expenditures

NONE

IV. B - Expenditures by Object Or Purpose

NONE

IV. C - Capital Budget Breakout

Acquisition and construction costs not reflected elsewhere on the fiscal note and description of potential financing methods.

NONE

IV. D - Capital FTE Detail:

FTEs listed by classification and corresponding annual compensation. Totals agree with total FTEs in Part IVB.

NONE

Part V: New Rule Making Required

Provisions of the bill that require the agency to adopt new administrative rules or repeal/revise existing rules.

SUMMARY OF RESULTS

BRIEF SUMMARY OF BILL: This bill changes the funding policy for the PERS and TRS Plans 1 Unfunded Actuarial Accrued Liability (UAAL).

COST SUMMARY

Change in Projected Plan 1 UAAL Rates						
	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029
PERS 1	0.00%	0.00%	(3.50%)	(3.50%)	(3.50%)	(3.50%)
TRS 1	0.00%	(5.75%)	0.00%	0.00%	0.00%	0.00%

Note: Actual results may vary from these projections.

Budget Impacts			
(Dollars in Millions)	2023-2025	2025-2027	2023-2029
General Fund-State	($425.7)	($371.6)	($1,196.5)
Local Government	($75.1)	($633.4)	($1,384.6)
Total Employer	**($500.8)**	**($1,316.4)**	**($3,224.2)**

Note: We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

The budget impacts within this fiscal note exclude the savings in FY 2023 of repealing the $800 million appropriation to TRS 1 UAAL. We assume the savings of that provision, if enacted, would be included as part of the supplemental budget bill. The impacts of this repeal, however, are included in this fiscal note for subsequent biennia.

HIGHLIGHTS OF ACTUARIAL ANALYSIS

- This bill results in an expected savings to the impacted retirement systems because it lowers annual UAAL contributions (from employers) below what is expected under current law.
- Based on our current law projections, we estimate $5.7 billion in total employer contributions to the PERS 1 and TRS 1 UAAL from FYs 2024 through 2029. We estimate this bill would lower those contributions by $3.2 billion.
- We estimate this bill would not impact the expected UAAL pay-off date of PERS 1 but would extend the expected pay-off date of TRS 1 by 3 years.
  - As of our June 30, 2021, AVR, PERS 1 and TRS 1 have a combined UAAL of $4.7 billion with a projected pay-off year of 2026 and 2023 for PERS 1 and TRS 1, respectively, under current law and rate-adoption practices.
- Lower contributions improve short-term budget affordability and increase the chance that the UAAL continues or reemerges in the future, but also decrease the chance PERS 1 and TRS 1 have funded statuses above 100 percent in the future.
- Higher than expected future returns would lower the expected savings of this bill. Lower than expected future returns may result in the continuation, or reemergence of the UAAL. Please see the section **HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE** for more information.

See the remainder of this fiscal note for additional details on the summary and highlights presented here.

WHAT IS THE PROPOSED CHANGE?

Summary of Bill

This bill impacts the following systems:

- ❖ Public Employees' Retirement System (PERS).
- ❖ Teachers' Retirement System (TRS).
- ❖ School Employees' Retirement System (SERS).
- ❖ Public Safety Employees' Retirement System (PSERS).

This bill changes PERS and TRS Plans 1 UAAL funding policy in three ways.

1. Revised Code of Washington (RCW) 41.45.060 is revised to state that the general policy of amortizing the UAAL over a rolling ten-year period can be superseded by any rates established in RCW 41.45.150. Current law states that the rolling ten-year amortization is subject to any minimum or maximum rates in RCW 41.45.150.
2. Ends current minimum rates and creates new prescribed rates. These new rates are separate from, and do not alter, any amounts required by RCW 41.45.070 to amortize Plans 1 benefit improvements effective after June 30, 2009. The new rates are as follows:

    a. For PERS and PSERS, the current minimum rate of 3.50 percent ends on June 30, 2025, and is replaced with a rate of 0.00 percent from July 1, 2025, to June 30, 2029, that supersedes rates established in RCW 41.45.060.

    b. For SERS, the current minimum rate of 3.50 percent ends on August 31, 2025, and is replaced with a rate of 0.00 percent from September 1, 2025, to August 31, 2029, that supersedes rates established in RCW 41.45.060.

    c. For TRS, the current minimum rate of 5.75 percent ends on August 31, 2024, and is replaced with a rate of 0.00 percent from September 1, 2024, to August 30, 2029, that supersedes rates established in RCW 41.45.060.

3. Repeals the one-time $800 million payment to TRS 1 UAAL set for June 30, 2023 (see 2021 Chapter 334 Section 747). This bill and House Bill 1141 both repeal this additional UAAL contribution.

This bill also modifies the Office of the State Actuary's (OSA) duties following an actuarial valuation. Instead of reviewing the appropriateness of the minimum rates, OSA shall review the appropriateness of establishing, removing, or adjusting minimum rates.

In this summary, we only include changes pertinent to our actuarial fiscal note. See the legislative bill report for a complete summary of the bill.

Effective Date: June 30, 2023.

What Is the Current Situation?

Under current law, PERS 1 and TRS 1 UAAL rates have two components:

- **Base UAAL Rates –** The UAAL, excluding the unfunded cost of any Plan 1 benefit improvements (see below) is amortized over a rolling ten-year period, as a level percentage of projected system payroll.
  - This calculation is subject to any minimum or maximum rates.
  - RCW 41.45.150 establishes minimum rates as follows:
    - 3.50 percent for PERS, PSERS, and SERS.
    - 5.75 percent for TRS.
- **Amortization of Past Benefit Improvements –** The expected cost of benefit improvements enacted after June 30, 2009, is amortized over a fixed ten-year period as a level percentage of projected system payroll. These rates are collected in addition to Base UAAL rates.

After completing each valuation, OSA is required to review the appropriateness of the minimum contribution rates.

In addition to contribution rates, a one-time payment of $800 million to the TRS 1 UAAL is set to occur on June 30, 2023. This one-time payment is over, and above, the standard UAAL rates collected over retirement system salaries.

Who Is Impacted and How?

This bill impacts all PERS, TRS, SERS, and PSERS employers through an expected decrease in PERS 1 and TRS 1 UAAL contribution rates. This bill will not affect member contribution rates or their benefits.

WHY THIS BILL HAS AN EXPECTED SAVINGS AND WHO RECEIVES IT

Why This Bill Has a Savings

This bill reduces the expected employer contributions to PERS and TRS Plans 1 UAAL.

Who Will Receive These Savings?

The expected savings that result from this bill will be realized by employers of PERS, TRS, SERS, and PSERS according to the standard funding method. PERS, SERS, and PSERS employers make PERS 1 UAAL payments, whereas TRS employers make TRS 1 UAAL payments. Any savings from the repeal of the scheduled $800 million appropriation to TRS 1 UAAL is expected to be realized by the General Fund-State (GF-S).

HOW WE VALUED THESE SAVINGS

We relied on our most recent projections model, [2021 Valuation Projections Model], to calculate the current law cost of the retirement systems. Our Projections Model is like the Actuarial Valuation Report (AVR) but includes additional assumptions and methodology for experience beyond the measurement date. For instance, we make assumptions for demographics of new entrants and how many new entrants annually join the retirement plans. This allows the Projections Model to estimate funding progress and contribution rates at future measurement dates which was necessary to determine the impacts of this bill.

We modeled the current law cost of the retirement systems consistent with data, assets, assumptions, and methods documented on our Projections webpage. To analyze the impact of this bill, we then adjusted the following assumptions and methods.

Assumptions We Made

This bill removes the PERS and TRS Plans 1 minimum rates in Fiscal Year (FY) 2025 and FY 2024, respectively. Our projections model does not assume any reinstitution of minimum rates resulting from an OSA review given that reinstating a minimum rate would require an additional change to law. Based on our understanding of the bill, we assume any PERS 1 or TRS 1 UAAL that continues, or reemerges, will be funded via rolling ten-year amortization rate beginning with the 2029-31 Biennium.

We assume any benefit improvements enacted, after June 30, 2009, will be separately funded over a fixed ten-year period and are not impacted under this bill.

How We Applied These Assumptions

Consistent with the bill, our projections model removed the $800 million TRS 1 UAAL payment that was assumed to occur on June 30, 2023. Additionally, our projection model applied lower Base UAAL contribution rates as outlined in the following tables.

Projected PERS 1 Base UAAL Rate		
FY	Current Law	Under Bill
2023	3.50%	3.50%
2024	3.50%	3.50%
2025	3.50%	3.50%
2026	3.50%	0.00%
2027	3.50%	0.00%
2028	3.50%	0.00%
2029	3.50%	0.00%
2030+	0.00%	0.00%

Projected TRS 1 Base UAAL Rate		
FY	Current Law	Under Bill
2023	5.75%	5.75%
2024	5.75%	5.75%
2025	5.75%	0.00%
2026	0.00%	0.00%
2027	0.00%	0.00%
2028	0.00%	0.00%
2029	0.00%	0.00%
2030+	0.00%	0.00%

The fiscal impact of this bill represents the change in projected contributions. To estimate the fiscal impact of this bill, we compared projected pension contributions under current law to the projected contributions we expect under this bill. For more detail, please see **Appendix A**.

ACTUARIAL RESULTS

How the Liabilities Changed

This bill does not change the present value of future benefits payable so there is no impact on the actuarial funding of the affected plans due to liability changes.

As of our most recent 2021 AVR, we estimate the PERS 1 UAAL is $2.9 billion and the TRS 1 UAAL is $1.8 billion. The UAAL amounts exclude the unfunded cost of any Plan 1 benefit improvements.

How the Assets Changed

This bill does not change asset values as measured in our most recent valuation (June 30, 2021); however, it does impact assets within our projections model at future measurement dates. This bill reduces the expected TRS 1 assets, within our projections model, by $800 million beginning on June 30, 2023. In addition, we modeled lower UAAL contributions relative to our expectations under current law.

The total amount of expected change in assets due to reduced UAAL contributions are summarized in the **How This Impacts Budgets and Employees** section. Please note that this table does not include any expected loss in investment earnings on the contributions that are not expected to be made under this bill.

How the Present Value of Future Salaries (PVFS) Changed

This bill does not change the PVFS, so there is no impact on the actuarial funding of the affected plans due to PVFS changes.

How Projected Contribution Rates Changed

Under current law, we expect the UAAL will be paid off at the end of FY 2026 for PERS and FY 2023 for TRS. Based on current law and rate-setting practices, the Base UAAL rates are expected to be collected until the end of FY 2029 for PERS and FY 2025 for TRS.

This bill prescribes new Base UAAL Rates and also repeals the June 30, 2023, appropriation to TRS 1. As a result, we expect the Plans 1 UAALs will be paid off at the end of FY 2026 for both PERS and TRS. As discussed in the **How We Applied These Assumptions** section, Base UAAL rates that exceed 0.00 percent are expected to continue until the end of FY 2025 for PERS and FY 2024 for TRS.

The table below summarizes the Total UAAL rates used to estimate budget impacts under this bill. Please see **Appendix B** for additional details including components of the Total UAAL Rates (Base UAAL and Benefit Improvement rates) as well as the funded status displayed on an annual basis.

Projected Total UAAL Rates for Each Fiscal Year*							
Fiscal Year	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**
PERS 1							
Current Law	3.85%	3.85%	3.85%	3.85%	3.85%	3.85%	3.75%
Under Bill	3.85%	3.85%	3.85%	0.35%	0.35%	0.35%	0.25%
Difference	**0.00%**	**0.00%**	**0.00%**	**(3.50%)**	**(3.50%)**	**(3.50%)**	**(3.50%)**
TRS 1							
Current Law	6.46%	6.46%	6.46%	0.71%	0.71%	0.71%	0.50%
Under Bill	6.46%	6.46%	0.71%	0.71%	0.71%	0.71%	0.50%
Difference	**0.00%**	**0.00%**	**(5.75%)**	**0.00%**	**0.00%**	**0.00%**	**0.00%**

**Total UAAL Rate = Base UAAL + Benefit Improvement Rate.*

Beyond FY 2029, we expect no difference in Total UAAL rates under current law and this bill. The above table relies on future experience matching our assumptions. Please see **HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE** section for information on the impact when experience differs from our assumptions.

How This Impacts Budgets and Employees

Budget Impacts					
(Dollars in Millions)	**PERS**	**TRS**	**SERS**	**PSERS**	**Total**
2023-2025					
General Fund	$0.0	($425.7)	$0.0	$0.0	($425.7)
Non-General Fund	0.0	0.0	0.0	0.0	0.0
Total State	**$0.0**	**($425.7)**	**$0.0**	**$0.0**	**($425.7)**
Local Government	0.0	(75.1)	0.0	0.0	(75.1)
Total Employer	**$0.0**	**($500.8)**	**$0.0**	**$0.0**	**($500.8)**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2025-2027					
General Fund	($204.1)	$0.0	($126.1)	($41.5)	($371.6)
Non-General Fund	(306.1)	0.0	0.0	(5.3)	(311.4)
Total State	**($510.2)**	**$0.0**	**($126.1)**	**($46.8)**	**($683.0)**
Local Government	(510.2)	0.0	(103.1)	(20.1)	(633.4)
Total Employer	**($1,020.3)**	**$0.0**	**($229.2)**	**($66.9)**	**($1,316.4)**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2023-2029					
General Fund	($421.2)	($425.7)	($261.2)	($88.4)	($1,196.5)
Non-General Fund	(631.8)	0.0	0.0	(11.4)	(643.2)
Total State	**($1,053.0)**	**($425.7)**	**($261.2)**	**($99.8)**	**($1,839.7)**
Local Government	(1,053.0)	(75.1)	(213.7)	(42.8)	(1,384.6)
Total Employer	**($2,105.9)**	**($500.8)**	**($474.9)**	**($142.6)**	**($3,224.2)**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**

Note: Totals may not agree due to rounding. We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

The budget impacts within this fiscal note exclude the savings in FY 2023 of repealing the $800 million appropriation to TRS 1 UAAL. We assume the savings of that provision, if enacted, would be included as part of the supplemental budget bill. If the savings from the repeal of the TRS 1 UAAL appropriation were included in the table above then the 2023-29 total GF-S and Total Employer savings is $1.9965 billion and $4.0242 billion, respectively.

The analysis of this bill does not consider any other proposed changes to the systems. The combined effect of several changes to the systems could exceed the sum of each proposed change considered individually.

Comments on Risk

Our office performs annual risk assessments to help us demonstrate and assess the effect of unexpected experience on pension plans. The risk assessment allows us to measure how affordability and funded status can change if investment experience, expected state revenue growth, and inflation do not match our long-term assumptions. Our annual risk assessment also considers past practices, for funding and benefit enhancements, and their impact on pension plan risk if those practices continue.

The following table displays our latest risk measurements as of June 30, 2021. The figures in this table were not reproduced for this bill but we may update this fiscal note prior to the end of the 2023 Legislative Session to reflect updated figures. For more information, please see our Risk Assessment, Commentary on Risk, and Glossary webpages.

Select Measures of Pension Risk as of June 30, 2021		
	FY 2022-41	FY 2042-71
Affordability Measures		
Chance of Pensions Double their Current Share of GF-S*	1%	2%
Chance of Pensions Half their Current Share of GF-S*	44%	42%
Solvency Measures		
Chance of PERS 1, TRS 1, in Pay-Go**	<1%	2%
Chance of Open Plan in Pay-Go**	<1%	1%
Chance of PERS 1, TRS 1, Total Funded Status Below 60%	5%	1%
Chance of Open Plans Total Funded Status Below 60%	20%	31%

**Pensions approximately 4.9% of current GF-S budget; does not include higher education.*
***When today's value of annual pay-go cost exceeds $50 million.*

We would expect this bill would improve short-term affordability of the plans but the impacts to long-term affordability could vary. The affordability of the plans is impacted in three ways under this bill:

1. Short-term affordability is improved with the repeal of the $800 million payment to the TRS 1 UAAL scheduled for June 30, 2023.

2. Short-term affordability is improved through FY 2029 when Base UAAL contribution rates are prescribed as 0.00 percent compared to higher Base UAAL rates (due to Plan 1 minimum rates) collected under current law.
3. Long-term affordability can either improve or worsen under this bill. Under this bill, Base UAAL payments for FY 2030 (and beyond) are funded via ten-year rolling amortization rate which results in lower (and more stable) rates that would be expected to be collected for a longer period of time relative to Base UAAL rates under current law. This bill would be considered more affordable when the UAAL is present in both current law and this bill.

   It's also possible that the UAAL is paid off earlier under current law due to the additional funding. This bill becomes less affordable in those years.

Changes to plan affordability will often produce a counteractive effect on solvency. For example, as affordability improves, the solvency risks of the plans worsen under this bill compared to current law. The solvency of the plans is impacted in two ways under this bill:

1. The Plans 1 are expected to have fewer future assets to pay required obligations and serve as a buffer to offset any adverse future experience.
2. In the absence of any minimum rate, any UAAL that continues, or reemerges, in the event of adverse experience, is not expected to be paid off using the ten-year rolling amortization rate. An example of the UAAL continuing in perpetuity under adverse experience can be found in the next section.

Additionally, this bill may impact the liquidity risks of the plans. Any changes made to the Plans 1 cash flows could impact the liquidity of the Commingled Trust Fund (CTF) and ultimately the investment earnings of the trust. If cash flows are reduced and depending on the size and timing of those reductions, liquidity issues for the CTF could arise and may require selling assets earlier than expected.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

The best estimate results can vary under a different set of assumptions. Under this bill, the PERS 1 and TRS 1 UAAL is expected to be paid off by the end of FY 2026 for both plans; however, the future asset returns can impact the funding levels of the plans and whether additional UAAL contributions are required.

To test how sensitive our best estimate results are to the return on assets assumption, we looked at what would happen under different assumed short-term and long-term return on assets experience. In these illustrations, we did not assume any reinstitution of minimum rates resulting from an OSA review given that reinstating a minimum rate would require an additional change to law.

Unless noted otherwise, each sensitivity or stress test was performed using data, assets, assumptions, and methods disclosed in the **How We Valued These Savings** section of this fiscal note.

Expected Short-term Return Stress Test

While we expect the CTF to earn 7.0 percent over the long-term, short-term volatility can impact the projected funded status and the resulting contribution rate requirements. Recently, the CTF experienced significantly higher-than-expected returns in FY 2021 (31.62 percent return for CTF) which can sometimes be followed by a period of lower-than-expected returns. For FY 2022, the total CTF return was approximately 0.2 percent. Given recent investment volatility, we calculated what future return on assets for FY 2023 would prevent the plans from reaching/maintaining an expected funded status of 100 percent (or higher) through FY 2029, if all other assumptions are realized. Under this stress test, we found a FY 2023 return of approximately 3.00 percent (or below) would result in a continuation of the UAAL for both plans. Any UAAL would be funded through the ten-year rolling amortization rate following FY 2029. Absent favorable experience afterwards, a ten-year rolling amortization rate may not result in the plans attaining 100 percent funding.

Long-term Return on Assets Assumption Sensitivity

In addition to a short-term stress test, we examined the overall impact if the return on assets were one percent higher (or lower) than assumed for all future years beginning in FY 2023.

A long-term return on assets assumption of 8 percent would result in improved funding levels, relative to our best estimate, as well as an earlier UAAL payoff date for both plans.

A long-term return on assets assumption of 6 percent is not expected to result in sufficient assets to cover pension obligations for either PERS or TRS Plans 1 under this bill. In this scenario, Base UAAL contributions would be expected to resume in the 2029-31 Biennium and continue for the life of the plan. Also, the funded status decreases annually because of consistent under performance of the assets.

We expect less savings under the 8 percent return scenario because the current law projection will have fewer expected years of Base UAAL payments if it experiences 8 percent returns annually. For the 6 percent return scenario, we expect no change in budget impact prior to FY 2029, relative to our best estimate, but an expected cost from this bill beginning in FY 2030. If the current law projection experiences 6 percent annually then the asset reserves would help to offset these lower-than-expected returns as discussed in the **Comments on Risk** section. Please see **Appendix C** for additional details including annual Base UAAL and funded status under this sensitivity.

Other Thoughts on Sensitivity of Results

While we tested the sensitivity of return on assets assumption, there are other factors that may influence the plan experience. For example, future longevity of plan members can play a significant role in the funding requirements of a plan.

Members living longer (or shorter) than expected would result in higher (or lower) pension obligations. Our projections model doesn't have the functionality to test demographic experience that differs from expectations, but our **Commentary on Risk** webpage (**Demographic Risks** section) provides examples of how mortality experience impacts AVR results.

The results of this fiscal note are also sensitive to the methods we currently apply when we calculate required UAAL rates under current law funding policy. A change in future methods could change the results of this fiscal note.

ACTUARY'S CERTIFICATION

The undersigned certifies that:

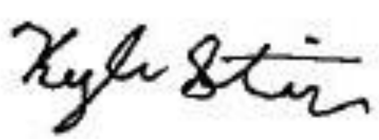
1. The actuarial assumptions, methods, and data used are reasonable for the purposes of this pricing exercise. The use of another set of assumptions, methods, and data may also be reasonable and might produce different results.
2. The risk analysis summarized in this Actuarial Fiscal Note (AFN) involves the interpretation of many factors and the application of professional judgment.
3. We prepared this AFN based on our current understanding of the bill as of the date shown in the footer. If the bill or our understanding of the bill changes, the results of a future AFN based on those changes may vary from this AFN. Additionally, the results of this AFN may change after our next annual update of the underlying actuarial measurements.
4. We prepared this AFN and provided opinions in accordance with Washington State law and accepted actuarial standards of practice as of the date shown in the footer of this AFN.

We prepared this AFN to support legislative deliberations during the 2023 Legislative Session. This AFN may not be appropriate for other purposes.

We advise readers of this AFN to seek professional guidance as to its content and interpretation, and not to rely on this communication without such guidance. Please read the analysis shown in this AFN as a whole. Distribution of, or reliance on, only parts of this AFN could result in its misuse and may mislead others.

The undersigned, with actuarial credentials, meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

While this AFN is meant to be complete, the undersigned is available to provide extra advice and explanations as needed.



Kyle Stineman, ASA, MAAA
Actuary

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APPENDIX A

How We Applied These Assumptions

We estimated the fiscal impact of this bill by comparing projected pension contributions under this bill to contributions under current law. The projected employer contributions reflect current member and future hire payroll.

To determine the projected contributions under current law, or the "base", we relied on projection system output. Projected pension contributions equal contributions rates from future AVRs multiplied by future payroll.

To determine the projected costs under this bill, we modified the base described above to reflect the provisions of the bill and assumptions noted above. We then multiplied the respective new contribution rates reflecting these changes by future payroll.

APPENDIX B

How the Projected Contribution Rates and Funded Status Changed

The following tables outline the expected contribution rates and funded status under current law and this bill.

PERS Plan 1 Projections							
Fiscal Year	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**
Current Law							
Base UAAL Rates*	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%
Benefit Improvement Rates	0.35%	0.35%	0.35%	0.35%	0.35%	0.35%	0.25%
Total UAAL Rates	**3.85%**	**3.85%**	**3.85%**	**3.85%**	**3.85%**	**3.85%**	**3.75%**
Funded Status of Base Benefits*	85%	91%	99%	108%	120%	133%	146%
Under Bill							
Base UAAL Rates*	3.50%	3.50%	3.50%	0.00%	0.00%	0.00%	0.00%
Benefit Improvement Rates	0.35%	0.35%	0.35%	0.35%	0.35%	0.35%	0.25%
Total UAAL Rates	**3.85%**	**3.85%**	**3.85%**	**0.35%**	**0.35%**	**0.35%**	**0.25%**
Funded Status of Base Benefits*	85%	91%	99%	101%	103%	105%	105%

**Excludes separately amortized benefit improvements. Funded status is measured as of June 30.*

TRS Plan 1 Projections							
Fiscal Year	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**
Current Law							
Base UAAL Rates*	5.75%	5.75%	5.75%	0.00%	0.00%	0.00%	0.00%
Benefit Improvement Rates	0.71%	0.71%	0.71%	0.71%	0.71%	0.71%	0.50%
Total UAAL Rates	**6.46%**	**6.46%**	**6.46%**	**0.71%**	**0.71%**	**0.71%**	**0.50%**
Funded Status of Base Benefits*	101%	111%	122%	126%	131%	137%	142%
Under Bill							
Base UAAL Rates*	5.75%	5.75%	0.00%	0.00%	0.00%	0.00%	0.00%
Benefit Improvement Rates	0.71%	0.71%	0.71%	0.71%	0.71%	0.71%	0.50%
Total UAAL Rates	**6.46%**	**6.46%**	**0.71%**	**0.71%**	**0.71%**	**0.71%**	**0.50%**
Funded Status of Base Benefits*	90%**	98%	99.8%	102%	104%	106%	107%

**Excludes separately amortized benefit improvements. Funded status is measured as of June 30.*
***Excludes the $800 million payment scheduled for 6/30/2023 which is repealed under this bill.*

Under current law and this bill, the funded status is expected to increase on an annual basis. This is primarily due to past investment performance. Consistent with the asset smoothing method, at each future measurement date, our projections model recognizes assets gains and losses that have been deferred from prior actual investment performances until those gains and losses are fully recognized. This is notable because of the FY 2021 CTF returns of 31.62 percent which significantly exceeded our expectations. The deferred asset gains from FY 2021 are steadily recognized but are not fully realized until the end of FY 2028. In addition, the funded status continues to increase because of expected returns on projected surplus assets.

APPENDIX C

How the Results Changes When the Assumptions Change

The tables below display how the best estimate Base UAAL calculation and Funded Status change when the return on assets is better (or worse) than our expectations.

PERS 1 Projections—Sensitivity of Return on Assets Assumption

	6% Return		7% Return		8% Return	
FY	Base UAAL Rate	Funded Status	Base UAAL Rate	Funded Status	Base UAAL Rate	Funded Status
2023	3.50%	84%	3.50%	85%	3.50%	86%
2024	3.50%	89%	3.50%	91%	3.50%	94%
2025	3.50%	95%	3.50%	99%	3.50%	103%
2026	0.00%	96%	0.00%	101%	0.00%	106%
2027	0.00%	96%	0.00%	103%	0.00%	110%
2028	0.00%	97%	0.00%	105%	0.00%	114%
2029	0.00%	96%	0.00%	105%	0.00%	116%
2030	0.21%	95%	0.00%	106%	0.00%	119%
...	...	...	...	...	...	...
2040	0.25%	80%	0.00%	126%	0.00%	>150%
...	...	...	...	...	...	...
2050	0.13%	<50%	0.00%	>150%	0.00%	>150%

Note: Figures exclude separately amortized benefit improvements. Funded status is measured as of June 30.

TRS 1 Projections—Sensitivity of Return on Assets Assumption

	6% Return		7% Return		8% Return	
FY	Base UAAL Rate	Funded Status	Base UAAL Rate	Funded Status	Base UAAL Rate	Funded Status
2023	5.75%	89%	5.75%	90%	5.75%	91%
2024	5.75%	96%	5.75%	98%	5.75%	101%
2025	0.00%	96%	0.00%	99.8%	0.00%	104%
2026	0.00%	96%	0.00%	102%	0.00%	107%
2027	0.00%	96%	0.00%	104%	0.00%	111%
2028	0.00%	98%	0.00%	106%	0.00%	115%
2029	0.00%	97%	0.00%	107%	0.00%	117%
2030	0.25%	96%	0.00%	107%	0.00%	121%
...	...	...	...	...	...	...
2040	0.36%	79%	0.00%	132%	0.00%	>150%
...	...	...	...	...	...	...
2050	0.18%	<50%	0.00%	>150%	0.00%	>150%

Note: Figures exclude separately amortized benefit improvements. Funded status is measured as of June 30.