Notes to the Financial Statements

For the Fiscal Year Ended June 30, 2012

Note 1: Summary of Significant Accounting Policies .... B - 40

Note 2: Accounting, Reporting and Entity Changes .... B - 50

Note 3: Deposits and Investments .... B - 51

Note 4: Receivables and Deferred/Unearned Revenues .... B - 71

Note 5: Interfund Balances and Transfers .... B - 74

Note 6: Capital Assets .... B - 78

Note 7: Long-Term Liabilities .... B - 82

Note 8: No Commitment Debt .... B - 92

Note 9: Governmental Fund Balances .... B - 93

Note 10: Deficit Net Assets .... B - 94

Note 11: Retirement Plans .... B - 95

Note 12: Other Postemployment Benefits .... B - 132

Note 13: Commitments and Contingencies .... B - 134

Note 14: Subsequent Events .... B - 137

Note 1
Summary of Significant Accounting Policies

The accompanying financial statements of the state of Washington have been prepared in conformity with generally accepted accounting principles (GAAP). The Office of Financial Management (OFM) is the primary authority for the state's accounting and reporting requirements. OFM has adopted the pronouncements of the Governmental Accounting Standards Board (GASB), which is the accepted standard-setting body for establishing governmental accounting and financial reporting principles nationally. For government-wide and enterprise fund reporting, the state follows only those private-sector standards issued on or before November 30, 1989, unless those pronouncements conflict with or contradict the pronouncements of the GASB. Following is a summary of the significant accounting policies:

A. REPORTING ENTITY

In defining the state of Washington for financial reporting purposes, management considers: all funds, organizations, institutions, agencies, departments, and offices that are legally part of the state (the primary government); organizations for which the state is financially accountable; and other organizations for which the nature and significance of their relationship with the state are such that exclusion would cause the state's financial statements to be misleading or incomplete.

Financial accountability exists when the primary government appoints a voting majority of an organization's governing body and is either able to impose its will on that organization or there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary government. The primary government may be financially accountable if an organization is fiscally dependent on the primary government regardless of whether the organization has a separately elected governing board, a governing board appointed by a higher level of government, or a jointly appointed board. An organization is fiscally dependent if it is unable to determine its budget without another government having the substantive authority to approve or modify that budget, to levy taxes or set rates or charges without substantive approval by another government, or to issue bonded debt without substantive approval by another government.

Based on these criteria, the following are included in the financial statements of the primary government:

State Agencies. Except as otherwise described herein, all state elected offices, departments, agencies, commissions, boards, committees, authorities, and councils (agencies) and all funds and subsidiary accounts of the state are included in the primary government. Executives of these agencies are either elected, directly appointed by the Governor, appointed by a board which is appointed by the Governor, or appointed by a board which is in part appointed by the Governor.

Additionally, a small number of board positions are established by statute or independently elected. The Legislature creates these agencies, assigns their programs, approves operational funding, and requires financial accountability. The Legislature also authorizes all bond issuances for capital construction projects for the benefit of state agencies. The legal liability for these bonds and the ownership of agency assets resides with the state.

Colleges and Universities. The governing boards of the five state universities, the state college, and the 34 state community and technical colleges are appointed by the Governor. Each college's governing board appoints a president to function as chief administrator. The Legislature approves budgets and budget amendments for the colleges' appropriated funds, which include the state's General Fund as well as certain capital projects funds. The State Treasurer issues general obligation debt for major campus construction projects. However, the colleges are authorized to issue revenue bonds.

The University of Washington issues general revenue bonds that are payable from general revenues, including student tuition and fees, grant indirect cost recovery, sales and services revenue, and investment income. The remainder of the college revenue bonds pledge the income derived from acquired or constructed assets such as housing, dining, and parking facilities. These revenue bonds are payable solely from, and secured by, fees and revenues derived from the operation of constructed facilities; the legal liability for the bonds and the ownership of the college assets reside with the state.

Colleges do not have separate corporate powers and sue and are sued as part of the state with legal representation provided through the state Attorney General's Office. Since the colleges are legally part of the state, their financial operations, including their blended component units, are reported in the primary government financial statements using the fund structure prescribed by GASB.

Retirement Systems. The state of Washington, through the Department of Retirement Systems, administers eight retirement systems for public employees of the state and political subdivisions: the Public Employees' Retirement System, the Teachers' Retirement System, the School Employees' Retirement System, the Law Enforcement Officers' and Fire Fighters' Retirement System, the Washington State Patrol Retirement System, the Public

Safety Employees' Retirement System, the Judicial Retirement System, and the Judges' Retirement Fund. The director of the Department of Retirement Systems is appointed by the Governor.

There are two additional retirement systems administered outside of the Department of Retirement Systems. The Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund is administered through the Board for Volunteer Fire Fighters, which is appointed by the Governor. The Judicial Retirement Account is administered through the Administrative Office of the Courts under the direction of the Board for Judicial Administration.

The Legislature establishes laws pertaining to the creation and administration of all public retirement systems. The participants of the public retirement systems, together with the state, provide funding for all costs of the systems based upon actuarial valuations. The state establishes benefit levels and approves the actuarial assumptions used in determining contribution levels.

All ten of the aforementioned retirement systems are included in the primary government's financial statements.

Blended Component Units. Blended component units, although legally separate entities, are part of the state's operations in substance. Accordingly, they are reported as part of the state and blended into the appropriate funds. The following entities are blended in the state's financial statements:

Tobacco Settlement Authority. The Tobacco Settlement Authority (TSA) was created by the Legislature in March 2002 as a public instrumentality separate and distinct from the state. It is governed by a five-member board appointed by the Governor. It was created solely for the purpose of issuing bonds to securitize a portion of the state's future tobacco settlement revenue. Proceeds of the debt instrument were transferred to the state to help fund health care, long-term care, and other programs of the state. Refer to Note 7.A for additional information.

Financial reports for the TSA may be obtained from the authority at the following address:

Tobacco Settlement Authority
1000 Second Avenue, Suite 2700
Seattle, WA 98104-1046

Other Blended Component Units. Tumwater Office Properties, FYI Properties, the University of Washington (UW) Physicians, UW Medicine Neighborhood Clinics, Twenty-Fifth Avenue Properties, TSB Properties, Washington Biomedical Research Properties I and II, and Washington Biomedical Research Facilities 3 are blended component units in the state's financial statements. All the aforementioned blended component units provide services entirely or almost entirely to the state. Financial information for these blended component units may be obtained from their respective administrative offices.

Discrete Component Units. Discretely presented component units are reported in a separate column in the government-wide financial statements. Discretely presented component units are legally separate from the state and primarily serve or benefit those outside of the state. They are financially accountable to the state, or have relationships with the state such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. These entities are reported as discrete component units because state officials either serve on or appoint the members of the governing bodies of the authorities. The state also has the ability to influence the operations of the authorities through legislation. The following entities are discretely presented in the financial statements of the state in the component unit's column:

The Washington State Housing Finance Commission, the Washington Higher Education Facilities Authority, the Washington Health Care Facilities Authority, and the Washington Economic Development Finance Authority (financing authorities) were created by the Legislature in a way that specifically prevents them from causing the state to be liable or responsible for their acts and obligations, including, but not limited to, any obligation to pay principal and interest on financing authority bonds. The financing authorities cannot obligate the state, either legally or morally, and the state has not assumed any obligation of, or with respect to, the financing authorities.

Financial reports of these financing authorities may be obtained from each authority at the following addresses:

Washington Health Care Facilities Authority
410 11th Avenue SE, Suite 201
PO Box 40935
Olympia, WA 98504-0935

Washington State Housing Finance Commission
Washington Higher Education Facilities Authority
Washington Economic Development Finance Authority
1000 Second Avenue, Suite 2700
Seattle, WA 98104-1046

The Washington State Public Stadium Authority (PSA) was created by the Legislature to acquire, construct, own, and operate a football/soccer stadium, exhibition center, and parking garage. Construction was completed in 2002. PSA capital assets, net of accumulated depreciation, total $342.0 million. The state issued general obligation bonds for a portion of the cost of the stadium construction. The total public share of the stadium and exhibition center cost did not exceed $300 million from all state and local government funding sources, as defined in statute.

Project costs in excess of $300 million were the responsibility of the project's private partner, First & Goal, Inc. The bonds are being repaid through new state lottery games, a state sales tax credit, extension of the local hotel/motel tax, and parking and admissions taxes at the new facility. Financial reports of the PSA may be obtained at the following address:

Washington State Public Stadium Authority
CenturyLink Field & Event Center
800 Occidental Avenue South, #700
Seattle, WA 98134

The state's component units each have a year-end of June 30 with the exception of the Washington Economic Development Finance Authority which has a December 31 year-end.

Joint Venture. In 1998, the University of Washington Medical Center (Medical Center) entered into an agreement with Seattle Children's Hospital and Fred Hutchinson Cancer Research Center to establish the Seattle Cancer Care Alliance (SCCA). Each member of the SCCA has a one-third interest. The mission of the SCCA is to eliminate cancer as a cause of human suffering and death and to become recognized as the premier cancer research and treatment center in the Pacific Northwest. The SCCA integrates the cancer research, teaching, and clinical cancer programs of all three institutions to provide state-of-the-art cancer care. Under the agreement, the Medical Center provides the patient care to all adult inpatients of the SCCA.

Inpatient Services – The SCCA operates a 20-bed unit located within the Medical Center in which its adult inpatients receive care. The fiscal intermediary has determined that the 20-bed unit qualifies as a hospital within a hospital for Medicare reimbursement purposes. The SCCA provides medical oversight and management of the inpatient unit. Under agreements, the Medical Center provides inpatient care services to the SCCA including necessary personnel, equipment, and ancillary services.

Outpatient Services – The SCCA operates an ambulatory cancer care service facility in Seattle. The Medical Center provides various services to the SCCA's outpatient facility including certain pharmacy, laboratory, and pathology services as well as billing, purchasing, and other administrative services.

The state accounts for the Medical Center's interest in SCCA under the equity method of accounting. Income of $7.2 million was recorded in fiscal year 2012, bringing the total equity investment to $82.3 million which is recognized in the state's financial statements in the Higher Education Student Services Fund.

Separate financial statements for SCCA may be obtained from:

Seattle Cancer Care Alliance
825 Eastlake Avenue East
PO Box 19023
Seattle, WA 98109-1023

B. GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

Government-wide Financial Statements

The state presents two basic government-wide financial statements: the Statement of Net Assets and the Statement of Activities. These government-wide financial statements report information on all non-fiduciary activities of the primary government and its component units. The financial information for the primary government is distinguished between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods and services.

Statement of Net Assets. The Statement of Net Assets presents the state's non-fiduciary assets and liabilities. As a general rule, balances between governmental and business-type activities are eliminated.

Assets and liabilities are presented in a net assets format in order of liquidity. Net assets are classified into three categories:

- Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances of bonds, notes and other debt that are attributed to the acquisition, construction, or improvement of those assets.

- Restricted net assets result when constraints are placed on net asset use either by external parties or by law through constitutional provision or enabling legislation.

- Unrestricted net assets consist of net assets that do not meet the definition of the two preceding categories.

Statement of Activities. The Statement of Activities reports the extent to which each major state program is supported by general state revenues or is self-financed through fees and intergovernmental aid. For governmental activities, a major program is defined as a function. For business-type activities, a major program is an identifiable activity.

Program revenues offset the direct expenses of major programs. Direct expenses are those that are clearly identifiable within a specific function or activity. Program revenues are identified using the following criteria:

- Charges to customers for goods and services of the program. A customer is one who directly benefits from the goods or services or is otherwise directly affected by the program, such as a state citizen or taxpayer, or other governments or nongovernmental entities.

- Amounts received from outside entities that are restricted to one or more specific programs. These amounts can be operating or capital in nature.

- Earnings on investments that are restricted to a specific program are also considered program revenues.

General revenues consist of taxes and other items not meeting the definition of program revenues.

Generally the effect of internal activities is eliminated. Exceptions to this rule include charges between the workers' compensation insurance programs and various other state programs and functions. Elimination of these charges would distort the direct costs and revenues reported for the various activities involved.

Fund Financial Statements

The state uses 678 accounts that are combined into 54 rollup funds. The state presents separate financial statements for governmental funds, proprietary funds, and fiduciary funds. Major individual governmental funds and major individual proprietary funds are reported in separate columns in the fund financial statements, with nonmajor funds being combined into a single column regardless of fund type. Internal service and fiduciary funds are reported by fund type. Major funds include:

Major Governmental Funds:

- **General Fund** is the state's primary operating fund. This fund accounts for all financial resources and transactions not accounted for in other funds.

- **Higher Education Special Revenue Fund** primarily accounts for tuition, student fees, and grants and contracts received for research and other educational purposes.

- **Higher Education Endowment Permanent Fund** accounts for gifts and bequests that the donors have specified must remain intact. Each gift is governed by various restrictions on the investment and use of the funds.

Major Enterprise Funds:

- **Workers' Compensation Fund** accounts for the workers' compensation program that provides medical, time-loss, and disability benefit payments to qualifying individuals sustaining work-related injuries.

- **Unemployment Compensation Fund** accounts for the unemployment compensation program. It accounts for the deposit of funds, requisitioned from the Federal Unemployment Trust Fund, to provide services to eligible participants within the state and to pay unemployment benefits.

- **Higher Education Student Services Fund** is used by colleges and universities principally for bookstore, cafeteria, parking, student housing, food service, and hospital business enterprise activities.

- **Guaranteed Education Tuition Program Fund** accounts for Washington's Guaranteed Education Tuition (GET) program. GET is a qualified tuition program under Section 529 of the Internal Revenue Code.

The state includes the following governmental and proprietary fund types within nonmajor funds:

Nonmajor Governmental Funds:

- **Special Revenue Funds** account for the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments, or for major capital projects) that are restricted or committed to expenditures for specific purposes. These include a variety of state programs including public safety and health assistance programs; natural resource and wildlife protection and management programs; the state's transportation programs which include the operation of the state's ferry system and maintenance and preservation of interstate and non-interstate highway systems; driver licensing, highway and non-highway operations, and capital improvements; K-12 school construction; and construction and loan programs for local public works projects.

- **Debt Service Funds** account for the accumulation of resources that are restricted or committed to expenditures for, and the payment of, principal and interest on the state's bonds issued in support of governmental activities.

- **Capital Projects Funds** account for financial resources that are restricted or committed to expenditures for the acquisition, construction, or improvement of major state-owned capital facilities (other than highway infrastructure or those financed by proprietary funds).

- **Common School Permanent Fund** accounts for the principal derived from the sale of timber. Interest earned is used for the benefit of common schools.

Nonmajor Proprietary Funds:

- **Enterprise Funds** account for the state's business type operations for which a fee is charged to external users for goods or services including: the state lottery; state liquor stores; vocational/education programs at correctional institutions, and other activities.

- **Internal Service Funds** account for the provision of legal, motor pool, data processing, risk management, health insurance, and other services by one department or agency to other departments or agencies of the state on a cost-reimbursement basis.

The state reports the following fiduciary funds:

- **Pension (and other employee benefit) Trust Funds** are used to report resources that are required to be held in trust by the state for the members and beneficiaries of defined benefit pension plans, defined contribution pension plans, and other employee benefit plans.

- **Investment Trust Fund** accounts for the external portion of the Local Government Investment Pool, which is reported by the state as the sponsoring government.

- **Private-Purpose Trust Fund** is used to report trust arrangements, other than pension and investment trusts, under which principal and income benefit individuals, private organizations, or other governments such as the administration of unclaimed property.

- **Agency Funds** account for resources held by the state in a custodial capacity for other governments, private organizations, or individuals.

Operating and Nonoperating Revenues and Expenses. The state's proprietary funds make a distinction between operating and nonoperating revenues and expenses. Operating revenues and expenses generally result from providing goods and services directly related to the principal operations of the funds. For example, operating revenues for the state's workers' compensation and health insurance funds consist of premiums and assessments collected. Operating expenses consist of claims paid to covered individuals, claims adjustment expenses, costs of commercial insurance coverage, and administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating, including interest expense and investment gains and losses.

C. MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

For government-wide reporting purposes, the state uses the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

For fund statement reporting purposes, the state uses the current financial resources measurement focus and modified accrual basis of accounting for governmental funds. With the current financial resources measurement focus, generally only current assets and current liabilities are included on the governmental funds balance sheet. Operating statements for these funds present inflows (i.e., revenues and other financing sources) and outflows (i.e., expenditures and other financing uses) of expendable financial resources.

Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they become both measurable and available). "Measurable" means the amount of the transaction can be reasonably estimated. "Available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Primary revenues that are determined to be susceptible to accrual include sales taxes, business and occupation taxes, motor fuel taxes, federal grants-in-aid, and charges for services.

Revenues from property taxes are determined to be available if collectible within 60 days. Taxes imposed on exchange transactions are accrued when the underlying exchange transaction occurs if collectible within one year. Revenue for timber cutting contracts is accrued when the timber is harvested. Revenues from licenses, permits, and fees are recognized when received in cash. Revenues related to expenditure-driven grant agreements are recognized when the qualifying expenditures are made, provided that the availability criteria is met. Expenditure-driven grant revenue is considered available if it can be collected by the state at the same time cash is disbursed to cover the associated grant expenditure. Pledges are accrued when the eligibility requirements are met and resources are available. All other accrued revenue sources are determined to be available if collectible within 12 months.

Property taxes are levied in December for the following calendar year. The first half-year collections are due by April 30, and the second half-year collections are due by October 31. Since the state is on a fiscal year ending June 30, the first half-year collections are recognized as revenue, if collectible within 60 days of the fiscal year end. The second half-year collections are recognized as receivables offset by deferred revenue. The lien date on property taxes is January 1 of the tax levy year.

Under modified accrual accounting, expenditures are generally recognized when the related liability is incurred. However, unmatured interest on general long-term obligations are recognized when due, and certain compensated absences, other postemployment benefits, and claims and judgments are recognized when the obligations are expected to be liquidated with available expendable financial resources.

The state reports both deferred and unearned revenues on its governmental fund balance. Deferred revenues arise when a potential revenue does not meet both the "measurable" and the "available" criteria for revenue recognition in the current period. Unearned revenues arise when resources are received by the state before it has a legal claim to them, such as when grant monies are received prior to incurring qualifying expenditures/expenses.

All proprietary and trust funds are accounted for using the economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operations of these funds are included on their respective statements of net assets. Operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in total net assets.

Net assets for trust funds are held in trust for external individuals and organizations.

All proprietary and trust funds are reported using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

D. ASSETS, LIABILITIES, AND NET ASSETS OR EQUITY

1. Cash and Investments

Investments of surplus or pooled cash balances are reported on the accompanying Statements of Net Assets, Balance Sheets and Statements of Cash Flows as "Cash and Pooled Investments." The Office of the State Treasurer invests state treasury cash surpluses where funds can be disbursed at any time without prior notice or penalty. For reporting purposes, pooled investments are stated at fair value or amortized cost, which approximates fair value. For purposes of reporting cash flows, the state considers cash and pooled investments to be cash equivalents. Pooled investments include short-term, highly-liquid investments that are both readily convertible to cash and are so near their maturity dates that they present insignificant risk of changes in value because of changes in interest rates.

The method of accounting for noncurrent investments varies depending upon the fund classification. Investments in the state's Local Government Investment Pool (LGIP), an external investment pool operated in a manner consistent with the Securities and Exchange Commission's Rule 2a-7 of the Investment Company Act of 1940, are reported at amortized cost. The Office of the State Treasurer prepares a stand-alone LGIP financial report. A copy of the report is available from the Office of the State Treasurer, PO Box 40200, Olympia, Washington 98504-0200, phone number (360) 902-9000 or TTY (360) 902-8963.

Certain pension trust fund investments, including real estate and private equity, are reported at fair value based on appraisals or estimates in the absence of readily ascertainable fair values. At June 30, 2012, these investments are valued at $25.51 billion. Because of the inherent uncertainties in the estimation of fair value, it is possible that the estimates will change.

All other noncurrent investments are reported at fair value. Fair values are based on published market prices, quotations from national security exchanges and security pricing services, or by the respective fund managers for securities that are not actively traded. Privately held mortgages are valued at cost, which approximates fair value. Additional disclosure describing investments is provided in Note 3.

2. Receivables and Payables

Receivables in the state's governmental fund type accounts consist primarily of taxes and federal revenues. Receivables in all other funds have arisen in the ordinary course of business. Receivables are recorded when either the asset or revenue recognition criteria (refer to Note 1.C) have been met. All receivables are reported net of an allowance for accounts estimated to be uncollectible.

For government-wide reporting purposes, amounts recorded as interfund/interagency receivables and payables are eliminated in the governmental and business-type activities columns on the Statement of Net Assets, except for the net residual balances due between the governmental and business-type activities, which are reported as internal balances. Amounts recorded in governmental and business-type activities as due to or from fiduciary funds have been reported as due to or from other governments.

Noncurrent receivables are recorded in the Workers' Compensation Fund representing estimated recoveries from third parties for a certain portion of claims expenses that are recorded as noncurrent claims payable. The accrued recoveries are computed using a variety of actuarial and statistical techniques and are discounted at assumed interest rates to arrive at the recorded value.

Disclosures related to the Workers' Compensation Fund activities and claims payable are provided in Note 1.E.1 and Note 7.E.

3. Inventories and Prepaids

Consumable inventories, consisting of expendable materials and supplies held for consumption, are valued and reported in the state's financial statements if the fiscal year-end balance on hand within an agency is estimated to be $25,000 or more. Consumable inventories are generally valued at cost using the first-in, first-out method. Donated consumable inventories are recorded at fair market value.

All merchandise inventories are considered reportable for financial statement purposes. Merchandise inventories are generally valued at cost using the first-in, first-out method.

Inventories of governmental funds are valued at cost and recorded using the consumption method. Proprietary funds expense inventories when used or sold.

For governmental fund financial reporting, inventory balances are also recorded as a reservation of fund balance indicating that they do not constitute "available spendable resources" except for $7.1 million in federally donated consumable inventories, which are offset by unearned revenues because they are not earned until they are distributed to clients.

Prepaid items are those certain types of supplies and/or services (not inventory) that are acquired or purchased during an accounting period but not used or consumed during that accounting period.

In governmental fund type accounts, prepaid items are generally accounted for using the purchases method. Under the purchases method, prepaid items are treated as expenditures when purchased and residual balances, if any, at year end are not accounted for as assets.

In proprietary and trust fund type accounts, prepaid items are accounted for using the consumption method. The portion of supplies or services consumed or used during a period is recorded as an expense. The balance that remains is reported as an asset until consumed or used.

4. Restricted Assets

Unspent proceeds of state bond issues and other debt financing programs are classified as restricted assets because their use is limited by applicable bond and other debt covenants. These are reflected on the balance sheets and statements of net assets.

5. Capital Assets

Capital assets are tangible and intangible assets held and used in state operations, which have a service life of more than one year and meet the state's capitalization policy.

It is the state's policy to capitalize:

- All land, including land use rights with indefinite lives acquired with the purchase of the underlying land, and ancillary costs;
- The state highway system operated by the Department of Transportation;
- Infrastructure, other than the state highway system, with a cost of $100,000 or more;
- Buildings, building improvements, improvements other than buildings, and leasehold improvements with a cost of $100,000 or more;
- Intangible assets, either purchased or internally developed, with a cost of $1,000,000 or more that are identifiable by meeting one of the following conditions:
    - The asset is capable of being separated or divided and sold, transferred, licensed, rented, exchanged; or
    - The asset arises from contractual or other legal rights, regardless of whether those rights are transferable or separable;
- All capital assets acquired with Certificates of Participation, a debt financing program administered by the Office of the State Treasurer; and
- All other capital assets with a unit cost (including ancillary costs) of $5,000 or greater, or collections with a total cost of $5,000 or greater except for assets held by the University of Washington (UW). The capitalization threshold for all other capital assets held by the UW is $2,000.

Assets acquired by capital leases are capitalized if the asset's fair market value meets the state's capitalization threshold described above.

Purchased capital assets are valued at cost where historical records are available and at estimated historical cost where no historical records exist. Capital asset costs include the purchase price plus those costs necessary to place the asset in its intended location and condition for use (ancillary costs). Normal maintenance and repair costs that do not materially add to the value or extend the life of the state's capital assets are not capitalized.

Donated capital assets are valued at their estimated fair market value on the date of donation, plus all appropriate ancillary costs. When the fair market value is not practically determinable due to lack of sufficient records, estimated cost is used. Where necessary, estimates of original cost and fair market value are derived by factoring price levels from the current period to the time of acquisition.

The value of assets constructed by agencies for their own use includes all direct construction costs and indirect costs that are related to the construction. In enterprise and trust funds, net interest costs (if material) incurred during the period of construction are capitalized.

State agencies are not required to capitalize art collections, library reserve collections, and museum and historical collections that are considered inexhaustible, in that their value does not diminish over time, if all of the following conditions are met:

- The collection is held for public exhibition, education, or research in furtherance of public service, rather than financial gain.

- The collection is protected, kept unencumbered, cared for, and preserved.

- The collection is subject to policy requirements that the proceeds from sales of collection items be used to acquire other items for the collection.

Depreciation/amortization is calculated using the straight-line method over the estimated useful lives of the assets. Generally, estimated useful lives are as follows:

Buildings & building components	5-50 years
Furnishings, equipment & collections	3-50 years
Other improvements	3-50 years
Intangibles	3-50 years
Infrastructure	20-50 years

The cost and related accumulated depreciation/ amortization of disposed capital assets are removed from the accounting records.

The state capitalizes the state highway system as a network but does not depreciate it since the system is being preserved approximately at or above a condition level established by the state. That condition level is documented and disclosed. Additionally, the highway system is managed using an asset management system that includes:

- Maintenance of an up-to-date inventory of system assets,
- Performance of condition assessments of the assets at least every three years with summarization of the results using a measurement scale, and

- Annual estimation of the amount to maintain and preserve the assets at the condition level established and disclosed.

All state highway system expenditures that preserve the useful life of the system are expensed in the period incurred. Additions and improvements that increase the capacity or efficiency of the system are capitalized. This approach of reporting condition instead of depreciating the highway system is called the modified approach.

For government-wide financial reporting purposes, capital assets of the state are reported as assets in the applicable governmental or business-type activities column on the Statement of Net Assets. Depreciation/amortization expense related to capital assets is reported in the Statement of Activities.

Capital assets and the related depreciation/amortization expense are also reported in the proprietary fund financial statements.

In governmental funds, capital assets are not capitalized in the accounts that acquire or construct them. Instead, capital acquisitions and construction are reflected as expenditures in the year assets are acquired or construction costs are incurred. No depreciation/amortization is reported.

6. Compensated Absences

State employees accrue vested vacation leave at a variable rate based on years of service. In general, accrued vacation leave cannot exceed 240 hours at the employee's anniversary date.

Employees accrue sick leave at the rate of one day per month without limitation on the amount that can be accumulated. Sick leave is not vested; i.e., the state does not pay employees for unused sick leave upon termination except upon employee death or retirement. At death or retirement, the state is liable for 25 percent of the employee's accumulated sick leave. In addition, the state has a sick leave buyout option in which, each January, employees who accumulate sick leave in excess of 480 hours may redeem sick leave earned but not taken during the previous year at the rate of one day's pay in exchange for each four days of sick leave.

It is the state's policy to liquidate unpaid compensated absences outstanding at June 30 with future resources rather than advance funding it with currently available expendable financial resources.

For government-wide reporting purposes, the state reports compensated absences obligations as liabilities in the applicable governmental or business-type activities columns on the Statement of Net Assets.

For fund statement reporting purposes, governmental funds recognize an expenditure for annual and sick leave when it is payable, i.e., upon employee's use, resignation, or retirement. Proprietary and trust funds recognize the expense and accrue a liability for annual leave and estimated sick leave buyout, including related payroll taxes and benefits as applicable, as the leave is earned.

7. Long-Term Liabilities

In the government-wide and proprietary fund financial statements, long-term obligations of the state are reported as liabilities on the Statement of Net Assets. Bonds payable are reported net of applicable original issuance premium or discount. When material, bond premiums, discounts, and issue costs are deferred and amortized over the life of the bonds.

For governmental fund financial reporting, the face (par) amount of debt issued is reported as other financing sources. Premiums and discounts on original debt issuance are also reported as other financing sources and uses, respectively. Issue costs are reported as debt service expenditures.

8. Fund Equity

In governmental fund type accounts, fund equity is called "fund balance." Fund balance is reported in the following classifications which reflect the extent to which the state is bound to honor constraints on the purposes for which the amounts can be spent: nonspendable, restricted, committed, assigned, and unassigned.

When resources meeting more than one of the classifications (excluding nonspendable) are comingled in an account, assuming that an expenditure meets the constraints of the classification, the assumed order of spending is restricted first, committed second, and finally assigned.

In proprietary funds, fund equity is called net assets. Net assets are comprised of three components: invested in capital assets, net of related debt; restricted; and unrestricted.

When both restricted and unrestricted resources are available for use, it is the state's policy to use restricted resources first and then use unrestricted resources as they are needed.

E. OTHER INFORMATION

1. Insurance Activities

Workers' Compensation. Title 51 RCW establishes the state of Washington's workers' compensation program. The statute requires all employers to secure coverage for job-related injuries and diseases with few exceptions, through the Workers' Compensation Fund or through self-insurance.

Direct private insurance is not authorized, although self-insurers are permitted to reinsure up to 80 percent of their obligations through private insurers.

The Workers' Compensation Fund, an enterprise fund, is used to account for the workers' compensation program which provides time-loss, medical, vocational, disability, and pension benefits to qualifying individuals sustaining work-related injuries or illnesses. The main benefit plans of the workers' compensation program are funded based on rates that will keep these plans solvent in accordance with recognized actuarial principles. The supplemental pension plan supports cost-of-living adjustments (COLA) granted for time-loss and disability payments; however, these are funded on a pay-as-you-go basis. By statute, the state is only allowed to collect enough revenue to fund the current COLA payments.

Premiums are based on individual employers' reported payroll hours and insurance rates based on each employer's risk classification(s) and past experience, except the Supplemental Pension Fund premiums are based on a flat rate per hours worked independent of risk class or past experience. In addition to its regular premium plan which is required for all employers, the Workers' Compensation Fund offers a voluntary retrospective premium rating plan under which premiums are subject to three annual adjustments based on group and individual employers' loss experience. Initial adjustments to the standard premiums are paid to or collected from the groups and individual employers approximately ten months after the end of each plan year.

The Department of Labor and Industries, as administrator of the workers' compensation program, establishes claims liabilities based on estimates of the ultimate cost of claims (including future claims adjustment expenses) that have already occurred. The length of time for which such costs must be estimated varies depending on the benefit involved. Because actual claims costs depend on such complex factors as inflation, changes in doctrines of legal liabilities, claims adjudication, and judgments, the process used in computing claims liabilities does not necessarily result in an exact amount.

Claims payable are recomputed quarterly using a variety of actuarial and statistical techniques. These techniques are used to produce current estimates that reflect recent settlements, claim frequency, expected inflation, and other economic, legal, and social factors. Adjustments to claims payable are charged or credited to claims expense in the periods in which they are made.

Risk Management. The state of Washington operates a self-insurance liability program pursuant to RCW 4.92.130. The state manages its tort claims as an insurance business activity rather than a general governmental activity. The state's policy is generally not to purchase commercial insurance for the risk of losses to which it is exposed. Instead, the state's management believes it is more economical to manage its risks internally and set aside assets for claims settlement in the Risk Management Fund, an internal service fund. A limited amount of commercial insurance is purchased for liabilities arising from the operations of the Washington State ferries, employee bonds, and to limit the exposure to catastrophic losses. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past ten fiscal years. Otherwise, the self-insurance liability program services all claims against the state for injuries and property damage to third parties. The majority of state funds and agencies participate in the self-insurance liability program in proportion to their anticipated exposure to liability losses.

Health Insurance. The state of Washington administers and provides medical, dental, basic life, and basic long-term disability insurance coverage for eligible state employees. In addition, the state offers coverage to K-12 school districts, educational service districts, tribal governments, political subdivisions, and employee organizations representing state civil service workers. The state establishes eligibility requirements and approves plan benefits of all participating health care organizations. Because the state and its employees are the predominant participants in the employee health insurance program, it is accounted for in the Employee Insurance Fund, an internal service fund.

The state's share of the cost of coverage for state employees is based on a per capita amount determined annually by the Legislature and allocated to state agencies.

The Health Care Authority, as administrator of the health care benefits program, collects this monthly "premium" from agencies for each active employee enrolled in the program. State employees self-pay for coverage beyond the state's contribution. Cost of coverage for non-state employees is paid by their respective employers. Most coverage is available on a self-paid basis to former employees and employees who are temporarily not in pay status.

Most coverage is also available on a self-paid basis to eligible retirees. In accordance with the provisions of GASB Statement No. 43, an agency fund, the Retiree Health Insurance Fund, is used to account for the retiree health insurance program. For additional information, refer to Note 12.

The state secures commercial insurance for certain coverage offered, but self-insures the risk of loss for the Uniform Medical Plan. The Uniform Medical Plan enrolled 63 percent of the eligible subscribers in fiscal year 2012. Claims are paid from premiums collected, and claims adjudication is contracted through a third-party administrator.

Considerations in calculating liabilities include frequency of claims, administrative costs, industry inflation trends, advances in medical technology, and other social and economic factors. Liabilities include an amount for claims incurred but not reported.

2. Postemployment Benefits

COBRA. In compliance with federal law, the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), the state offers health and dental benefits on a temporary basis to qualified beneficiaries whose benefit coverage would otherwise end because of a qualifying event such as loss of employment. COBRA coverage is available on a self-paid basis and is the same medical and dental coverage available to state employees.

Medical Expense Plan. As disclosed in Note 1.D, at the time of separation from state service due to retirement or death, the state offers a 25 percent buyout of an employee's accumulated sick leave. Individual state agencies may offer eligible employees a medical expense plan (MEP) that meets the requirements of the Internal Revenue Code. Agencies offering an MEP deposit the retiring employee's sick leave buyout in the MEP for reimbursement of medical expenses.

Retirement Benefits. Refer to Note 11 Retirement Plans and Note 12 Other Postemployment Benefits.

3. Interfund/Interagency Activities

The state engages in two major categories of interfund/interagency activity: reciprocal and nonreciprocal. Reciprocal interfund/interagency activity is the internal counterpart to exchange and exchange-like transactions and includes both interfund loans and services provided and used. Nonreciprocal activity is nonexchange in nature and includes both transfers and reimbursements.

4. Donor-restricted Endowments

The state of Washington reports endowments in higher education endowment permanent accounts. These accounts are established outside of the state treasury for use by the higher education institutions. There is no state law that governs endowment spending; rather, the policies of individual university and college boards govern the spending of net appreciation on investments.

Under the current spending policy, distributions to programs approximate an annual percentage rate of 4 percent of a five-year rolling average of the endowment's market valuation.

The net appreciation available for authorization for expenditure by governing boards totaled $266.4 million. This amount is reported as restricted for expendable endowment funds on the government-wide Statement of Net Assets.

Note 2

Accounting, Reporting, and Entity Changes

Reporting Changes. Effective for fiscal year 2012 reporting, the state adopted the following new standard issued by the Governmental Accounting Standards Board (GASB):

Statement No. 64 *Derivative Instruments: Application of Hedge Accounting Termination Provisions – an amendment of GASB Statement No. 53*. GASB Statement No. 64 clarifies the circumstances in which hedge accounting should continue when a swap counterparty, or a swap counterparty's credit support provider, is replaced. Existing state reporting and disclosure practices comply with the requirements of Statement No. 64.

Fund Reclassification. During fiscal year 2012, it was determined that one activity reported in the Other Activities Fund, which was a major enterprise fund in fiscal year 2011, would itself qualify as a major fund for fiscal year 2012. Accordingly, the Guaranteed Education Tuition Program Fund is removed from the Other Activities Fund and reported as a major fund with a beginning fund balance (deficit) of $(565.3) million and the Other Activities Fund is reported within Nonmajor Enterprise Funds with a beginning fund balance of $68.2 million.

It was also determined that two other activities being reported in Other Activities would be more appropriately reported as governmental activities, one in the General Fund and the other in the Multimodal Transportation Fund, a non-major governmental fund. Accordingly, beginning fund balances were restated by a reduction of $5.5 million in Other Activities, increase of $386 thousand in the General Fund, and an increase of $5.1 million in the Multimodal Transportation Fund to effect proper fund classification of the activities.

Prior Period Adjustments. The University of Washington recorded a prior period adjustment for a change in capitalization threshold. While the University's capitalization threshold has been at $2,000, for state reporting purposes they converted to the $5,000 level. For fiscal year 2012 reporting, the state adopted the $2,000 threshold for the University. As a result, the Higher Education Student Services Fund, a major enterprise fund, is reporting a beginning balance adjustment of $3.6 million and an increase of $1.3 million is reported in the Higher Education Revolving Fund, an internal service fund.

The UW also recorded a prior period adjustment to correct fund classification of the UW Educational Outreach and Genome Sciences activities to a special revenue fund. As a result of the reclassification, the beginning balance of the Higher Education Special Revenue Fund, a major governmental fund, increased by $3.0 million, the Higher Education Revolving Fund, an internal service fund, decreased by $2.3 million, and pooled cash in an agency fund decreased by $762 thousand.

The Department of Ecology recorded a period adjustment of $1.3 million in a Nonmajor Governmental Fund to record a receivable for monies held in trust for which the state is the beneficiary under a prior year court ordered pollution remediation settlement. The state also recognized the associated pollution remediation obligation.

The Legislature abolished the Spokane Intercollege Research and Technology Institute agency which reported in the Higher Education Student Services Fund and transferred residual balances to Innovate Washington, a new agency, which reports in the Higher Education Special Revenue Fund. As a result, the beginning fund balance of the Higher Education Student Services was reduced by $280 thousand and the Higher Education Special Revenue Fund was increased by $280 thousand.

The state recorded a prior period adjustment $54.5 million to report Other Postemployment Benefits liability in the Internal Service Funds. The liability was previously reported at the government-wide level, but not at the fund statement level.

Governmental Capital Assets and Long-term Obligations. The state's adoption of a $2,000 capitalization threshold for the University of Washington noted above also resulted in a $13.9 million prior period adjustment to governmental capital assets.

Fund equity at July 1, 2011, has been restated as follows (expressed in thousands):

	Fund equity (deficit) at June 30, 2011, as previously reported	Fund Reclassification	Prior Period Adjustment	Fund equity (deficit) as restated, July 1, 2011
Governmental Funds:				
General	$ 1,218,201	$ 386	$ -	$ 1,218,587
Higher Education Special Revenue	1,820,202	-	3,268	1,823,470
Higher Education Endowment	3,158,277	-	-	3,158,277
Nonmajor Governmental	4,354,388	5,094	1,296	4,360,778
Proprietary Funds:				
Enterprise Funds:				
Workers' Compensation	(9,860,511)	-	-	(9,860,511)
Unemployment Compensation	3,199,137	-	-	3,199,137
Higher Education Student Services	1,333,704	-	3,279	1,336,983
Guaranteed Education Tuition Program*	-	(565,274)	-	(565,274)
Other Activities**	(496,637)	496,637	-	-
Nonmajor Enterprise	79,247	63,157	-	142,404
Internal Service Funds	(39,519)	-	(55,396)	(94,915)
Fiduciary Funds:				
Private Purpose Trust	32,945	-	-	32,945
Local Government Investment Pool	8,863,128	-	-	8,863,128
Pension and Other Employee Benefit Plans	68,467,215	-	-	68,467,215
Component Units:				
Public Stadium	357,408	-	-	357,408
Nonmajor Component Units	96,704	-	-	96,704

* The Guaranteed Education Tuition Program Fund was reported In the Other Activities Fund, a major fund in fiscal year 2011, but is reported as a major proprietary fund in fiscal year 2012.

** The Other Activities Fund which was reported as a major proprietary fund in fiscal year 2011 became a nonmajor enterprise fund for reporting purposes in fiscal year 2012.

Note 3
Deposits and Investments

A. DEPOSITS

Custodial Credit Risk. Custodial credit risk is the risk associated with the failure of a depository financial institution. In the event of a depository financial institution's failure, it is the risk that the state would not be able to recover its deposits or collateralized securities that are in the possession of the outside parties.

The state minimizes custodial credit risk by restrictions set forth in state law. Statutes require state agencies to deposit funds in financial institutions that are physically located in Washington unless otherwise expressly permitted by statute and authorized by the Washington Public Deposit Protection Commission (PDPC). The PDPC, established under chapter 39.58 of the Revised Code of Washington (RCW), makes and enforces regulations and administers a collateral pool program to ensure public funds are protected if a financial institution becomes insolvent. Securities pledged are held by a trustee agent for the benefit of the collateral pool.

At June 30, 2012, $1.12 billion of the state's deposits with financial institutions were either insured or collateralized, with the remaining $17.7 million uninsured/ uncollateralized.

B. INVESTMENTS – PENSION AND OTHER EMPLOYEE BENEFIT TRUST FUNDS (PENSION TRUST FUNDS)

1. Summary of Investment Policies

Under RCW 43.33A.030, trusteeship of the pension trust funds is vested within the voting members of the Washington State Investment Board (WSIB). The Legislature has established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, chapter 42.52 RCW, as it makes its investment decisions and seeks to meet its investment objectives.

The pension trust funds consist of retirement contributions from employer and employee participants in the Washington State Retirement System and related earnings on those contributions. The Retirement System is administered by the Department of Retirement Systems. The WSIB has exclusive control of the investment of all money invested in the pension trust funds.

In accordance with RCW 43.33A.110, the WSIB manages the pension fund portfolio to achieve maximum return at a prudent level of risk. The WSIB establishes asset allocation targets that must be considered at all times when making investment decisions. The asset mix may deviate from the target. Deviations greater than predetermined acceptable levels require rebalancing back to the target. When an asset class exceeds its range, the goal of rebalancing is to meet the target allocation within consideration of the other remaining asset classes.

Eligible Investments. The WSIB is authorized by statute as having investment management responsibility for pension funds. The WSIB is authorized to invest as provided by statute (chapter 43.33A RCW) and WSIB policy in the following: U.S. treasury bills; discount notes; repurchase agreements; reverse repurchase agreements; banker's acceptances; commercial paper; guaranteed investment contracts; U.S. government and agency (government sponsored corporations eligible for collateral purposes at the Federal Reserve) securities; non-U.S. dollar bonds; investment grade corporate bonds; non-investment grade corporate bonds; publicly traded mortgage-backed securities; privately placed mortgages; private placements of corporate debt; U.S. and foreign common stock; U.S. preferred stock; convertible securities; private equity including but not limited to investment corporations, partnerships, and limited liability companies for venture capital, leveraged buy-outs, real estate, and other tangible assets, or other forms of private equity; asset-backed securities; and derivative securities including futures, options, options on futures, forward contracts, and swap transactions. There were no violations of these investment restrictions during fiscal year 2012.

Commingled Trust Fund. Pension trust funds are invested in the Commingled Trust Fund (CTF). The CTF is a diversified pool of investments used as an investment vehicle for 14 separate retirement plans and one supplemental insurance fund. These plans hold shares in the CTF, which represent a percentage ownership in the pool of investments. Plans are allowed to purchase or sell units in the CTF, based on the fair value of the underlying assets, on the first business day of each month.

In addition to share ownership in the CTF, each retirement plan holds short-term investments that are used to manage each plan's cash needs.

The CTF consists of the Public Employees' Retirement System (PERS) Plans 1 and 2/3; Teachers' Retirement System (TRS) Plans 1 and 2/3; School Employees' Retirement System (SERS) Plans 2/3; Law Enforcement Officers' and Fire Fighters' Retirement Plans 1 and 2; Washington State Patrol Retirement System Plans 1 and 2; Public Safety Employees' Retirement System Plan 2; Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund; and the Higher Education Supplemental Insurance Fund. PERS Plan 3, TRS Plan 3 and SERS Plan 3 are hybrid defined benefit/defined contribution plans. The participants of those plans have the option to direct their contributions to the CTF or invest their defined contributions in other external options not managed by the WSIB.

CTF Investment Policies and Restrictions. The CTF is comprised of public markets equities, fixed income securities, private equity investments, tangible assets, real estate, and an innovation portfolio. The CTF's performance objective is to exceed the return of two custom benchmarks, each consisting of public market indices weighted according to asset allocation targets.

The asset allocation for the CTF is formally reviewed at least every four years. The allocation policy will be reviewed more frequently if the WSIB believes there has been a fundamental change in the structure of the capital markets or in the underlying cash flow or liability structure of the pension trust funds.

When market values fall outside policy ranges, assets are rebalanced first by using normal cash flows and then through reallocations of assets across asset classes. In cases of a major rebalancing, the pension trust funds can utilize futures, forward contracts and options in order to maintain exposure within each asset class and reduce transaction costs. Major rebalancing can occur to bring asset classes within their target ranges or when the pension trust funds are transitioning managers.

To achieve the performance and diversification objectives of the pension trust funds, the public markets equity program seeks to achieve the highest return possible from active management consistent with prudent risk management and the desire for downside protection with passive management as the default; provide diversification to the pension trust funds overall investment program; maintain liquidity in public equity; and maintain transparency into all public equity strategies to the extent possible.

The public markets equity portion of the pension trust funds invests in publicly traded equities globally, including equity securities in the U.S., developed non-U.S. and emerging markets. The program has a global benchmark, currently the MSCI All Country World Investable Market Index. A mix of external managers approved by the WSIB is used to manage the program. Passive management delivers broad diversified equity market exposure at low costs and is used when active managers cannot be identified and monitored with existing resources. Passive management is also used when it is considered an appropriate alternative to active management, typically in more efficient markets. Active management is used when the pension trust funds can identify, access, and monitor successful managers in markets that are less efficient. Active management seeks to enhance the risk/return profile of the program.

The fixed income segment is managed to achieve the highest return possible consistent with the desire to control asset volatility; and emphasize high yield to maturity opportunities to add value through active management, provide diversification to the overall investment program, and to meet or exceed the return of the Barclays Capital Universal Bond Index, with volatility similar to or less than the index.

The fixed income portfolio limits exposure to any corporate issuer to 3 percent of the pension trust funds' fixed income portfolio's market value. The fixed income portfolio is constrained by policy from investing more than 1 percent of the portfolio's par holdings in any single issuer with a quality rating below investment grade (as defined by Barclays Capital Global Family of Fixed Income Indices). Total market value of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) shall not exceed 15 percent of the market value of the fixed income portfolio. The total market value of below investment grade mortgage-backed, asset-backed, and commercial mortgage-backed securities shall not exceed 5 percent of the market value of the fixed income portfolio. The duration of the portfolio (the sensitivity of the portfolio's fair value to changes in the level of interest rates) is targeted to be within 20 percent of the duration of the Barclays Capital Universal Index.

The major sector allocations of the fixed income portfolio are limited to the following ranges: U.S treasuries and government agencies – 10 percent to 45 percent, credit bonds – 10 percent to 60 percent, asset-backed securities – 0 percent to 10 percent, commercial mortgage-backed securities – 0 percent to 10 percent, and mortgage-backed securities – 5 percent to 45 percent.

Pension trust funds can be invested in any appropriate private equity investment opportunity that has the potential for returns superior to traditional investment opportunities and which is not prohibited by the WSIB's policies or by law. These investment types include venture capital investments, corporate finance, growth equity, special situations, distressed, mezzanine, and other investments. Private equity investments are made through limited partnership or direct investment vehicles.

The private equity investment portfolio is managed to meet or exceed the returns of the Russell 3000 (lagged by one quarter) plus 300 basis points. To meet the return and plan objectives, the private equity portfolio has diversified investments in companies in a variety of growth stages. The portfolio also includes a broad cross-section of opportunities in different industries and geographic regions.

The primary goal of the tangible asset portfolio is to generate a long-term, high quality, stable income stream. The secondary goal is to generate appreciation approximately commensurate with inflation. The structure of the investments are primarily targeted to those funds, separate accounts, or tangible asset operating companies providing the WSIB with the most robust governance provisions related to acquisition, dispositions, debt levels, and ongoing operational decisions for annual capital expenditures. The tangible asset portfolio invests in a number of sectors, but the primary focus is infrastructure, timber, and natural resource rights (oil and natural gas).

The WSIB's current return objective for tangible assets calls for a target benchmark of 4 percent above the U.S. Consumer Price Index over a long-term investment horizon defined as at least five years.

The WSIB's real estate program is an externally managed pool of selected partnership investments, intended to provide alternative portfolio characteristics when compared to traditional stock and bond investments. The majority of the WSIB's partnerships invest in institutional-quality real estate assets that are leased to third parties. The income generated from bond-like lease payments coupled with the hard asset qualities of commercial real estate combine to generate returns that are expected to fall between the return expectations for fixed income and equities over the long term. The real estate portfolio is managed to deliver risk-adjusted returns that are consistent with the WSIB's long-term return expectations for the asset class.

The WSIB's real estate partnerships typically invest in private real estate assets that are held for long-term income and appreciation. Many of the WSIB's investment partnerships do not involve co-investment with other financial entities, thereby providing the WSIB with control provisions, related transactions, and ongoing operational decisions for annual capital expenditures.

Volatility in the real estate portfolio is minimized through a combination of factors. First, the majority of the WSIB's partners own real estate assets in a private investment form which are not subject to public market volatility. Second, real estate capital is diversified among a host of partners with varying investment styles. Third, partnership assets are invested in numerous economic regions, including foreign markets, and in various property types. Finally, the WSIB's partners invest at different points within the properties' capital structure and life cycle.

The WSIB's real estate portfolio current benchmark seeks to earn an 8 percent annual investment return over a rolling 10-year period.

The innovation portfolio investment strategy is to provide the WSIB with the ability to invest in assets that fall outside of traditional asset classes and to provide the WSIB with comfort and demonstrated success before committing large dollar amounts to the strategy. The overall benchmark for the innovation portfolio is the weighted average of the underlying benchmark for each asset in the portfolio.

Currently, there are three investment strategies in the innovation portfolio, two involving private partnerships and one investing in public equities.

2. Unfunded Commitments

The WSIB has entered into a number of agreements that commit the pension trust funds, upon request, to make additional investment purchases up to predetermined amounts. As of June 30, 2012, the pension trust funds had unfunded commitments of $9.07 billion, $7.18 billion, $408.4 million, and $194.8 million in private equity, real estate, tangible assets, and the innovation portfolio, respectively.

3. Securities Lending

State law and Board policy permit the pension trust funds to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the WSIB in securities lending transactions. As JPMorgan is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

The pension trust funds report securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are reported as assets if the pension trust funds have the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities that the pension trust funds do not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

In anticipation of the custodian bank conversion on July 1, 2012, the pension trust funds recalled all securities on loan. There were no assets on loan at June 30, 2012, and no collateral held related to securities lending transactions.

Fixed income and equity securities were loaned during the fiscal year and collateralized by the pension trust funds' agent with cash, U.S. government securities (exclusive of mortgage-backed securities and letters of credit), and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities.

During fiscal year 2012, securities lending transactions could be terminated on demand by either the WSIB or the borrower. The weighted average maturity of loans for 2012 was 1.5 days.

Cash collateral was invested by the WSIB's agents in securities in the WSIB's separately managed short-term investment pool. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the WSIB by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During fiscal year 2012, there were no significant violations of legal or contractual provisions and no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the pension trust funds incurred no losses during fiscal year 2012 resulting from a default by either the borrowers or the securities lending agents.

4. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Increases in prevailing interest rates generally translate into decreases in fair values of those investments, and decreases in interest rates result in increases in valuations.

While the WSIB does not have a formal policy specifically for interest rate risk, the pension trust funds' fixed income investments are actively managed to meet or exceed the return of the Barclays Capital Universal Index, with a duration that is not 20 percent higher or lower than the duration of the index. As of June 30, 2012, the duration of the pension trust funds' fixed income investments was within the duration target of this index.

The schedule below provides information about the interest rate risks associated with the pension trust funds' investments as of June 30, 2012. The schedule displays various asset classes held by maturity in years and credit ratings. Residential mortgage-backed, commercial mortgage-backed, and asset-backed securities are reported using the average life within the portfolio. The average life is a calculated estimate of the average time (in years) until maturity for these securities taking into account possible prepayments of principal. All other securities on this schedule are reported using the stated maturity date. Certain foreign investments are recorded in U.S. dollars (USD), while others are recorded in non U.S. dollars (Non USD) but have been converted to U.S. dollars for reporting purposes.

Pension Trust Funds
Schedule of Maturities and Credit Quality
June 30, 2012
(expressed in thousands)

		Maturity				
Investment Type	**Fair Value**	**Less than 1 Year**	**1-5 Years**	**6-10 Years**	**More than 10 Years**	**Credit Rating**
Asset-backed securities	$ 20,133	$ -	$ 20,113	$ -	$ 20	Multiple
Residential mortgage-backed securities	1,828,200	407,760	1,420,379	61	-	Multiple
Commercial mortgage-backed securities	233,569	-	233,569	-	-	Multiple
Corporate bonds - domestic (USD)	980,534	-	195,683	615,398	169,453	Multiple
Corporate bonds - domestic (Non USD)	62,171	-	62,171	-	-	Multiple
Corporate bonds - foreign (USD)	3,881,367	15,936	659,954	2,576,569	628,908	Multiple
Corporate bonds - foreign (Non USD)	160,521	-	73,555	55,812	31,154	Multiple
U.S. government treasuries	3,282,516	300,743	2,175,807	805,966	-	Aaa
Foreign government and agencies (USD)	1,122,853	-	135,001	829,062	158,790	Multiple
Foreign government and agencies (Non USD)	619,043	-	154,596	285,694	178,753	Multiple
Supranational (Non USD)	379,992	7,563	271,937	100,492	-	Aaa
	12,570,899	$ 732,002	$ 5,402,765	$ 5,269,054	$ 1,167,078	
Corporate stock (USD)	2,917,446					
Corporate stock (Non USD)	9,557,040					
Commingled equity index funds	9,914,679					
Alternative investments	25,514,273					
Liquidity	1,500,573					
Total	$ 61,974,910					

Investments with multiple credit ratings are presented using the Moody's rating scale as follows:

Pension Trust Funds
Investments with Multiple Credit Ratings
June 30, 2012
(expressed in thousands)

	Investment Type									
Moody's Equivalent Credit Rating	**Asset-Backed Securities**	**Residential Mortgage-Backed Securities**	**Commercial Mortgage-Backed Securities**	**Corporate Bonds - Domestic (USD)**	**Corporate Bonds - Domestic (Non USD)**	**Corporate Bonds - Foreign (USD)**	**Corporate Bonds - Foreign (Non USD)**	**Foreign Government and Agencies (USD)**	**Foreign Government and Agencies (Non USD)**	**Total**
Aaa	$ 20,113	$ 1,810,713	$ 189,359	$ -	$ -	$ -	$ -	$ -	$ 169,112	$ 2,189,297
Aa1	20	-	-	-	-	-	-	18,408	22,019	40,447
Aa2	-	2,206	-	-	-	28,541	-	28,825	-	59,572
Aa3	-	-	44,210	57,490	-	16,480	-	63,094	-	181,274
A1	-	-	-	22,033	-	62,279	10,273	285,193	24,510	404,288
A2	-	15,281	-	189,906	21,902	65,031	31,154	24,133	42,494	389,901
A3	-	-	-	49,640	-	334,750	32,401	25,618	68,517	510,926
Baa1	-	-	-	207,127	-	513,425	21,220	49,459	25,858	817,089
Baa2	-	-	-	205,090	40,269	949,835	20,758	281,266	105,862	1,603,080
Baa3	-	-	-	66,946	-	1,072,689	44,715	285,937	105,146	1,575,433
Ba1 or lower	-	-	-	182,302	-	838,337	-	60,920	55,525	1,137,084
Total	$ 20,133	$ 1,828,200	$ 233,569	$ 980,534	$ 62,171	$ 3,881,367	$ 160,521	$ 1,122,853	$ 619,043	$ 8,908,391

5. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Rated debt investments of the pension trust funds as of June 30, 2012, were rated by Moody's and/or an equivalent national rating organization.

Concentration of Credit Risk. Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The WSIB policy states no corporate fixed income issue shall exceed 3 percent of cost at the time of purchase or 6 percent of fair value thereafter of the fund, and no high yield issues shall exceed 1 percent of cost or 2 percent of fair value of the fund. There was no concentration of credit risk exceeding these policy guidelines as of June 30, 2012.

Custodial Credit Risk. Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the pension trust funds would not be able to recover the value of investments that are in the possession of an outside party. The WSIB does not have a policy specifically for custodial credit risk. The WSIB mitigates custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the WSIB for the benefit of the pension trust funds, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

6. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The WSIB does not have a formal policy to limit foreign currency risk. The WSIB manages their exposure to fair value loss by requiring their international securities investment managers to maintain diversified portfolios by sector and by issuer to limit foreign currency and security risk.

The following schedule presents the exposure of pension fund investments to foreign currency risk. The schedule provides information on deposits and investments held in various foreign currencies. Private equity and real estate are presented according to the financial reporting currency of the individual funds. This is not a presentation of currency exposure relating to the underlying holdings. The schedule is stated in U.S. dollars.

Pension Trust Funds
Foreign Currency Exposure by Country
June 30, 2012
(expressed in thousands)

	Investment Type					
Foreign Currency Denomination	**Currency**	**Fixed Income**	**Common Stock**	**Private Equity**	**Real Estate**	**Total**
Australia-Dollar	$ 1,663	$ 387,973	$ 556,211	$ -	$ 24,674	$ 970,521
Brazil-Real	323	295,387	119,277	-	-	414,987
Canada-Dollar	4,241	-	742,340	-	-	746,581
Denmark-Krone	1,808	-	105,052	-	-	106,860
E.M.U.-Euro	21,940	-	2,314,191	2,112,225	168,632	4,616,988
Hong Kong-Dollar	2,602	-	388,007	-	-	390,609
India-Rupee	-	123,752	83,881	-	-	207,633
Indonesia-Rupiah	679	71,417	61,284	-	-	133,380
Japan-Yen	21,098	-	1,576,982	-	-	1,598,080
Malaysia-Ringgit	2,379	68,517	25,813	-	-	96,709
Mexico-Peso	218	57,012	41,567	-	-	98,797
Singapore-Dollar	1,576	-	141,508	-	-	143,084
South Korea-Won	1	-	151,774	-	-	151,775
Sweden-Krona	2,127	-	240,710	1,654	-	244,491
Switzerland-Franc	2,282	-	682,056	-	-	684,338
Turkey-Lira	-	62,982	40,291	-	-	103,273
United Kingdom-Pound	25,144	-	1,956,769	4,174	-	1,986,087
Other-Miscellaneous	3,431	154,687	329,327	-	-	487,445
Total	$ 91,512	$ 1,221,727	$ 9,557,040	$ 2,118,053	$ 193,306	$ 13,181,638

7. Derivatives

Pension trust funds are authorized to utilize various derivative financial instruments, including mortgage-backed securities, financial futures, forward contracts, interest rate swaps, credit default swaps, equity swaps, and options. Derivative transactions involve, to varying degrees, market and credit risk. In connection with the cash overlay program, at June 30, 2012, the pension trust funds held investments in financial futures, forward currency contracts, and other derivative securities that are recorded at fair value with changes in value recognized in investment income in the Statement of Changes in Net Assets in the period of change.

Derivatives are generally used to achieve the desired market exposure of a security, index or currency, adjust portfolio duration, or rebalance the total portfolio to the target asset allocation. Derivative contracts are instruments that derive their value from underlying assets, indices, reference interest rates, or a combination of these factors.

A derivative instrument could be a contract negotiated on behalf of the pension trust funds and a specific counterparty. This would typically be referred to as an "over the counter (OTC) contract" such as forward contracts and "to be announced (TBA) securities." Alternatively, a derivative instrument, such as futures, could be listed and traded on an exchange and referred to as "exchange traded."
Inherent in the use of OTC derivatives, the pension trust funds are exposed to counterparty credit risk on all open OTC positions. Counterparty credit risk is the risk that a derivative counterparty may fail to meet its payment obligation under the derivative contract. As of June 30, 2012, the pension trust funds counterparty risk was not deemed to be significant, whether evaluating counterparty exposure outright or netting collateral against net asset positions on contracts with each counterparty.

Mortgage TBAs are used to achieve the desired market exposure of a security or asset class or adjust portfolio duration. A TBA is a contract for the purchase or sale of agency mortgage-backed securities to be delivered at a future agreed-upon date. TBAs carry future settlement risk due to the possibility of not receiving the asset or associated gains specified in the contract. Such loss associated with failure by counterparties to deliver under the contracts was not deemed material at June 30, 2012.

Futures contracts are standardized, exchange-traded contracts to purchase or sell a specific financial instrument at a predetermined price. Gains and losses on futures contracts are settled daily based on a notional (underlying) principal value and do not involve an actual transfer of the specific instrument. The exchange assumes the risk that the counterparty will not pay and generally requires margin payments to minimize such risk. Futures are generally used to achieve the desired market exposure of a security or index or to rebalance the total portfolio.
Forward currency contracts are agreements to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. These forward commitments are not standardized and

carry credit risk due to the possible nonperformance by one of the counterparties. The maximum potential loss is the aggregate face value in U.S. dollars at the time the contract was opened; however, the likelihood of such loss is remote.

At June 30, 2012, the pension trust funds had outstanding forward currency contracts to purchase foreign currencies with a fair value of $1.03 billion and outstanding contracts to sell foreign currencies with a fair value of $1.03 billion. The net unrealized gain of $2.2 million is included in the Statement of Changes in Net Assets. The contracts have varying maturity dates ranging from July 2, 2012, to September 19, 2012.

At June 30, 2012, the pension trust funds' fixed income portfolio held derivative securities consisting of collateralized mortgage obligations with a fair value of $682.0 million. Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable.

Derivatives which are exchange traded are not subject to credit risk. The maximum loss that would be recognized at June 30, 2012, if all counterparties fail to perform as contracted is de minimus.

At June 30, 2012, the counterparties for forward currency contracts that are subject to credit risk had a credit rating of no less than A1 using the Moody's rating scale.

The following schedule presents the significant terms for derivatives held as investments by the WSIB:

Pension Trust Funds
Derivative Investments
June 30, 2012
(expressed in thousands)

	Changes in Fair Value - Included in Investment Income (Loss) Amount	Fair Value - Investment Derivative Amount	Notional
Futures Contracts:			
Bond index futures	$ 54,598	$ 1,840	$ 4,520
Equity index futures	(3,770)	3,725	1,049
Total	$ 50,828	$ 5,565	$ 5,569
To Be Announced (TBA) Securities:			
FHLMC TBA	$ 1,208	$ 47,713	$ 43,906
FNMA TBA	9,940	182,609	171,016
GNMA TBA	2,415	61,270	56,042
Total	$ 13,563	$ 291,592	$ 270,964
Forward Currency Contracts:			
Australia-Dollar	$ (9,147)	$ 40	$ 240,943
Brazil-Real	(282)	-	-
Canada-Dollar	(6,869)	554	127,606
Denmark-Krone	(572)	(14)	25,933
E.M.U.-Euro	(34,124)	(2,412)	246,525
Hong Kong-Dollar	1	-	222,301
Israel-Shekel	(1)	(1)	922
Japan-Yen	(1,822)	(10)	8,198,145
Mexico-Peso	(7)	(7)	6,500
New Zealand-Dollar	(467)	(169)	6,141
Norway-Krone	(2,957)	(11)	142,531
Singapore-Dollar	(713)	(3)	1,547
South Africa-Rand	175	177	56,459
Sweden-Krona	(3,565)	(188)	282,251
Switzerland-Franc	(8,396)	(1)	19,690
United Kingdom-Pound	(8,655)	(115)	74,865
United States-Dollar	74,798	-	1,023,077
Total	$ (2,603)	$ (2,160)	$ 10,675,436

8. Reverse Repurchase Agreements – None.

C. INVESTMENTS – WORKERS' COMPENSATION FUND

1. Summary of Investment Policies

Under RCW 43.33A.030, trusteeship of the Workers' Compensation Fund investments is vested in the voting members of the WSIB. The Legislature established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must comply with other state laws, such as the Ethics in Public Service Act, chapter 42.52 RCW, as it makes investment decisions and seeks to meet its investment objectives.

The Workers' Compensation Fund consist of contributions from employers and their employees participating in the state workers' compensation program and related earnings on those contributions. The workers' compensation program provides medical, time-loss, and disability benefit payments to qualifying individuals sustaining work-related injuries.

In accordance with state laws, the Workers' Compensation Fund investments are managed to limit fluctuations in the industrial insurance premiums and, subject to this purpose, achieve a maximum return at a prudent level of risk. Based on this requirement, the order of the objectives is:

- Maintain the solvency of the funds.
- Maintain premium rate stability.
- Ensure sufficient assets are available to fund the expected liability payments.
- Subject to the objectives above, achieve a maximum return at a prudent level of risk.

Eligible Investments. Eligible investments are securities and deposits that are in accordance with the WSIB's investment policy and chapter 43.33A RCW. Eligible investments include:

- U.S. equities.
- International equities.
- Treasury inflation protection securities (TIPS).
- U.S. treasuries and government agencies.
- Credit bonds.
- Mortgage-backed securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices.
- Asset-backed securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices.
- Commercial mortgage-backed securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices.
- Investment grade non-U.S. dollar bonds.

Investment Restrictions. To meet stated objectives, investments of the Workers' Compensation Fund are subject to the following constraints:

- All assets under the management of the WSIB are to be invested to maximize return at a prudent level of risk in accordance with RCW 43.33A.110 and RCW 43.33A.140.
- Asset allocations are to be reviewed every three to four years or sooner if there are significant changes in funding levels or the liability durations.
- Assets are to be rebalanced across asset classes when the fair value of the assets falls outside the policy ranges. The timing of any rebalancing will be based on market opportunities, cash flows, and the consideration of transaction costs; therefore, they need not occur immediately.
- Sector allocation for U.S. equities should be within a range of 55 percent to 65 percent. Allocation for international equities should be within a range of 35 percent to 45 percent.
- The benchmark and structure for U.S. equities will be the broad U.S. stock market as defined by the MSCI US IMI passive mandate. The benchmark and structure for international equities will be the Morgan Stanley Capital International All Country World Ex U.S. Investable Market Index. Both portfolios will be 100 percent passively managed in commingled index funds. The commingled funds may use futures for hedging or establishing a long position.
- TIPS will be managed to plus or minus 20 percent of the duration of the Barclays Capital U.S. TIPS Index.
- The structure of the fixed income portfolio varies depending upon the required duration target. No corporate fixed income issue cost shall exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fund's fair value at any time.

- Sector allocation of fixed income investments must be managed within the following prescribed ranges: U.S. treasuries and government agencies – 5 percent to 25 percent, credit bonds – 20 percent to 70 percent, asset-backed securities – 0 percent to 10 percent, commercial mortgage-backed securities – 0 percent to 10 percent and mortgage-backed securities – 0 percent to 25 percent. These targets are long-term in nature. Deviations may occur in the short term as a result of interim market conditions. However, if a range is exceeded the portfolios must be rebalanced to the target allocations as soon as it is practical.

- Total market value of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) shall not exceed 5 percent of the total market value of the funds. Although below investment grade mortgage-backed, asset-backed, and commercial mortgage-backed securities may not be purchased, portfolio holdings that are downgraded to those levels or are no longer rated may continue to be held.

- Total holdings of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) should not exceed 5 percent of total fixed income holdings.

2. Securities Lending

State law and Board policy permit the Workers' Compensation Fund to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with JPMorgan to act as agent for the Workers' Compensation Fund in securities lending transactions. As JPMorgan is the custodian bank for the Workers' Compensation Fund, it is counterparty to securities lending transactions.

The Workers' Compensation Fund reports securities lent (the underlying securities) as assets in the Statement of Net Assets. Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are reported as assets if the Workers' Compensation Fund has the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the Statement of Net Assets. Securities lending transactions collateralized by securities that the Workers' Compensation Fund does not have the ability to pledge or sell unless the borrower defaults are not reported as assets and liabilities.

In anticipation of the custodian bank conversion on July 1, 2012, the Workers' Compensation Fund recalled all securities on loan. There were no assets on loan at June 30, 2012, and no collateral held related to securities lending transactions.

During fiscal year 2012, fixed income securities were loaned and collateralized by the WSIB's agent with cash and U.S. government securities (exclusive of mortgage-backed securities and letters of credit) and irrevocable letters of credit. When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest, of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest, of the loaned securities. Securities lending transactions could be terminated on demand by either the Workers' Compensation Fund or the borrower. The weighted average maturity of loans was 1.5 days.

Cash collateral was invested by the Workers' Compensation Fund in the WSIB's short-term investment pool. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. Non-cash collateral could not be pledged or sold absent borrower default. There are no restrictions on the amount of securities that can be lent.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. JPMorgan indemnified the Workers' Compensation Fund by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. JPMorgan's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During fiscal year 2012, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the Workers' Compensation Fund incurred no losses during fiscal year 2012 resulting from a default by either the borrowers or the securities lending agents.

3. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. Increases in prevailing interest rates generally translate into decreases in fair values of those investments.

While the WSIB does not have a formal policy specifically for interest rate risk, the Workers' Compensation Fund fixed income portfolio is managed to set duration targets. The duration targets will be reviewed every three years, or sooner, if there are significant changes in the funding levels or the liability durations. As of June 30, 2012, the Workers' Compensation Fund portfolio durations were within the prescribed duration targets.

The schedule below provides information about the interest rate risks associated with the Workers' Compensation Fund investments as of June 30, 2012. The schedule displays various asset classes held by maturity in years and credit ratings. Residential mortgage-backed, commercial mortgage-backed, and asset-backed securities are reported using the average life within the portfolio. The average life is a calculated estimate of the average time (in years) until maturity for these securities taking into account possible prepayments of principal. All other securities on the schedule are reported using the stated maturity date.

Workers' Compensation Fund
Schedule of Maturities and Credit Quality
June 30, 2012
(expressed in thousands)

		Maturity				
Investment Type	**Fair Value**	**Less than 1 Year**	**1-5 Years**	**6-10 Years**	**More than 10 Years**	**Credit Rating**
Residential mortgage-backed securities	$ 1,743,809	$ 25,143	$ 1,004,023	$ 667,980	$ 46,663	Aaa
Commercial mortgage-backed securities	429,228	30,322	377,786	21,120	-	Multiple
Corporate bonds-domestic	3,191,256	203,994	534,684	1,021,460	1,431,118	Multiple
Corporate bonds-foreign (USD)	2,463,565	267,206	439,806	814,804	941,749	Multiple
Foreign government and agencies (USD)	941,850	44,791	396,713	303,048	197,298	Multiple
Supranational (USD)	184,781	45,792	138,989	-	-	Aaa
U.S. government treasuries	777,685	145,357	599,355	32,973	-	Aaa
U.S. treasury inflation protected securities	1,889,532	-	597,280	618,101	674,151	Aaa
	11,621,706	$ 762,605	$ 4,088,636	$ 3,479,486	$ 3,290,979	
Commingled index funds-domestic	951,396					
Commingled index funds-foreign	628,820					
Money market funds	119,900					
Total	$ 13,321,822					

USD: Reported in U.S. dollars

Investments with multiple credit ratings are presented using the Moody's rating scale as follows:

Workers' Compensation Fund
Investments with Multiple Credit Ratings
June 30, 2012
(expressed in thousands)

	Investment Type				
Moody's Equivalent Credit Rating	**Commercial Mortgage-Backed Securities**	**Corporate Bonds - Domestic**	**Corporate Bonds- Foreign (USD)**	**Foreign Government and Agencies (USD)**	**Total**
Aaa	$ 332,934	$ 6,101	$ -	$ 166,303	$ 505,338
Aa2	-	-	-	53,237	53,237
Aa3	96,294	226,940	224,345	139,208	686,787
A1	-	178,665	225,957	248,947	653,569
A2	-	762,672	35,017	-	797,689
A3	-	481,087	313,892	-	794,979
Baa1	-	558,674	425,599	27,297	1,011,570
Baa2	-	770,301	636,284	146,050	1,552,635
Baa3	-	123,108	443,673	83,253	650,034
Ba1 or lower	-	83,708	158,798	77,555	320,061
Total	$ 429,228	$ 3,191,256	$ 2,463,565	$ 941,850	$ 7,025,899

4. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The rated debt investments of the Workers' Compensation Fund as of June 30, 2012, were rated by Moody's and/or an equivalent national rating organization.

Concentration of Credit Risk. Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The Workers' Compensation Fund policy states corporate fixed income issue's cost shall not exceed 3 percent of the fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the fund's fair value at any time. There was no concentration of credit risk as of June 30, 2012.

Custodial Credit Risk. Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the Workers' Compensation Fund would not be able to recover the value of investments that are in the possession of an outside party. The Workers' Compensation Fund does not have a policy specifically for custodial credit risk. The WSIB mitigates custodial credit risk by having its investment securities held by its custodian. Also, investment securities are registered in the name of the WSIB for the benefit of the Workers' Compensation Fund, excluding cash and cash equivalents and repurchase agreements held as securities lending collateral.

5. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The Workers' Compensation Fund does not have a formal policy to limit foreign currency risk. At June 30, 2012, the Workers' Compensation Fund had $628.8 million invested in an international commingled equity index fund.

6. Derivatives

The Workers' Compensation Fund is authorized to utilize various derivative financial instruments, including mortgage-backed securities, financial futures, forward contracts, interest rate and equity swaps, and options to manage its exposure to fluctuations in interest and currency rates while increasing portfolio returns. Derivative transactions involve, to varying degrees, market and credit risk. The Workers' Compensation Fund mitigates market risks arising from derivative transactions by requiring collateral in cash and investments to be maintained equal to the securities positions outstanding, and thereby prohibiting the use of leverage or speculation. Credit risks arising from derivative transactions are mitigated by selecting and monitoring creditworthy counterparties and collateral issuers.

Consistent with the Workers' Compensation Fund's authority to invest in derivatives, international active equity managers may make limited investments in financial futures, forward contracts or other derivative securities to manage exposure to currency rate risk and equitize excess cash holdings. No such derivative securities were held as of June 30, 2012.

Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable.

At June 30, 2012, the only derivative securities held directly by the Workers' Compensation Fund were collateralized mortgage obligations of $1.74 billion.

7. Reverse Repurchase Agreements – None.

D. INVESTMENTS – LOCAL GOVERNMENT INVESTMENT POOL

1. Summary of Investment Policies

The Local Government Investment Pool (LGIP) is managed and operated by the Office of the State Treasurer (OST). The State Finance Committee is the administrator of the statute that created the pool and adopts appropriate rules. The OST is responsible for establishing the investment policy for the pool and reviews the policy annually. Any proposed changes are reviewed by the LGIP Advisory Committee. The terms of the policy are designed to ensure the safety and liquidity of the funds deposited in the LGIP.

The state treasurer and designated investment officers shall adhere to all restrictions on the investment of funds established by law and by policy.

The LGIP portfolio is invested in a manner generally consistent with a Rule 2a-7 money market fund recognized by the Securities and Exchange Commission (17CFR.270.2a-7). Rule 2a-7 funds are limited to high quality obligations with limited maximum and average maturities, the effect of which is to minimize both market and credit risk. As such, investments are reported at amortized cost (which approximates fair value).

Investment Objectives. The objectives of the LGIP investment policy, in priority order, are safety, liquidity, and return on investment.

Safety of principal is the primary objective. Investments shall be undertaken in a manner that seeks to ensure preservation of capital in the overall portfolio.

The investment portfolio will remain liquid to enable the state treasurer to meet all cash requirements that might reasonably be anticipated.

The LGIP will be structured with the objective of attaining a market rate of return throughout budgetary and economic cycles, commensurate with the investment risk parameters and the cash flow characteristics of the pool.

The primary objective of safety will be measured in cash as opposed to accounting terms, where different, and in terms of the portfolio as a whole as opposed to the terms of any individual transaction. This means, for example, that a single transaction that generated an accounting loss but actually increased the amount of cash received in the portfolio would be considered to have increased capital, and not decreased it.

Eligible Investments. Eligible investments are only those securities and deposits authorized by statute (chapters 39.58, 39.59, 43.84.080, and 43.250 RCW). Eligible investments include:

- Obligations of the U.S. government.

- Obligations of U.S. government agencies or of corporations wholly owned by the U.S. government.

- Obligations of government-sponsored corporations that are or may become eligible as collateral for advances to member banks as determined by the board of governors of the Federal Reserve.

- Banker's acceptances purchased on the secondary market rated with the highest short-term credit rating of any two Nationally Recognized Statistical Rating Organizations (NRSROs) at the time of purchase. If the banker's acceptance is rated by more than two NRSROs, it must have the highest rating from all of the organizations.

- Commercial paper provided that the OST adheres with policies and procedures of the State Investment Board regarding commercial paper (RCW 43.84.080(7)).

- Certificates of deposit or demand deposits with financial institutions qualified by the Washington Public Deposit Protection Commission.

- Obligations of the state of Washington or its political subdivisions.

Investment Restrictions. To provide for the safety and liquidity of LGIP funds, the investment portfolio will be subject to the following restrictions:

- Investments are restricted to fixed rate securities that mature in 397 days or less, floating and variable rate securities that mature in 762 days or less, and securities utilized in repurchase agreements.

- The weighted average maturity of the portfolio will not exceed 60 days.

- The weighted average life of the portfolio will not exceed 120 days.

- The purchase of investments in securities other than those issued by the U.S. government or its agencies will be limited.

- Cash generated through securities lending or reverse repurchase agreement transactions will not increase the dollar amount of specified investment types beyond stated limits.

2. Securities Lending

State statutes permit the LGIP to lend its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The LGIP, which has contracted with a lending agent to lend securities in the LGIP, earns a fee for this activity. The lending agent lends securities and receives collateral, which can be in the form of cash or other securities. The collateral, unless it is cash received from the lending of non coupon-bearing securities, must be valued at 102 percent of the fair value of the loaned securities, is priced daily and, if necessary, action is taken to maintain the collateralization level at 102 percent. Cash collateral received from the lending of non coupon-bearing securities shall not be valued at less than 102 percent of market value, not to exceed par.

The cash is invested by the lending agent in accordance with investment guidelines approved by the LGIP. The securities held as collateral and the securities underlying the cash collateral are held by the LGIP's custodian. One option available to the lending agent is to invest cash collateral with the LGIP. On June 30, 2012, there was $441.0 million invested with the LGIP by the lending agent. The average life of both the loans and the investment of cash received as collateral was one day.

The LGIP investment policy requires that any securities on loan be made available by the lending agent for next day liquidity at the option of the LGIP. During fiscal year 2012, the LGIP had no credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts the borrowers owed the LGIP. Furthermore, the contract requires the lending agent to indemnify the LGIP if the borrowers fail to return the securities (and if collateral is inadequate to replace the securities lent) or if the borrower fails to pay the LGIP for income distribution by the securities' issuers while the securities are on loan.

The LGIP cannot pledge or sell collateral securities received unless the borrower defaults. The LGIP investment policy limits the amount of reverse repurchase agreements and securities lending to 30 percent of the total portfolio. There were no violations of legal or contractual provisions and no losses resulting from a default of a borrower or lending agent during the year. There was $441.0 million on loan as of June 30, 2012.

3. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates of debt instruments will adversely affect the fair value of an investment. The LGIP portfolio is invested in a manner generally consistent with the Securities and Exchange Commission's Rule 2a-7 of the Investment Company Act of 1940, i.e., money market funds. To a great extent, the Rule 2a-7 investment guidelines are directed towards limiting interest rate risk in order to maintain a stable net asset value.

The LGIP policy places a 60-day maximum on the weighted average maturity and a 120-day maximum on the weighted average life. Further, the maximum maturity of any security will not exceed 397 days, except securities utilized in repurchase agreements and U.S. agency floating or variable rate notes may have a maximum maturity of 762 days, provided that they have reset dates within one year and that on any reset date can reasonably be expected to have a market value that approximates its amortized cost. As of June 30, 2012, the LGIP had a weighted average maturity of 40 days and a weighted average life of 112 days.

The following schedule presents the LGIP investments, deposits, and related maturities, by type, and provides information about the interest rate risks associated with the LGIP investments as of June 30, 2012:

Local Government Investment Pool (LGIP)
June 30, 2012
(expressed in thousands)

		Maturity	
Investment Type	**Fair Value**	**Less than 1 Year**	**1-5 Years**
U.S. agency securities	$ 3,374,944	$ 2,340,713	$ 1,034,231
U.S. treasury securities	1,649,151	1,649,151	-
Repurchase agreements	3,609,500	3,609,500	-
Demand deposit accounts	599,041	599,041	-
Certificates of deposit and other	87,873	87,873	-
Total	$ 9,320,509	$ 8,286,278	$ 1,034,231

4. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The LGIP investment policy limits the types of securities available for investment to obligations of the U.S. government or its agencies, obligations of government-sponsored corporations, banker's acceptances, commercial paper, deposits with qualified public depositaries, and obligations of the state of Washington or its political subdivisions.

Banker's acceptances and commercial paper must be rated with the highest short-term credit rating of any two Nationally Recognized Statistical Rating Organizations at the time of purchase. The LGIP currently does not have any banker's acceptances, commercial paper, or municipal bonds in its portfolio.

Custodial Credit Risk. Custodial credit risk is the risk that, in the event of a failure of the counterparty, the LGIP will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The LGIP investment policy requires that securities purchased by the office be held by the master custodian, acting as an independent third party, in its safekeeping or trust department. Securities utilized in repurchase agreements are subject to additional restrictions. These restrictions are designed to limit the LGIP's exposure to risk and insure the safety of the investment. All securities utilized in repurchase agreements were rated AAA by Moody's and AA+ by Standard & Poor's. The fair value of securities utilized in repurchase agreements must be at least 102 percent of the value of the repurchase agreement.

Concentration of Credit Risk. Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. With the exception of U.S. treasury and U.S. agency securities, the LGIP limits the purchase of securities of any one issuer to no more than 5 percent of the portfolio.

As of June 30, 2012, U.S. treasury securities comprised 17.7 percent of the total portfolio. U.S. agency securities comprised 36.2 percent of the total portfolio, including Federal Home Loan Mortgage Corporation (4.5 percent), Federal Home Loan Bank (15.3 percent), Federal National Mortgage Association (9.4 percent), and Federal Farm Credit Bank (7.0 percent).

5. Foreign Currency Risk - None.

6. Derivatives - None.

7. Repurchase and Reverse Repurchase Agreements

State law permits the LGIP to enter into reverse repurchase agreements which are, by contract, sales of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest.

The fair value of the securities pledged as collateral by the LGIP underlying the reverse repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in the fair value of the securities.

If the dealers default on their obligations to resell these securities to the LGIP or to provide equal value in securities or cash, the LGIP would suffer an economic loss equal to the difference between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. During the fiscal year there was no credit risk for the LGIP due to the fair value plus accrued interest of the underlying securities being less than the fair value plus accrued interest of the reinvested cash. On June 30, 2012, there were no obligations under reverse repurchase agreements.

The fair value plus accrued income of mortgage-backed securities utilized in repurchase agreements with more than seven days remaining until maturity will be 105 percent of the value of the repurchase agreement. The fair value plus accrued income of securities utilized in all other repurchase agreements will be 102 percent of the value of the repurchase agreement.

The securities utilized in repurchase agreements are priced daily and held by the LGIP's custodian in the state's name. Collateralized Mortgage Obligations utilized in repurchase agreements must pass the Federal Financial Institutions Examination Council test, or not exceed a volatility rating of V-5 by Fitch Investor Services, or a similar rating of a nationally recognized rating agency. As of June 30, 2012, repurchase agreements totaled $3.61 billion.

E. INVESTMENTS – HIGHER EDUCATION SPECIAL REVENUE, ENDOWMENT, AND STUDENT SERVICES FUNDS

1. Summary of Investment Policies

The investments of the University of Washington represent 73 percent of the total investments in Higher Education Special Revenue, Endowment, and Student Services Funds.

The Board of Regents of the University of Washington is responsible for the management of the University's investments. The Board establishes investment policy, which is carried out by the Chief Investment Officer.

The University of Washington Investment Committee, comprised of Board members and investment professionals, advises on matters relating to the management of the University's investment portfolios.

The majority of the University's investments are insured, registered, and held by the University's custodial bank as an agent for the University. Investments not held by the custodian include venture capital, private equity, opportunistic investments, marketable alternatives, mortgages, real assets, and miscellaneous investments.

The University combines most short-term cash balances in the Invested Funds Pool. At June 30, 2012, the Invested Funds Pool totaled $1.39 billion. The fund also owns units in the Consolidated Endowment Fund valued at $422.9 million on June 30, 2012.

By University policy, departments with qualifying funds in the Invested Funds Pool receive distributions based on their average balances and on the type of balance. Campus depositors received 2 percent in fiscal year 2012. Endowment operating and gift accounts received 3 percent in fiscal year 2012. The difference between the actual earnings of the Invested Funds Pool and the calculated distributions is used to support activities benefiting all University departments.

The majority of the endowed funds are invested in a pooled fund called the Consolidated Endowment Fund (CEF). Individual endowments purchase units in the pool on the basis of a per unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed based on the number of units held. Chapter 24.55 RCW and the Uniform Prudent Management of Institutional Funds Act allow for the spending of appreciation in the CEF under comprehensive prudent standards.

Under the CEF spending policy approved by the Board of Regents, quarterly distributions to programs are based on an annual percentage rate of 4 percent applied to the five-year rolling average of the CEF's market valuation. Additionally, the policy allows for an administrative fee of 1 percent supporting campus-wide fundraising and stewardship activities and offsetting the internal cost of managing endowment assets.

The University records its permanent endowments at the lower of original gift value or current market value in the Restricted Nonexpendable Net Assets category. Of the total $1.31 billion permanent endowment funds (at fair value) as of June 30, 2012, the aggregate amount of the deficiencies where the fair value of the assets is less than the original gifts is $41.6 million.

Funds in irrevocable trusts managed by trustees other than the University are not reported in the financial statements. The fair value of these funds was $49.1 million at June 30, 2012. Income received from these trusts, which is included in investment income, was $2.3 million for the year ended June 30, 2012.

Net appreciation (depreciation) in the fair value of investments includes both realized and unrealized gains and losses on investments. The University realized net gains of $7.9 million in 2012 from the sale of investments.

The calculation of realized gains and losses is independent of the net appreciation of the fair value of investments. Realized gains and losses on investments that have been held in more than one fiscal year and are sold in the current year include the net appreciation of these investments reported in the prior year(s). The net depreciation in the fair value of investments during the year ended June 30, 2012 was $35.1 million.

The following schedule presents the fair value of the University of Washington's investments by type at June 30, 2012:

University of Washington
June 30, 2012
(expressed in thousands)

Investment Type	Fair Value
Cash equivalents	$ 243,017
Fixed income	1,726,157
Equity	974,827
Non-marketable alternatives	405,866
Absolute return	332,359
Real assets	166,461
Miscellaneous	7,343
Total	$ 3,856,030

2. Funding Commitments

The University enters into contracts with investment managers to fund alternate investments. As of June 30, 2012, the University had outstanding commitments to fund alternative investments in the amount of $233.7 million.

3. Securities Lending

The University's investment policies permit it to lend its securities to broker dealers and other entities. Due to market conditions, the University terminated this program in September 2008, and as of June 30, 2012, the University had no securities on loan.

4. Interest Rate Risk

The University manages interest rate risk through its investment policies and the investment guidelines established with each manager. Each fixed income manager is assigned a maximum boundary for duration as compared to the manager's relevant benchmark index. The goal is to allow ample freedom for the manager to perform while controlling the interest rate risk in the portfolio.

5. Credit Risk

Fixed income securities are subject to credit risk, which is the risk that the issuer or other counterparty to a financial instrument will not fulfill its obligations, or negative perceptions of the issuer's ability to make these payments will cause prices to decline.

The University investment policies limit fixed income exposure to investment grade assets. The investment policy for the University's invested funds cash pool requires each manager to maintain an average quality rating of "AA" as issued by a nationally recognized rating organization. The invested funds liquidity pool requires each manager to maintain an average quality rating of "A" and to hold 25 percent of their portfolios in government and government agency issues.

The investment policy for the CEF reflects its long-term nature by specifying average quality rating levels by individual manager, but still restricting investments to investment grade securities.

Custodial Credit Risk. Custodial credit risk is the risk that, in the event of a failure of the counterparty to a transaction, the University will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The University does not have a formal policy regarding custodial credit risk. However, all University assets are held in the name of the University of Washington and are not subject to custodial credit risk.

Concentration of Credit Risk. Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The CEF investment policy limits concentration by manager, country (other than U.S.), and market sector. The University further mitigates concentration of credit risk through the due diligence of each manager and careful monitoring of asset concentrations.

The composition of the fixed income securities at June 30, 2012, along with credit quality and effective duration measures is summarized below. The schedule excludes $248.4 million of fixed-income securities held outside the CEF and the Invested Funds Pool, which makes up 6.4 percent of the University's investments.

University of Washington
Invested Funds Pool and Consolidated Endowment Fund
Fixed Income Credit Quality and Effective Duration
June 30, 2012
(expressed in thousands, duration in years)

Investments	U.S. Government	Investment Grade	Non-Investment Grade	Not Rated	Total	Duration (in years)
U.S. treasuries	$ 825,433	$ -	$ -	$ -	$ 825,433	3.20
U.S. government agency	534,137	-	-	-	534,137	2.61
Mortgage-backed	-	64,500	16,739	5,920	87,159	3.59
Asset-backed	-	122,815	3,757	-	126,572	2.02
Corporate and other	-	142,890	151	4,384	147,425	1.62
Total	$ 1,359,570	$ 330,205	$ 20,647	$ 10,304	$ 1,720,726	2.84

6. Foreign Currency Risk

The University's investment policies permit investments in international equity and other asset classes that can include foreign currency exposure. At June 30, 2012, the University had net outstanding forward commitments to sell foreign currency with a total fair value of $10.9 million, which equals 0.28 percent of the total portfolio.

The following schedule details the market value of foreign denominated securities by currency type:

University of Washington
Consolidated Endowment Fund
Foreign Currency Risk
June 30, 2012
(expressed in thousands)

Foreign Currency	Amount
E.M.U.-Euro	$ 70,764
Britain-Pound	67,889
China-Renminbi	52,213
India-Rupee	49,802
Japan-Yen	48,273
Russia-Ruble	38,328
Brazil-Real	36,451
Canada-Dollar	28,153
Hong Kong-Dollar	24,181
Switzerland-Franc	22,876
South Korean-Won	22,465
Australia-Dollar	14,271
Thailand-Baht	13,564
Taiwan-Dollar	13,159
Indonesia-Rupiah	12,829
Remaining currencies	122,296
Total	$ 637,514

7. Derivatives

The University's investment policies allow investing in various derivative instruments, including futures, swaps, and forwards, to manage its exposure to market fluctuations in various asset classes. Futures are financial contracts obligating the buyer to purchase an asset at a predetermined future date and price. Total return swaps involve commitments to pay interest in exchange for a market linked return, both based on notional amounts.

Credit exposure represents exposure to counterparties relating to financial instruments where gains exceed collateral held by the University or losses are less than the collateral posted by the University. There was no credit exposure as of June 30, 2012.

The University did not hold any investment or hedging derivatives as of June 30, 2012. Details on foreign currency derivatives are disclosed under Foreign Currency Risk.

The following schedule presents the significant terms for derivatives held as investments by the University:

University of Washington
Derivative Investments
June 30, 2012
(expressed in thousands)

Category	Changes in Fair Value - Included in Investment Income (Loss) Amount	Fair Value - Investment Derivative Amount	Notional
Futures contracts	$ 8,336	$ 90,732	$ 86,732

8. Reverse Repurchase Agreements – None.

F. INVESTMENTS - OFFICE OF THE STATE TREASURER CASH MANAGEMENT ACCOUNT

1. Summary of Investment Policies

The Office of the State Treasurer (OST) operates the state's Cash Management Account for investing Treasury/Trust Funds in excess of daily requirements.

The overall objective of the OST investment policy is to construct, from eligible investments noted below, an investment portfolio that is optimal or efficient. An optimal or efficient portfolio is one that provides the greatest expected return for a given expected level of risk, or the lowest expected risk for a given expected return.

The emphasis on "expected" is to recognize that investment decisions are made under conditions of risk and uncertainty. Neither the actual risk nor return of any investment decision is known with certainty at the time the decision is made.

Eligible Investments. Eligible investments are only those securities and deposits authorized by statute, including chapters 39.58, 39.59, 43.84.080, and 43.250 RCW. Eligible investments include:

- Obligations of the U.S. government.
- Obligations of U.S. government agencies or of corporations wholly owned by the U.S. government.
- Obligations of government-sponsored corporations that are or may become eligible as collateral for advances to member banks as determined by the board of governors of the Federal Reserve.
- Banker's acceptances purchased on the secondary market rated with the highest short-term credit rating of any two Nationally Recognized Statistical Rating Organizations (NRSROs) at the time of purchase. If the banker's acceptance is rated by more than two NRSROs, it must have the highest rating from all of the organizations.
- Commercial paper, provided that the OST adheres to policies and procedures of the State Investment Board regarding commercial paper (RCW 43.84.080(7)).
- Certificates of deposit with financial institutions qualified by the Washington Public Deposit Protection Commission.
- Local Government Investment Pool.
- Obligations of the state of Washington or its political subdivisions.

Investment Restrictions. To provide for the safety and liquidity of Treasury/Trust Funds, the Cash Management Account investment portfolio is subject to the following restrictions:

- The final maturity of any security will not exceed ten years.

- Purchase of collateralized mortgage obligations is not allowed.

- The allocation to investments subject to high price sensitivity or reduced marketability will not exceed 15 percent of the daily balance of the portfolio.

Additionally, investments in non-government securities, excluding collateral of repurchase agreements, must fall within prescribed limits.

2. Securities Lending

State statutes permit the OST to lend its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The OST, which has contracted with a lending agent to lend securities, earns a fee for this activity.

The OST lending agent lends U.S. government and U.S. agency securities and receives collateral, which can be in the form of cash or other securities. The collateral, which must be valued at 102 percent of the fair value of the loaned securities, is priced daily and, if necessary, action is taken to maintain the collateralization level at 102 percent.

The cash is invested by the lending agent in repurchase agreements or money market instruments, in accordance with investment guidelines approved by the OST. The securities held as collateral and the securities underlying the cash collateral are held by the custodian.

The contract with the lending agent requires them to indemnify the OST if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or if the borrower fails to pay the OST for income distribution by the securities' issuers while the securities are on loan. The OST cannot pledge or sell collateral securities received unless the borrower defaults. At June 30, 2012, there were no securities on loan.

The OST investment policy requires that any securities on loan be made available by the lending agent for next day liquidity at the option of the OST. During fiscal year 2012, the OST had no credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts the borrowers owed the OST.

There were no violations of legal or contractual provisions or any losses resulting from a default of a borrower or lending agent during the fiscal year.

3. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the value of the investment. The Treasury/Trust investments are separated into portfolios with objectives based primarily on liquidity needs.

The OST's investment policy limits the weighted average maturity of its investments based on cash flow expectations. Policy also directs due diligence to be exercised with timely reporting of material deviation from expectations and actions taken to control adverse developments as may be possible.

The following schedule presents the fair value of the OST's investments by type at June 30, 2012:

Office of the State Treasurer (OST)
Cash Management Account
June 30, 2012
(expressed in thousands)

		Maturity		
Investment Type	**Fair Value**	**Less than 1 Year**	**1-5 Years**	**6-10 Years**
U.S. agency obligations	$ 1,055,336	$ 20,000	$ 1,015,346	$ 19,990
U.S. government obligations	589,694	-	589,694	-
Repurchase agreements	2,225,000	2,225,000	-	-
Certificates of deposit	151,797	151,797	-	-
Investments with LGIP	350,322	350,322	-	-
Demand deposit accounts	61,446	61,446	-	-
Municipal bonds	12	12	-	-
Total	$ 4,433,607	$ 2,808,577	$ 1,605,040	$ 19,990

4. Credit Risk

The OST limits credit risk by adhering to the OST investment policy which restricts the types of investments the OST can participate in, such as: U.S. government and agency securities, banker's acceptances, commercial paper, and deposits with qualified public depositaries.

Custodial Credit Risk. The custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, a government will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The OST investment policy requires that securities purchased by the office be held by the master custodian, acting as an independent third party, in its safekeeping or trust department. Securities utilized in repurchase agreements are subject to additional restrictions. These restrictions are designed to limit the OST's exposure to risk and insure the safety of the investment.

Concentration of Credit Risk. Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. For non-governmental securities, the OST limits its exposure to concentration of credit risk by restricting the amount of investments to no more than 5 percent of the portfolio to any single issuer. During fiscal year 2012, the non-governmental securities of a single issuer held by the Cash Management Account did not exceed 5 percent of the total portfolio.

5. Foreign Currency Risk - None.

6. Derivatives - None.

7. Reverse Repurchase Agreements

State law also permits the OST to enter into reverse repurchase agreements, which are, by contract, sales of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. The fair value of the securities pledged as collateral by the OST underlying the reverse repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in the fair value of the securities.

If the dealers default on their obligations to resell these securities to the OST or to provide equal value in securities or cash, the OST would suffer an economic loss equal to the differences between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. The OST investment policy limits the amount of reverse repurchase agreements to 30 percent of the total portfolio.

The market value, plus accrued income, of mortgage-backed securities utilized in repurchase agreements with more than seven days remaining until maturity will be 105 percent of the value of the repurchase agreement.

The market value, plus accrued income, of securities utilized in all other repurchase agreements will be 102 percent of the value of the repurchase agreement. The securities utilized in repurchase agreements are priced daily and held by the Treasury/Trust custodian in the state's name. Collateralized mortgage obligations utilized in repurchase agreements must pass the Federal Financial Institutions Examination Council test or not exceed a volatility rating of V-5 by Fitch Investor Services, or a similar rating of a nationally recognized rating agency. There were no reverse repurchase agreements as of June 30, 2012.

Note 4
Receivables and Deferred/Unearned Revenue

A. GOVERNMENTAL FUNDS

Taxes Receivable
Taxes receivable at June 30, 2012, consisted of the following (expressed in thousands):

Taxes Receivable	General	Higher Education Special Revenue	Higher Education Endowment	Nonmajor Governmental Funds	Total
Property	$ 991,803	$ -	$ -	$ 178	$ 991,981
Sales	1,545,033	-	-	-	1,545,033
Business and occupation	670,164	-	-	-	670,164
Estate	1,053	18,145	-	-	19,198
Fuel	-	-	-	111,739	111,739
Other	6,598	-	-	355	6,953
Subtotals	3,214,651	18,145	-	112,272	3,345,068
Less: Allowance for uncollectible receivables	48,993	-	-	790	49,783
Total Taxes Receivable	$ 3,165,658	$ 18,145	$ -	$ 111,482	$ 3,295,285

Other Receivables
Other receivables at June 30, 2012, consisted of the following (expressed in thousands):

Other Receivables	General	Higher Education Special Revenue	Higher Education Endowment	Nonmajor Governmental Funds	Total
Public assistance (1)	$ 823,955	$ -	$ -	$ -	$ 823,955
Accounts receivable	26,418	174,564	812	72,506	274,300
Interest	-	7,582	4,064	3,504	15,150
Loans (2)	3,995	130,636	-	448,990	583,621
Long-term contracts (3)	1,867	-	9,912	66,612	78,391
Miscellaneous	121,592	46,414	9,458	181,054	358,518
Subtotals	977,827	359,196	24,246	772,666	2,133,935
Less: Allowance for uncollectible receivables	810,274	24,436	-	39,006	873,716
Total Other Receivables	$ 167,553	$ 334,760	$ 24,246	$ 733,660	$ 1,260,219

Notes:

(1) Public assistance receivables mainly represent amounts owed the state as a part of the Support Enforcement Program at the Department of Social and Health Services for the amounts due from persons required to pay support for individuals currently on state assistance, and have a low realization expectation. Accordingly, the receivable is offset by a large allowance for uncollectible receivables.

(2) Significant long-term portions of loans receivable include $107.0 million in the Higher Education Special Revenue Fund for student loans and $421.8 million in Nonmajor Governmental Funds for low income housing, public works, and economic development/revitalization loans.

(3) Long-term contracts in Nonmajor Governmental Funds are for timber sales contracts.

Deferred and Unearned Revenue

Deferred and unearned revenue at June 30, 2012, consisted of the following (expressed in thousands):

Deferred and Unearned Revenue	General	Higher Education Special Revenue	Higher Education Endowment	Nonmajor Governmental Funds	Total
Property taxes	$ 964,786	$ -	$ -	$ 57	$ 964,843
Other taxes	475,362	14,924	-	283	490,569
Timber sales	1,867	-	9,912	66,612	78,391
Charges for services	107,078	191,217	606	38,268	337,169
Donable goods	-	-	-	7,103	7,103
Grants and donations	18,317	1,552	-	9,694	29,563
Loan programs	-	13	-	801,626	801,639
Seizure of forfeited assets	-	-	-	6,390	6,390
Miscellaneous	26,925	5,171	-	28,745	60,841
Total Deferred and Unearned Revenue	$ 1,594,335	$ 212,877	$ 10,518	$ 958,778	$ 2,776,508

B. PROPRIETARY FUNDS

Taxes Receivable

Taxes receivable at June 30, 2012, consisted of $9.8 million in liquor taxes reported in Nonmajor Enterprise Funds.

Other Receivables

Other receivables at June 30, 2012, consisted of the following (expressed in thousands):

	Business-Type Activities Enterprise Funds						Governmental Activities
Other Receivables	**Workers' Compensation**	**Unemployment Compensation**	**Higher Education Student Services**	**Guaranteed Education Tuition Program**	**Nonmajor Enterprise Funds**	**Total**	**Internal Service Funds**
Accounts receivable	$ 156,880	$ -	$ 240,597	$ 6	$ 39,818	$ 437,301	$ 12,366
Interest	109,783	-	526	5,589	-	115,898	9
Miscellaneous	576,663	665,224	2,862	1	48	1,244,798	9,509
Subtotals	843,326	665,224	243,985	5,596	39,866	1,797,997	21,884
Less: Allowance for uncollectible receivables	156,691	95,054	72,481	-	263	324,489	354
Total Other Receivables	$ 686,635	$ 570,170	$ 171,504	$ 5,596	$ 39,603	$ 1,473,508	$ 21,530

Unearned Revenue

Unearned revenue at June 30, 2012, consisted of the following (expressed in thousands):

	Business-Type Activities Enterprise Funds						Governmental Activities
Unearned Revenue	**Workers' Compensation**	**Unemployment Compensation**	**Higher Education Student Services**	**Guaranteed Education Tuition Program**	**Nonmajor Enterprise Funds**	**Total**	**Internal Service Funds**
Charges for services	$ 3	$ -	$ 35,606	$ -	$ -	$ 35,609	$ 1,074
Other taxes	510	-	-	-	-	510	-
Miscellaneous	7,176	-	333	-	-	7,509	2
Total Unearned Revenue	$ 7,689	$ -	$ 35,939	$ -	$ -	$ 43,628	$ 1,076

C. FIDUCIARY FUNDS

Other Receivables

Other receivables at June 30, 2012, consisted of the following (expressed in thousands):

Other Receivables	Local Government Investment Pool	Agency Funds
Interest	$ 1,045	$ 6,903
Other	-	1,872
Subtotals	1,045	8,775
Less: Allowance for uncollectible receivables	-	3,534
Total Other Receivables	$ 1,045	$ 5,241

Unearned Revenue

Unearned revenue at June 30, 2012, consisted of $883 thousand for service credit restorations reported in Pension and Other Employee Benefit Plans.

Note 5
Interfund Balances and Transfers

A. INTERFUND BALANCES

Interfund balances as reported in the financial statements at June 30, 2012, consisted of the following (expressed in thousands):

	Due From				
Due To	**General**	**Higher Education Special Revenue**	**Higher Education Endowment**	**Nonmajor Governmental Funds**	**Workers' Compensation**
General	$ -	$ 975	$ -	$ 125,545	$ 985
Higher Education Special Revenue	56,845	-	-	9,063	253
Higher Education Endowment	-	-	-	1	-
Nonmajor Governmental Funds	681,675	133,807	1,769	171,700	35
Workers' Compensation	6	-	-	19	-
Unemployment Compensation	1,732	1,750	-	1,091	74
Higher Education Student Services	836	142,774	-	281,719	238
Guaranteed Education Tuition Program	1	-	-	-	-
Nonmajor Enterprise Funds	4,223	576	-	442	20
Internal Service Funds	28,476	970	-	20,316	6,990
Fiduciary Funds	-	-	-	-	-
Totals	$ 773,794	$ 280,852	$ 1,769	$ 609,896	$ 8,595

Nearly all interfund balances are expected to be paid within one year from the date of the financial statements. These balances resulted from the time lag between the dates that (1) interfund goods and services were provided and when the payments occurred and (2) interfund transfers were accrued and when the liquidations occurred. Interfund balances include a $28.5 million loan from a nonmajor governmental fund to the General Fund which is expected to be paid over the next six years.

In addition to the interfund balances noted in the schedule above, there are interfund balances of $6.0 million within the state's Pension Trust Funds.

Due From						
Unemployment Compensation	Higher Education Student Services	Guaranteed Education Tuition Program	Nonmajor Enterprise Funds	Internal Service Funds	Fiduciary Funds	Totals
$ 1	$ 28,465	$ 126	$ 33,762	$ 2,851	$ -	$ 192,710
-	407,832	-	-	15,449	-	489,442
-	-	-	-	-	-	1
1,091	139,920	-	253	1,669	22	1,131,941
-	-	-	-	20	-	45
-	40	-	189	188	173	5,237
-	-	-	-	-	-	425,567
-	-	-	-	-	-	1
-	40	2	574	50	42	5,969
-	30	4	1,317	53,315	1,362	112,780
-	-	-	10	-	-	10
$ 1,092	$ 576,327	$ 132	$ 36,105	$ 73,542	$ 1,599	$ 2,363,703

B. INTERFUND TRANSFERS

Interfund transfers as reported in the financial statements for the year ended June 30, 2012, consisted of the following (expressed in thousands):

	Transferred To				
Transferred From	General	Higher Education Special Revenue	Higher Education Endowment	Nonmajor Governmental Funds	Workers' Compensation
General	$ -	$ 906	$ -	$ 1,041,373	$ -
Higher Education Special Revenue	26,056	-	369	6,552	-
Higher Education Endowment	-	8,488	-	121,095	-
Nonmajor Governmental Funds	243,623	37,915	1,785	900,941	-
Workers' Compensation	-	-	-	-	-
Unemployment Compensation	-	-	-	-	-
Higher Education Student Services	-	43,175	-	-	-
Guaranteed Education Tuition Program	-	-	-	-	-
Nonmajor Enterprise Funds	220,015	-	-	10,280	-
Internal Service Funds	5,960	183	-	-	-
Totals	$ 495,654	$ 90,667	$ 2,154	$ 2,080,241	$ -

Except as noted below, transfers are used to 1) move revenues from the fund that statute requires to collect them to the fund that statute requires to expend them, 2) move receipts designated for debt service from the funds collecting the receipts to the debt service fund as debt service payments become due, 3) move unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations, 4) move profits from the Liquor Fund and the Lottery Fund as required by law, and 5) transfer amounts to and from the General Fund as required by law.

On June 30, 2012, $129.5 million was transferred from the General Fund Basic Account to the Budget Stabilization Account (BSA) in accordance with the provisions of the Constitution. The BSA is reported as an Administrative Account within the General Fund. The Constitution details a limited number of circumstances under which funds can be appropriated from the BSA, one of which is a favorable vote of at least three-fifths of the members of each house of the Legislature.

In addition to the transfers noted in the schedule above, there were transfers of $3.0 million within the state's Pension Trust Funds.

Transferred To					
Unemployment Compensation	Higher Education Student Services	Guaranteed Education Tuition Program	Nonmajor Enterprise Funds	Internal Service Funds	Totals
$ -	$ -	$ -	$ -	$ 14,044	$ 1,056,323
-	90,603	-	-	1,776	125,356
-	-	-	-	-	129,583
-	21,145	-	-	-	1,205,409
-	-	-	-	-	-
-	-	-	-	-	-
-	-	-	-	3,685	46,860
-	-	-	-	-	-
-	-	-	15,987	-	246,282
-	527	-	-	18,798	25,468
$ -	$ 112,275	$ -	$ 15,987	$ 38,303	$ 2,835,281

Note 6
Capital Assets

Capital assets at June 30, 2012, are reported by the state of Washington within Governmental Activities and Business-Type Activities, as applicable.

A. GOVERNMENTAL CAPITAL ASSETS

The following is a summary of governmental capital asset activity for the year ended June 30, 2012 (expressed in thousands):

Capital Assets	Balances July 1, 2011*	Additions	Deletions / Adjustments**	Balances June 30, 2012
Capital assets, not being depreciated:				
Land	$ 1,330,517	$ 1,041,379	$ (13,772)	$ 2,358,124
Transportation infrastructure	20,976,355	922,836	(1,031,694)	20,867,497
Intangible assets - indefinite lives	3,415	1,520	(3,415)	1,520
Art collections, library reserves, and museum and historical collections	113,071	9,641	(40)	122,672
Construction in progress	969,522	261,622	(418,543)	812,601
Total capital assets, not being depreciated	23,392,880			24,162,414
Capital assets, being depreciated:				
Buildings	10,778,797	739,774	(57,286)	11,461,285
Accumulated depreciation	(3,698,571)	(270,520)	18,352	(3,950,739)
Net buildings	7,080,226			7,510,546
Other improvements	1,214,674	60,790	(9,499)	1,265,965
Accumulated depreciation	(539,010)	(48,175)	4,611	(582,574)
Net other improvements	675,664			683,391
Furnishings, equipment and intangible assets	4,184,669	380,951	(128,246)	4,437,374
Accumulated depreciation	(2,801,889)	(258,530)	103,312	(2,957,107)
Net furnishings, equipment and intangible assets	1,382,780			1,480,267
Infrastructure	840,985	45,231	-	886,216
Accumulated depreciation	(397,230)	(27,242)	-	(424,472)
Net infrastructure	443,755			461,744
Total capital assets, being depreciated, net	9,582,425			10,135,948
Governmental Activities Capital Assets, Net	$ 32,975,305			$ 34,298,362

* Beginning balances reflect the prior period adjustment to the capitalization threshold for the University of Washington (UW) which resulted in an increase in governmental furnishings and equipment of $112.4 million and an increase to accumulated depreciation of $97.2 million.

** Adjustment activity includes a UW transfer of net assets from the Higher Education Student Services Fund, a major enterprise fund, to the Higher Education Revolving Fund, an internal service fund, of $7.8 million. The Department of Transportation made adjustments to transportation infrastructure to reclassify $907.4 million to land, and properly expense items previously capitalized that should not have been.

B. BUSINESS-TYPE CAPITAL ASSETS

The following is a summary of business-type capital asset activity for the year ended June 30, 2012 (expressed in thousands):

Capital Assets	Balances July 1, 2011*	Additions	Deletions / Adjustments **	Balances June 30, 2012
Capital assets, not being depreciated:				
Land	$ 65,264	$ -	$ (2,502)	$ 62,762
Art collections	35	-	-	35
Construction in progress	292,830	429,113	(40,529)	681,414
Total capital assets, not being depreciated	358,129			744,211
Capital assets, being depreciated:				
Buildings	2,040,447	219,346	(157,204)	2,102,589
Accumulated depreciation	(677,007)	(57,252)	34,053	(700,206)
Net buildings	1,363,440			1,402,383
Other improvements	83,305	4,825	(488)	87,642
Accumulated depreciation	(28,057)	(3,807)	342	(31,522)
Net other improvements	55,248			56,120
Furnishings, equipment and intangible assets	584,580	87,045	(53,857)	617,768
Accumulated depreciation	(437,021)	(41,273)	22,038	(456,256)
Net furnishings, equipment and intangible assets	147,559			161,512
Infrastructure	41,273	409	-	41,682
Accumulated depreciation	(14,845)	(1,486)	-	(16,331)
Net infrastructure	26,428			25,351
Total capital assets, being depreciated, net	1,592,675			1,645,366
Business-Type Activities Capital Assets, Net	$ 1,950,804			$ 2,389,577

* Beginning balances reflect the prior period adjustment to the capitalization threshold for the University of Washington (UW) which resulted in an increase in furnishings and equipment of $20.5 million and an increase in accumulated depreciation of $16.9 million.

** Adjustment activity includes a UW transfer of net assets from the Higher Education Student Services Fund, a major enterprise fund, to the Higher Education Revolving Fund, an internal service fund, of $7.8 million.

C. DEPRECIATION

Depreciation expense for the year ended June 30, 2012, was charged by the primary government as follows (expressed in thousands):

		Amount
Governmental Activities:		
General government	$	50,529
Education - elementary and secondary (K-12)		2,198
Education - higher education		335,704
Human services		31,265
Adult corrections		46,610
Natural resources and recreation		41,566
Transportation		96,595
Total Depreciation Expense - Governmental Activities *	$	604,467
Business-Type Activities:		
Workers' compensation	$	6,634
Unemployment compensation		-
Higher education student services		92,137
Guaranteed education tuition program		7
Other		5,040
Total Depreciation Expense - Business-Type Activities	$	103,818

* Includes $72.7 million internal service fund depreciation that was allocated to functions as a part of the net internal service fund activity.

D. CONSTRUCTION IN PROGRESS

Major construction commitments of the state at June 30, 2012, are as follows (expressed in thousands):

Agency / Project Commitments	Construction In Progress June 30, 2012	Remaining Project Commitments
Department of Enterprise Services:		
O'Brien Building improvement, Transportation Building preservation, Capitol Campus High Voltage System and other projects	$ 63,617	$ 16,484
Department of Labor and Industries:		
Early claims solution software and Retro rewrite	3,681	13,080
Department of Social and Health Services:		
Residential housing unit renovations and other projects	25,651	6,193
Department of Veterans Affairs:		
Veterans Cemetery, Walla Walla Veterans Home and other projects	9,873	31,769
Department of Corrections:		
Prison intake center	-	252,226
Correctional center housing units and kitchen expansion and other projects	31,235	24,868
Department of Transportation:		
State ferry vessels and terminals and other projects	149,268	231,568
Transportation infrastructure	-	3,073,930
Department of Fish and Wildlife:		
Voights Creek Hatchery, Skookumchuck Hatchery renovation, Deschutes Watershed Center, and other projects	10,426	26,017
Employment Security Department:		
Next generation TAXIS system project	27,447	27,030
University of Washington:		
HUB renovation	95,052	13,550
Washington Biomed Research Facilities	97,406	89,654
UW Bothell sportfield and Husky stadium projects	95,439	138,337
UWMC expansion	190,207	69,083
Elm, Alder and Lander Student Hall renovations, and Mercer Hall replacement	129,899	284,474
Odegard renovation, high voltage infrastructure, UW Tacoma & Bothell and other projects	122,582	64,107
Washington State University:		
Veterinary Medical Research Building, Agricultural Animal Health Research Facility, and Global Animal Health Building	103,522	59,369
Biomedical and Health Sciences Building	14,944	63,671
Martin Stadium improvements	38,664	41,336
Clean Technology Laboratory	539	57,161
Duncan Dunn/Community Hall renovation, Northside Resident Hall construction, and other projects	35,195	45,306
Eastern Washington University:		
Patterson Hall renovation, residence hall project, and other projects	32,388	53,149
Central Washington University:		
Hogue Hall renovation, new residence hall construction, and other projects	61,390	14,200
The Evergreen State College:		
Communication Building project and other projects	10,255	13,434
Western Washington University:		
Carver and Fraser Hall renovation, housing and dining, and other projects	11,772	336
Community and Technical Colleges:		
Bellevue Health Science Building	3,011	42,276
Everett index replacement, Parks Union and Jackson remodel	14,864	19,778
Green River Lindbloom Center, Trades and Industry and SMT renovation	4,427	82,988
Seattle Community College District Employment Residence Center, Georgetown PSIEC, and wood construction replacement	30,005	3,768
Tacoma Health Careers Center	2,262	38,772
Other miscellaneous community college projects	44,089	116,089
Other Agency Projects	34,906	28,537
Total Construction in Progress	$ 1,494,016	$ 5,042,540

Note 7
Long-Term Liabilities

A. BONDS PAYABLE

Bonds payable at June 30, 2012, are reported by the state of Washington within governmental activities and business-type activities, as applicable.

The State Constitution and enabling statutes authorize the incurrence of state general obligation debt, to which the state's full faith, credit, and taxing power are pledged, either by the Legislature or by a body designated by statute (presently the State Finance Committee).

Legislative authorization arises from:

- An affirmative vote of 60 percent of the members of each house of the Legislature, without voter approval, in which case the amount of such debt is generally subject to the constitutional debt limitation described below;

- When authorized by law for a distinct work or object and approved by a majority of the voters voting thereon at a general election, or a special election called for that purpose, in which case the amount of the debt so approved is not subject to the constitutional debt limitations described below;

- By the State Finance Committee without limitation as to amount, and without approval of the Legislature or approval of the voters.

The State Finance Committee debt authorization does not require voter approval; however, it is limited to providing for: (1) meeting temporary deficiencies of the state treasury if such debt is discharged within 12 months of the date of incurrence and is incurred only to provide for appropriations already made by the Legislature; or (2) refunding of outstanding obligations of the state.

Legal Debt Limitation

The State Constitution limits the amount of state debt that may be incurred by restricting the amount of general state revenues which may be allocated to pay principal and interest on debt subject to these limitations. More specifically, the constitutional debt limitation prohibits the issuance of new debt if it would cause the maximum annual debt service on all thereafter outstanding debt to exceed 9 percent of the arithmetic mean of general state revenues for the preceding three fiscal years. This limitation restricts the incurrence of new debt and not the amount of debt service that may be paid by the state in future years.

The State Constitution and current statutes require the State Treasurer to certify the debt service limitation for each fiscal year. In accordance with these provisions, the debt service limitation for fiscal year 2012 is $1.09 billion.

This computation excludes specific bond issues and types, which are not secured by general state revenues. Of the $17.85 billion general obligation bond debt outstanding at June 30, 2012, $10.71 billion is subject to the limitation.

Based on the debt limitation calculation, the debt service requirements as of June 30, 2012, did not exceed the authorized debt service limitation.

For further information on the debt limit refer to the Certification of the Debt Limitation of the State of Washington available from the Office of the State Treasurer at: http://www.tre.wa.gov/documents/debt_cdl2012.pdf, or to Schedule 11 in the Statistical Section of this report.

Authorized But Unissued

The state had a total of $7.42 billion in general obligation bonds authorized but unissued as of June 30, 2012, for the purpose of capital construction, higher education, and transportation projects throughout the state.

Interest Rates

Interest rates on fixed rate general obligation bonds ranged from 0.3 to 6.75 percent. Variable rate demand obligations (VRDO) of $108.8 million as of June 30, 2012, are remarketed on a weekly basis. Interest rates on revenue bonds range from 2 to 7.4 percent.

Debt Service Requirements to Maturity

General Obligations Bonds

General obligation bonds have been authorized and issued primarily to provide funds for:

- Acquisition and construction of state and common school capital facilities;
- Transportation construction and improvement projects;
- Assistance to local governments for public works capital projects; and
- Refunding of general obligation bonds outstanding.

Outstanding general obligations bonds are presented in the Washington State Treasurer's Annual Report for 2012. A copy of the report is available from the Office of the State Treasurer, PO Box 40200, Olympia, Washington, 98504-0200, phone number (360) 902-9000 or TTY dial 711 for the Washington Relay Service, or by visiting their website at: http://www.tre.wa.gov/aboutUs/publications/annualReports.shtml.

Total debt service requirements to maturity for general obligation bonds as of June 30, 2012, are as follows (expressed in thousands):

	Governmental Activities		Business-Type Activities		Totals	
General Obligation Bonds	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**
By Fiscal Year:						
2013	$ 695,292	$ 847,183	$ 3,400	$ 717	$ 698,692	$ 847,900
2014	765,572	826,184	3,605	527	769,177	826,711
2015	798,035	801,394	3,820	325	801,855	801,719
2016	817,732	770,862	4,050	110	821,782	770,972
2017	844,159	757,285	-	-	844,159	757,285
2018-2022	4,118,737	3,192,832	-	-	4,118,737	3,192,832
2023-2027	3,990,131	2,169,955	-	-	3,990,131	2,169,955
2028-2032	3,487,804	1,193,629	-	-	3,487,804	1,193,629
2033-2037	1,737,345	332,984	-	-	1,737,345	332,984
2038-2042	583,044	65,052	-	-	583,044	65,052
Total Debt Service Requirements	$ 17,837,851	$ 10,957,360	$ 14,875	$ 1,679	$ 17,852,726	$ 10,959,039

Revenue Bonds

Revenue bonds are authorized under current state statutes, which provide for the issuance of bonds that are not supported, or not intended to be supported, by the full faith and credit of the state.

The University of Washington issues general revenue bonds that are payable from general revenues, including student tuition and fees, grant indirect cost recovery, sales and services revenue, and investment income. General revenue bonds outstanding as of June 30, 2012, include $221.0 million in governmental activities and $1.16 billion in business-type activities.

The remainder of the state's revenue bonds pledge income derived from acquired or constructed assets for retirement of the debt and payment of the related interest.

Total debt service requirements for revenue bonds to maturity as of June 30, 2012, are as follows (expressed in thousands):

	Governmental Activities		Business-Type Activities		Totals	
Revenue Bonds	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**
By Fiscal Year:						
2013	$ 19,733	$ 81,142	$ 18,482	$ 86,267	$ 38,215	$ 167,409
2014	29,210	87,179	48,842	86,970	78,052	174,149
2015	26,728	85,613	43,965	84,835	70,693	170,448
2016	76,599	83,250	46,288	82,553	122,887	165,803
2017	80,802	79,286	47,985	80,339	128,787	159,625
2018-2022	441,552	333,788	258,200	365,734	699,752	699,522
2023-2027	406,477	211,587	268,650	294,554	675,127	506,141
2028-2032	294,660	123,506	275,175	217,812	569,835	341,318
2033-2037	168,687	59,381	373,670	144,269	542,357	203,650
2038-2042	112,708	10,992	300,573	36,862	413,281	47,854
Total Debt Service Requirements	$ 1,657,156	$ 1,155,724	$ 1,681,830	$ 1,480,195	$ 3,338,986	$ 2,635,919

Governmental activities include revenue bonds outstanding at June 30, 2012, of $388.8 million issued by the Tobacco Settlement Authority (TSA), which is a blended component unit of the state. In November 2002, the TSA issued $517.9 million in bonds and transferred $450.0 million to the state to be used for increased health care, long-term care, and other programs.

These bonds do not constitute either a legal or moral obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. The bonds are obligations of the TSA and are secured solely by the TSA's right to receive 29.2 percent of the state's tobacco settlement revenues, restricted investments of the TSA, undistributed TSA bond proceeds, and the earnings thereon held under the indenture authorizing the bonds. Total principal and interest remaining on the bonds is $706.4 million, payable through 2032. For the current year, pledged revenue and debt service were $44.8 million and $44.3 million, respectively.

Governmental activities include revenue bonds outstanding at June 30, 2012, of $500.4 million issued for the Washington State Department of Transportation. The bonds were issued to finance a portion of the costs of constructing the State Route 520 Floating Bridge and Eastside Project.

These bonds do not constitute either a legal or moral obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on the bonds is $702.5 million, payable through 2025. The bonds were issued on June 6, 2012, so both pledged revenue and debt service were zero for the current year.

Governmental activities include revenue bonds outstanding at June 30, 2012, of $179.9 million issued by Washington State University. The bonds were issued to fund various capital construction projects.

These bonds do not constitute either a legal or moral obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on the bonds is $294.1 million, payable through 2038. For the current year, pledged revenue and debt service were $27.8 million and $7.1 million, respectively.

Governmental activities include revenue bonds outstanding at June 30, 2012, of $52.9 million issued by the Tumwater Office Properties (TOP), which is a blended component unit of the state. The bonds, issued in 2004, are payable solely from the trust estate pledged under the indenture, including rental payments. The bonds were used to construct an office building in Tumwater, Washington which the state occupied beginning in fiscal year 2006.

The bonds are not a general obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on the bonds is $82.9 million, payable through 2028. For the current year, both pledged revenue and debt service were $3.9 million.

Governmental activities include revenue bonds outstanding at June 30, 2012, of $304.5 million issued by FYI Properties, a blended component unit of the state. The bonds, issued in 2009, are payable solely from the trust estate pledged under the indenture, including rental payments. The bonds were used to construct an office building in Olympia, Washington which the state occupied beginning in fiscal year 2012.

The bonds are not a general obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on the bonds is $584.2 million, payable through 2039. For the current year, both pledged revenue and debt service were $17.5 million.

Additionally, governmental activities include revenue bonds outstanding at June 30, 2012, of $9.7 million issued by the City of Aberdeen. The bonds were used to extend utilities to the state Department of Corrections Stafford Creek Corrections Center (SCCC). The Department of Corrections entered into an agreement with the City of Aberdeen to pay a system development fee sufficient to pay the debt service on the bonds. The bonds were issued in 1998 and 2002, and refunded by the City in 2010, and are payable solely from current operating appropriations.

The bonds are not a general obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds. Total principal and interest remaining on these bonds is $11.6 million, payable through 2022. For the current year, both pledged revenue and debt service were $1.6 million.

The state's colleges and universities issue bonds for the purpose of housing, dining, parking, and student facilities construction. These bonds are reported within business-type activities and are secured by a pledge of specific revenues. These bonds are not a general obligation of the state, nor does the state pledge its full faith, credit, or taxing power for payment of these bonds.

Total pledged specific revenues for the state's colleges and universities to repay the principal and interest of revenue bonds as of June 30, 2012, are as follows (expressed in thousands):

Source of Revenue Pledged	Housing and Dining Revenues (Net of Operating Expenses)	Student Facilities Fees and Earnings on Invested Fees	Parking Revenues (Net of Operating Expenses)	Bookstore Revenues
Current revenue pledged	$ 31,097	$ 43,598	$ 2,687	$ 38
Current year debt service	19,617	19,728	777	228
Total future revenues pledged *	477,223	458,458	9,311	5,024
Description of debt	Housing and dining bonds, issued in 1998-2012	Student facilities bonds, issued in 1996-2009 and refunding revenue bonds, issued in 2002-2012	Parking system and refunding revenue bonds, issued in 2004-2005	Student union and recreation center bonds issued in 2004
Purpose of debt	Construction and renovation of student housing and dining projects	Construction, renovation and improvements to student activity facilities and sports stadium	Construction of parking garage and improvements	Construct new bookstore as part of new student union and recreation center building
Term of commitment	2013-2042	2019-2038	2024-2030	2034
Percentage of debt service to pledged revenues (current year)	63.08%	45.25%	28.92%	594.19%

* Total future principal and interest payments.

B. CERTIFICATES OF PARTICIPATION

Certificates of participation at June 30, 2012, are reported by the state of Washington within governmental activities and business-type activities, as applicable.

Current state law authorizes the state to enter into long-term financing contracts for the acquisition of real or personal property and for the issuance of certificates of participation in the contracts. These certificates of participation do not fall under the general obligation debt limitations and are generally payable only from annual appropriations by the Legislature.

Other specific provisions could also affect the state's obligation under certain agreements. The certificates of participation are recorded for financial reporting purposes if the possibility of the state not meeting the terms of the agreements is considered remote.

Total debt service requirements for certificates of participation to maturity as of June 30, 2012, are as follows (expressed in thousands):

	Governmental Activities		Business-Type Activities		Totals	
Certificates of Participation	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**
By Fiscal Year:						
2013	$ 83,552	$ 25,667	$ 8,587	$ 2,855	$ 92,139	$ 28,522
2014	48,711	15,377	6,124	1,710	54,835	17,087
2015	43,240	13,715	4,810	1,526	48,050	15,241
2016	39,458	12,131	4,389	1,349	43,847	13,480
2017	27,695	18,785	3,081	2,089	30,776	20,874
2018-2022	113,345	38,427	12,608	4,274	125,953	42,701
2023-2027	80,712	17,211	8,978	1,914	89,690	19,125
2028-2032	31,933	2,842	3,552	316	35,485	3,158
Total Debt Service Requirements	$ 468,646	$ 144,155	$ 52,129	$ 16,033	$ 520,775	$ 160,188

C. DEBT REFUNDINGS

When advantageous and permitted by statute and bond covenants, the State Finance Committee authorizes the refunding of outstanding bonds and certificates of participation. Colleges and universities may also refund revenue bonds.

When the state refunds outstanding bonds, the net proceeds of each refunding issue are used to purchase U.S. government securities that are placed in irrevocable trusts with escrow agents to provide for all future debt service payments on the refunded bonds.

As a result, the refunded bonds are considered defeased and the liability is removed from the government-wide statement of net assets.

Current Year Defeasances

Bonds

Governmental Activities. On November 9, 2011, the state issued $461.4 million of various purpose general obligation refunding bonds with an average interest rate of 4.84 percent to refund $488.1 million of various purpose general obligation bonds with an average interest rate of 4.91 percent. The refunding resulted in a $58.4 million gross debt service savings over the next 13 years and a net present value savings of $48.7 million.

Also on November 9, 2011, the state issued $42.3 million of motor vehicle fuel tax refunding bonds with an average interest rate of 4.84 percent to refund $43.7 million of motor vehicle fuel tax general obligation bonds with an average interest rate of 4.91 percent. The refunding resulted in a $3.9 million gross debt service savings over the next 13 years and a net present value savings of $2.9 million.

On February 21, 2012, the state issued $733.7 million of various purpose general obligation refunding bonds with an average interest rate of 4.43 percent to refund $781.2 million of various purpose general obligation bonds with an average interest rate of 5 percent. The refunding resulted in a $145.6 million gross debt service savings over the next 18 years and a net present value savings of $114.7 million.

Also on February 21, 2012, the state issued $271.1 million of motor vehicle fuel tax refunding bonds with an average interest rate of 4.37 percent to refund $288.5 million of motor vehicle fuel tax general obligation bonds with an average interest rate of 4.93 percent. The refunding resulted in a $50.4 million gross debt service savings over the next 18 years and a net present value savings of $40.5 million.

Business-Type Activities. On July 28, 2011, the University of Washington issued $211.4 million in general revenue and refunding bonds. $74.5 million of the proceeds were used to refund $89.3 million of 63-20 financings issued through third parties. The refunded bonds had coupon rates ranging from 5 to 6.6 percent; the new bonds have an average interest rate of 4.623 percent. The refunding resulted in a $17.0 million gross debt service savings over the next 20.7 years and resulted in a total economic gain of $13.7 million.

On March 7, 2012, the University of Washington issued $50.3 million of general revenue and refunding bonds with an average interest rate of 4.79 percent to refund $62.0 million of existing bonds with an average interest rate of 4.99 percent. The refunding resulted in an $8.2 million gross debt service savings over the next 11.7 years and an economic gain of $8.0 million.

On April 17, 2012, Central Washington University issued $7.7 million in business-type activity revenue refunding bonds with an average interest rate of 3.34 percent to refund $7.5 million of business-type activity revenue bonds with an average interest rate of 5.31 percent. The refunding resulted in a $1.6 million gross debt service savings over the next 20 years and an economic loss of $101,577.

On April 30, 2012, Western Washington University issued $24.4 million in student recreation fee revenue and refunding bonds with an average interest rate of 3.92 percent to refund $23.6 million of student recreation fee revenue bonds with an average interest rate of 5.19 percent. The refunding resulted in a $697,615 gross debt service loss over the next 15 years and an economic gain of $2.7 million.

Certificates of Participation (COPs)

On August 24, 2011, the state issued $16.5 million in refunding certificates of participation with an average interest rate of 4.67 percent to refund $18.1 million of certificates of participation with interest rates between 4.57 and 5.28 percent. The refunding resulted in a $2.4 million gross debt service savings over the next 12 years and a net present value savings of $2.1 million.

On March 23, 2012, the state issued $9.1 million in refunding certificates of participation with an average interest rate of 2.71 percent to refund $10.1 million of certificates of participation with an average interest rate of 4.84 percent. The refunding resulted in a $1.0 million gross savings over the next 10.5 years and a net present value savings of $998,000.

Prior Year Defeasances

In prior years, the state defeased certain general obligation bonds, revenue bonds, and certificates of participation by placing the proceeds of new bonds and certificates in an irrevocable trust to provide for all future debt service payments on the prior bonds and certificates.

Accordingly, the trust account assets and the liability for the defeased bonds and certificates are not included in the state's financial statements.

General Obligation Bond Debt

On June 30, 2012, $1.91 billion of general obligation bonded debt outstanding is considered defeased.

Revenue Bond Debt

On June 30, 2012, $75.2 million of revenue bonded debt outstanding is considered defeased.

Certificates of Participation Debt

On June 30, 2012, $66.1 million of certificates of participation debt outstanding is considered defeased.

D. LEASES

Leases at June 30, 2012, are reported by the state of Washington within governmental activities and business-type activities, as applicable.

The state leases land, office facilities, office and computer equipment, and other assets under a variety of agreements. Although lease terms vary, most leases are subject to appropriation from the Legislature to continue the obligation. If the possibility of receiving no funding from the Legislature is remote, leases are considered noncancelable for financial reporting purposes. Leases that represent acquisitions are classified as capital leases, and the related assets and liabilities are recorded in the financial records at the inception of the lease.

Other leases are classified as operating leases with the lease payments recorded as expenditures or expenses during the life of the lease. Certain operating leases are renewable for specified periods. In most cases, management expects that the leases will be renewed or replaced by other leases.

Land, buildings and equipment under capital leases as of June 30, 2012, include the following (expressed in thousands):

	Governmental Activities	Business-Type Activities
Land (non-depreciable)	$ 1,918	$ -
Buildings	4,105	4,512
Equipment	24,026	5,791
Less: Accumulated depreciation	(16,547)	(7,871)
Totals	$ 13,502	$ 2,432

The following schedule presents future minimum payments for capital and operating leases as of June 30, 2012 (expressed in thousands):

	Capital Leases		Operating Leases	
Capital and Operating Leases	**Governmental Activities**	**Business-Type Activities**	**Governmental Activities**	**Business-Type Activities**
By Fiscal Year:				
2013	$ 3,242	$ 825	$ 106,319	$ 25,960
2014	1,911	963	97,718	25,256
2015	1,582	946	86,326	23,930
2016	278	933	67,070	21,245
2017	134	920	45,637	16,638
2018-2022	420	2,592	163,632	20,295
2023-2027	25	48	114,636	13,045
2028-2032	-	-	112,458	15,119
2033-2037	-	-	117,831	17,523
2038-2042	-	-	41,026	19,133
Total Future Minimum Payments	7,592	7,227	952,653	198,144
Less: Executory Costs and Interest Costs	(441)	(1,505)	-	-
Net Present Value of Future Minimum Lease Payments	$ 7,151	$ 5,722	$ 952,653	$ 198,144

The total operating lease rental expense for fiscal year 2012 for governmental activities was $277.0 million, of which $1.0 million was for contingent rentals. The total operating lease rental expense for fiscal year 2012 for business-type activities was $51.2 million, of which $34 thousand was for contingent rentals.

E. CLAIMS AND JUDGMENTS

Claims and judgments are materially related to three activities: workers' compensation, risk management, and health insurance. Workers' compensation is a business-type activity, and risk management and health insurance are governmental activities. A description of the risks to which the state is exposed by these activities, and the ways in which the state handles the risks, is presented in Note 1.E.

Workers' Compensation

At June 30, 2012, $35.42 billion of unpaid claims and claim adjustment expenses are presented at their net present and settlement value of $22.60 billion. These claims are discounted at assumed interest rates of 2.0 percent (time loss and medical) to 6.5 percent (pensions) to arrive at a settlement value.

The claims and claim adjustment liabilities of $22.60 billion as of June 30, 2012, include $10.86 billion for supplemental pension cost of living adjustments (COLAs) that by statute are not to be fully funded.

These COLA payments are funded on a pay-as-you-go basis, and the workers' compensation actuaries have indicated that future premium payments will be sufficient to pay these claims as they come due.

The remaining claims liabilities of $11.74 billion are fully funded by long-term investments, net of obligations under securities lending agreements.

Changes in the balances of workers' compensation claims liabilities during fiscal years 2011 and 2012 were as follows (expressed in thousands):

Workers' Compensation Fund	Balances Beginning of Fiscal Year	Incurred Claims and Changes in Estimates	Claim Payments	Balances End of Fiscal Year
2011	$ 24,025,832	1,016,932	(2,099,453)	$ 22,943,311
2012	$ 22,943,311	1,731,341	(2,078,302)	$ 22,596,350

Risk Management

The Risk Management Fund administers tort and sundry claims filed against Washington state agencies, except the University of Washington and the Department of Transportation Ferries Division. The Fund reports a tort liability when it becomes probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an actuarially determined amount for tort claims that have been incurred but not reported. It also includes an actuarial estimate of loss adjustment expenses for tort defense.

Because actual liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, it should be recognized that future loss emergence will likely deviate, perhaps materially, from the actuarial estimates. Liabilities are re-evaluated annually to take into consideration recently settled claims, the frequency of claims, and other economic or social factors.

The state is a defendant in a significant number of lawsuits pertaining to general and automobile liability matters.

As of June 30, 2012, outstanding and actuarially determined claims against the state and its agencies, with the exception of the University of Washington, including actuarially projected defense costs were $813.4 million for which the state has recorded a liability. The state is restricted by law from accumulating funds in the Self Insurance Liability Program in excess of 50 percent of total outstanding and actuarially determined liabilities.

At June 30, 2012, the Risk Management Fund held $107.9 million in cash and pooled investments designated for payment of these claims under the state's Self Insurance Liability Program.

Changes in the balances of risk management claims liabilities during fiscal years 2011 and 2012 were as follows (expressed in thousands):

Risk Management Fund	Balances Beginning of Fiscal Year	Incurred Claims and Changes in Estimates	Claim Payments	Tort Defense Payments	Balances End of Fiscal Year
2011	$ 727,136	86,297	(74,051)	(36,750)	$ 702,632
2012	$ 702,632	170,437	(42,747)	(16,949)	$ 813,373

Health Insurance

The Health Insurance Fund establishes a liability when it becomes probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an actuarially determined amount for claims that have been incurred but not reported. Because actual claims liabilities depend on various complex factors, the process used in computing claims liabilities does not always result in an exact amount.

Claims liabilities are re-evaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors.

At June 30, 2012, health insurance claims liabilities totaling $68.9 million are fully funded with cash and investments, net of obligations under securities lending agreements.

Changes in the balances of health insurance claim liabilities during fiscal years 2011 and 2012 were as follows (expressed in thousands):

Health Insurance Fund	Balances Beginning of Fiscal Year	Incurred Claims and Changes in Estimates	Claim Payments	Balances End of Fiscal Year
2011	$ 88,395	736,340	(739,745)	$ 84,990
2012	$ 84,990	771,328	(787,411)	$ 68,907

F. POLLUTION REMEDIATION

The state reports pollution remediation obligations in accordance with GASB Statement No. 49. The liability reported involves estimates of financial responsibility and amounts recoverable as well as remediation costs.

The liability could change over time as new information becomes available and as a result of changes in remediation costs, technology and regulations governing remediation efforts. Additionally, the responsibilities and liabilities discussed in this disclosure are intended to refer to obligations solely in the accounting context. This disclosure does not constitute an admission of any legal responsibility or liability. Further, it does not establish or affect the rights or obligations of any person under the law, nor does this disclosure impose upon the state any new mandatory duties or obligations.

The state and its agencies are participating as potentially responsible parties in numerous pollution remediation projects under the provisions of the federal Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA, generally referred to as Superfund) and the state Model Toxics Control Act.

There are 25 projects in progress for which the state has recorded a liability of $26.4 million.

The state has also voluntarily agreed to conduct certain remediation activities to the extent of funding paid to the state by third parties for such purposes. At June 30, 2012, the state has recorded a liability of $138.8 million for remaining project commitments.

Overall, the state has recorded a pollution remediation liability of $165.2 million, measured at its estimated amount, using the expected cash flow technique. The overall estimate is based on professional judgment, experience, and historical cost data. For some projects, the state can reasonably estimate the range of expected outlays early in the process because the site situation is common or similar to other sites with which the state has experience. In other cases, the estimates are limited to an amount specified in a settlement agreement, consent decree, or contract for remediation services.

The pollution remediation activity at some sites for which the state would otherwise have a reportable obligation is at a point where certain costs are not reasonably estimable. For example, a site assessment, remedial investigation, or feasibility study is in progress and the cleanup methodology has not yet been determined; consequently, associated future costs cannot be estimated.

The state's reported liability does not include remediation costs for future activities where costs are not yet reasonably estimable.

G. LONG-TERM LIABILITY ACTIVITY

Long-term liability activity at June 30, 2012, is reported by the state of Washington within governmental activities and business-type activities, as applicable. Long-term liability activity for governmental activities for fiscal year 2012 is as follows (expressed in thousands):

Governmental Activities:	Beginning Balance July 1, 2011	Additions	Reductions	Ending Balance June 30, 2012	Amounts Due Within One Year
Long-Term Debt:					
GO Bonds Payable:					
General obligation (GO) bonds	$ 16,084,175	$ 3,337,180	$ 2,214,805	$ 17,206,550	$ 659,800
GO - zero coupon bonds (principal)	666,196	-	34,895	631,301	35,492
Subtotal - GO bonds payable	16,750,371	3,337,180	2,249,700	17,837,851	695,292
Accreted interest - GO - zero coupon bonds	393,181	21,538	-	414,719	-
Revenue bonds payable	739,691	972,208	54,743	1,657,156	19,733
Less: Deferred amounts for issuance discounts	(7,310)	626	-	(6,684)	-
Total Bonds Payable	17,875,933	4,331,552	2,304,443	19,903,042	715,025
Other Liabilities:					
Certificates of participation	481,929	57,433	70,716	468,646	83,552
Claims and judgments	891,239	276,626	145,881	1,021,984	279,411
Installment contracts	7,012	-	213	6,799	96
Leases	5,913	3,954	2,716	7,151	3,120
Compensated absences	537,454	326,364	309,867	553,951	67,244
Unfunded pension obligations	234,320	48,392	289	282,423	-
Other postemployment benefits obligations	921,841	224,649	-	1,146,490	-
Pollution remediation obligations	168,219	20,739	23,724	165,234	-
Unclaimed property refunds	100,172	29,086	6	129,252	51
Other	316,097	1,180,040	1,065,362	430,775	299,678
Total Other Liabilities	3,664,196	2,167,283	1,618,774	4,212,705	733,152
Total Long-Term Debt	$ 21,540,129	$ 6,498,835	$ 3,923,217	$ 24,115,747	$ 1,448,177

For governmental activities, certificates of participation are being repaid approximately 52 percent from the General Fund, 35 percent from the Higher Education Special Revenue Fund, and the balance from various governmental funds. The compensated absences liability will be liquidated approximately 44 percent by the General Fund, 33 percent by the Higher Education Special Revenue Fund, and the balance by various other governmental funds. The claims and judgments liability will be liquidated approximately 80 percent by the Risk Management Fund (an internal service fund), 7 percent by the Health Insurance Fund (an internal service fund), and the balance by various other governmental funds. The other postemployment benefits obligations liability will be liquidated approximately 44 percent by the General Fund, 33 percent by the Higher Education Special Revenue Fund, and the balance by various other governmental funds. The pollution remediation liability will be liquidated approximately 84 percent by the Wildlife and Natural Resources Fund, a nonmajor governmental fund, and the balance by various other governmental funds. The unclaimed property refunds will be liquidated against future unclaimed property deposited to the General Fund. Leases, installment contract obligations, and other liabilities will be repaid from various other governmental funds.

Long-term liability activity for business-type activities for fiscal year 2012 (expressed in thousands) is as follows:

Business-Type Activities	Beginning Balance July 1, 2011	Additions	Reductions	Ending Balance June 30, 2012	Amounts Due Within One Year
Long-Term Debt:					
General obligation bonds payable	$ 18,080	$ -	$ 3,205	$ 14,875	$ 3,400
Revenue bonds payable	1,423,167	445,554	186,891	1,681,830	18,482
Plus: Unamortized amounts issuance premiums	13,662	63,897	4,898	72,661	-
Less: Deferred amounts for issuance discounts	(449)	33	-	(416)	-
Less: Deferred gain/loss on bond refunding	(8,517)	510	7,666	(15,673)	-
Total Bonds Payable	1,445,943	509,994	202,660	1,753,277	21,882
Other Liabilities:					
Certificates of participation	61,666	10,310	19,847	52,129	8,587
Less: Deferred amounts for issuance discounts	-	4	(1,244)	1,248	-
Claims and judgments	22,955,326	633,244	980,617	22,607,953	1,777,642
Lottery prize annuities payable	240,158	54,087	87,666	206,579	40,137
Tuition benefits payable	2,730,700	336,759	125,459	2,942,000	160,000
Leases	6,490	67	835	5,722	539
Compensated absences	60,991	28,841	24,243	65,589	33,097
Other postemployment benefits obligations	105,926	26,965	-	132,891	-
Other	225,200	493,625	616,725	102,100	76,753
Total Other Liabilities	26,386,457	1,583,902	1,854,148	26,116,211	2,096,755
Total Long-Term Debt	$ 27,832,400	$ 2,093,896	$ 2,056,808	$ 27,869,488	$ 2,118,637

Note 8

No Commitment Debt

The Washington State Housing Finance Commission, Washington Higher Education Facilities Authority, Washington Health Care Facilities Authority, and Washington Economic Development Finance Authority (financing authorities) were created by the Legislature. For financial reporting purposes, they are discretely presented as component units. These financing authorities issue bonds for the purpose of making loans to qualified borrowers for capital acquisitions, construction, and related improvements.

These bonds do not constitute either a legal or moral obligation of the state or these financing authorities, nor does the state or these financing authorities pledge their faith and credit for the payment of such bonds.

Debt service on the bonds is payable solely from payments made by the borrowers pursuant to loan agreements. Due to their no commitment nature, the bonds issued by these financing authorities are excluded from the state's financial statements.

The schedule below presents the June 30, 2012, balances for the "No Commitment" debt of the state's financing authorities (expressed in thousands):

Financing Authorities	Principal Balance
Washington State Housing Finance Commission	$ 3,622,082
Washington Higher Education Facilities Authority	674,828
Washington Health Care Facilities Authority	5,425,000
Washington Economic Development Finance Authority	838,121
Total No Commitment Debt	$ 10,560,031

Note 9

Governmental Fund Balances

A. GOVERNMENTAL FUND BALANCES

The state's governmental fund balances are classified according to the relative constraints that control how amounts can be spent. Classifications include:

- **Nonspendable.** Balances that either are not in a spendable form or are legally or contractually required to remain intact.

- **Restricted**. Balances that are restricted for specific purposes by the constitution, enabling legislation or external resource providers such as creditors, grantors, or laws or regulations of other governments. Net assets restricted as a result of enabling legislation totaled $29.7 million at June 30, 2012.

- **Committe**d. Balances that can only be used for specific purposes pursuant to constraints imposed by formal action of the Legislature.

- **Assigned.** Balances that are constrained by management to be used for specific purposes, but are neither restricted nor committed.

- **Unassigned.** Residual balances that are not contained in the other classifications.

A summary of governmental fund balances at June 30, 2012, is as follows (expressed in thousands):

Fund Balances	General	Higher Education Special Revenue	Higher Education Endowment	Nonmajor Governmental Funds	Total
Nonspendable:					
Permanent funds	$ -	$ -	$ 1,856,749	$ 192,447	$ 2,049,196
Consumable inventories	12,883	10,457	-	43,363	66,703
Petty cash	555	2,800	-	1,625	4,980
Investments	-	36,930	62,635	1	99,566
Other receivables – long-term	41,288	-	-	-	41,288
Total Nonspendable Fund Balance	54,726	50,187	1,919,384	237,436	2,261,733
Restricted for:					
Higher education	-	706,621	1,153,452	81,573	1,941,646
Education	-	-	23,408	11,954	35,362
Transportation	-	-	-	759,321	759,321
Other purposes	5,704	-	-	21,595	27,299
Human services	-	-	156	202,937	203,093
Wildlife and natural resources	17,137	-	-	783,013	800,150
Local grants and loans	7,171	-	-	283	7,454
School construction	1,573	-	-	131,077	132,650
State facilities	-	-	-	265,148	265,148
Budget stabilization	130,104	-	-	-	130,104
Debt service	-	-	-	86,924	86,924
Pollution remediation	-	-	-	140,548	140,548
Unspent bond proceeds	-	-	-	29,589	29,589
Operations and maintenance	-	-	-	2,566	2,566
Unspent GARVEE bond proceeds	-	-	-	517,395	517,395
Third tier debt service	-	-	-	2,169	2,169
Total Restricted Fund Balance	161,689	706,621	1,177,016	3,036,092	5,081,418
Committed for:					
Higher education	42,473	1,258,434	-	57,658	1,358,565
Education	-	-	-	1,599	1,599
Transportation	-	-	-	120,819	120,819
Other purposes	5,560	-	-	149,926	155,486
Human services	8,959	-	-	262,897	271,856
Wildlife and natural resources	15,983	-	-	435,838	451,821
Local grants and loans	5,142	-	-	985,123	990,265
State facilities	-	-	-	14,431	14,431
Debt service	-	-	-	216,921	216,921
Total Committed Fund Balance	78,117	1,258,434	-	2,245,212	3,581,763
Assigned for:					
Working capital	710,091	-	-	-	710,091
Other purposes	-	-	-	44	44
Total Assigned Fund Balance	710,091	-	-	44	710,135
Total Fund Balance	$ 1,004,623	$ 2,015,242	$ 3,096,400	$ 5,518,784	$ 11,635,049

B. BUDGET STABILIZATION ACCOUNT

In accordance with Article 7, Section 12 of the Washington State Constitution, the state maintains the Budget Stabilization Account ("Rainy Day Fund"). The Budget Stabilization Account is reported in the General Fund.

By June 30th of each fiscal year, an amount equal to 1 percent of the general state revenues for that fiscal year is transferred to the Budget Stabilization Account.

The Budget Stabilization Account balance can only be used as follows: (a) If the governor declares a state of emergency resulting from a catastrophic event that necessitates government action to protect life or public safety, then for that fiscal year money may be withdrawn and appropriated from the Budget Stabilization Account, via separate legislation setting forth the nature of the emergency and containing an appropriation limited to the above-authorized purposes as contained in the declaration, by a favorable vote of a majority of the members elected to each house of the Legislature; (b) If the employment growth forecast for any fiscal year is estimated to be less than 1 percent, then for that fiscal year money may be withdrawn and appropriated from the Budget Stabilization Account by the favorable vote of a majority of the members elected to each house of the Legislature; (c) Any amount may be withdrawn and appropriated from the Budget Stabilization Account at any time by the favorable vote of at least three-fifths of the members of each house of the Legislature.

When the balance in the Budget Stabilization Account, including investment earnings, equals more than 10 percent of the estimated general state revenues in that fiscal year, the Legislature by the favorable vote of a majority of the members elected to each house of the Legislature may withdraw and appropriate the balance to the extent that the balance exceeds 10 percent of the estimated general state revenues. These appropriations may be made solely for deposit to the Education Construction Fund.

As June 30, 2012, the Budget Stabilization Account had restricted fund balance of $130.1 million.

Note 10
Deficit Net Assets

Risk Management Fund

The Risk Management Fund, an internal service fund, had deficit net assets of $709.7 million at June 30, 2012. The Risk Management Fund is used to administer the Self-Insurance Liability Program. This program investigates, processes, and adjudicates tort and sundry claims filed against Washington state agencies, with the exception of the University of Washington and the Department of Transportation Ferries Division. The Self Insurance Liability Program, initiated in 1990, is intended to provide funds for the payment of all tort claims and defense expenses.

The Risk Management Fund is supported by premium assessments to state agencies. The state is restricted by law from accumulating funds in the Self Insurance Liability Program in excess of 50 percent of total outstanding and actuarially determined claims. As a consequence, when outstanding and incurred but not reported claims are actuarially determined and accrued, the result is deficit net assets.

The following schedule details the changes in fund balance for the Risk Management Fund during the fiscal year ended June 30, 2012 (expressed in thousands):

Risk Management Fund	Net Assets (Deficit)
Balance, July 1, 2011, as restated	$ (610,964)
Fiscal year 2012 activity	(98,778)
Balance, June 30, 2012	$ (709,742)

Note 11
Retirement Plans

A. GENERAL

The state of Washington, through the Department of Retirement Systems, the Board for Volunteer Fire Fighters, and the Administrative Office of the Courts, administers 13 defined benefit retirement plans, three combination defined benefit/defined contribution retirement plans, and one defined contribution retirement plan covering eligible employees of the state and local governments.

Basis of Accounting

Pension plans administered by the state are accounted for using the accrual basis of accounting. Under the accrual basis of accounting, employee and employer contributions are recognized in the period in which employee services are performed; investment gains and losses are recognized as incurred; and benefits and refunds are recognized when due and payable in accordance with the terms of the applicable plan.

Investments

Pension plan investments are presented at fair value. Fair values are based on published market prices, quotations from national security exchanges and security pricing services, or by the respective fund managers for securities that are not actively traded. Privately held mortgages are valued at cost, which approximates fair value. Certain pension trust fund investments, including real estate and private equity, are valued based on appraisals or independent advisors. The pension funds have no investments of any commercial or industrial organization whose market value exceeds 5 percent of each plan's net assets. Additional disclosure describing investments is provided in Note 3.

Department of Retirement Systems. As established in chapter 41.50 of the Revised Code of Washington (RCW), the Department of Retirement Systems (DRS) administers eight retirement systems comprising 12 defined benefit pension plans and three combination defined benefit/defined contribution plans as follows:

- Public Employees' Retirement System (PERS)
  Plan 1 - defined benefit
  Plan 2 - defined benefit
  Plan 3 - defined benefit/defined contribution

- Teachers' Retirement System (TRS)
  Plan 1 - defined benefit
  Plan 2 - defined benefit
  Plan 3 – defined benefit/defined contribution

- School Employees' Retirement System (SERS)
  Plan 2 - defined benefit
  Plan 3 - defined benefit/defined contribution

- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF)
  Plan 1 - defined benefit
  Plan 2 - defined benefit

- Washington State Patrol Retirement System (WSPRS)
  Plan 1 - defined benefit
  Plan 2 - defined benefit

- Public Safety Employees' Retirement System (PSERS)
  Plan 2 - defined benefit

- Judicial Retirement System (JRS)
  Defined benefit plan

- Judges' Retirement Fund (Judges)
  Defined benefit plan

Although some assets of the plans are commingled for investment purposes, each plan's assets may be used only for the payment of benefits to the members of that plan in accordance with the terms of the plan.

Administration of the PERS, TRS, SERS, LEOFF, WSPRS, and PSERS systems and plans was funded by an employer rate of 0.16 percent of employee salaries. Administration of the JRS and Judges plans is funded by means of legislative appropriations.

In January 2012, the Department of Retirement Systems began collecting contributions from state institutions of higher education for deposit in the Higher Education Retirement Plan Supplemental Benefit Fund. The contributions are to begin prefunding the unfunded future obligations related to the supplemental benefits of the Higher Education Retirement Plans. Refer to Note 11.J Higher Education Retirement Plans.

Pursuant to RCW 41.50.770, the state offers its employees and employees of those political subdivisions that elect to participate, a deferred compensation program in accordance with Internal Revenue Code Section 457. The deferred compensation is not available to employees until termination, retirement, disability, death or unforeseeable financial emergency. This deferred compensation plan is administered by the Department of Retirement Systems.

The Department of Retirement Systems prepares a stand-alone financial report. Copies of the report that include financial statements and required supplementary information may be obtained by writing to Washington State Department of Retirement Systems, PO Box 48380, Olympia, Washington 98504-8380 or by visiting their website at: http:\\www.drs.wa.gov.

Board for Volunteer Fire Fighters. As established in chapter 41.24 RCW, the Washington Board for Volunteer Fire Fighters administers the Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFFRPF), a defined benefit plan. Administration of VFFRPF is funded through legislative appropriation.

Administrative Office of the Courts. As established in chapter 2.14 RCW, the Administrative Office of the Courts administers the Judicial Retirement Account (JRA), a defined contribution plan. Administration of JRA is funded through member fees.

Higher Education. As established in chapter 28B.10 RCW, eligible higher education state employees may participate in Higher Education Retirement Plans. These plans are privately administered defined contribution plans with a supplemental defined benefit component.

Plan Disclosures

Plan descriptions, funding policies, a table of employer contributions required and paid for defined benefit plans, schedules of funded status and funding progress, defined benefit pension plans valuations, annual pension cost, and three year trend information follow in Note 11.B through G, respectively. Information related to changes in actuarial assumptions and methods, and changes in benefit provisions are provided in Note 11.H and I. For information related to defined contribution plans, refer to Note 11.J. Details on plan net assets and changes in plan net assets of pension plans and other employee benefit funds administered by the state are presented in Note 11.K.

Membership of each state administered plan consisted of the following at June 30, 2011, the date of the latest actuarial valuation for all plans:

Number of Participating Members

Plans	Retirees and Beneficiaries Receiving Benefits	Terminated Members Entitled To But Not Yet Receiving Benefits	Active Plan Members Vested	Active Plan Members Nonvested	Total Members
PERS 1	53,264	1,789	7,260	473	62,786
PERS 2	24,711	24,456	87,495	29,601	166,263
PERS 3	1,388	3,680	10,823	16,765	32,656
TRS 1	36,118	581	3,700	40	40,439
TRS 2	2,657	2,423	5,719	4,566	15,365
TRS 3	2,934	6,200	33,040	19,138	61,312
SERS 2	3,823	4,874	13,849	6,935	29,481
SERS 3	2,605	5,388	19,042	12,506	39,541
LEOFF 1	7,932	1	250	-	8,183
LEOFF 2	2,015	655	13,692	3,113	19,475
WSPRS 1	875	117	767	-	1,759
WSPRS 2	-	6	145	170	321
PSERS 2	15	1	167	4,020	4,203
JRS	124	-	3	-	127
Judges	13	-	-	-	13
JRA	1	169	9	-	179
VFFRPF	3,836	6,142	4,008	6,554	20,540
Total	142,311	56,482	199,969	103,881	502,643

Following is a summary of the number of government employers participating in state administered retirement plans as of June 30, 2012:

Number of Participating Employers

Plans	State Agencies	School Districts	Counties/ Municipalities	Other Political Subdivisions	Total Employers
PERS 1	129	220	155	174	678
PERS 2	169	-	274	494	937
PERS 3	157	-	206	300	663
TRS 1	47	257	-	-	304
TRS 2	24	295	-	-	319
TRS 3	35	302	-	-	337
SERS 2	-	299	-	-	299
SERS 3	-	301	-	-	301
LEOFF 1	-	-	42	12	54
LEOFF 2	8	-	212	153	373
WSPRS 1	1	-	-	-	1
WSPRS 2	1	-	-	-	1
PSERS 2	10	-	65	1	76
JRS	1	-	-	-	1
Judges	-	-	-	-	-
JRA	3	-	-	-	3
VFFRPF	-	-	-	642	642
Total	585	1,674	954	1,776	4,989

Employers can participate in multiple systems and/or plans. The actual total number of participating employers as of June 30, 2012 is 1,965.

B. PLAN DESCRIPTIONS

Public Employees' Retirement System

The Legislature established the Public Employees' Retirement System (PERS) in 1947. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior Courts (other than judges currently in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees not in national higher education retirement programs; judges of district and municipal courts; and employees of local governments. Approximately 50 percent of PERS salaries are accounted for by state employment. PERS retirement benefit provisions are established in chapters 41.34 and 41.40 RCW and may be amended only by the Legislature.

PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a combination defined benefit/ defined contribution plan.

PERS members who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977, and by either, February 28, 2002, for state and higher education employees, or August 31, 2002, for local government employees, are Plan 2 members unless they exercised an option to transfer their membership to Plan 3.

PERS participants joining the system on or after March 1, 2002, for state and higher education employees, or September 1, 2002, for local government employees, have the irrevocable option of choosing membership in either PERS Plan 2 or PERS Plan 3. The option must be exercised within 90 days of employment. Employees who fail to choose within 90 days default to PERS Plan 3. Notwithstanding, PERS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill with less than five years to live.

PERS is comprised of and reported as three separate plans: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members.

Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund.
All assets of this Plan 2/3 defined benefit plan may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by

the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for reporting purposes.

PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the PERS Plan 1 and Plan 2 defined benefit plans accrue interest at a rate specified by the Director of DRS. During fiscal year 2012, the rate was 5.5 percent compounded quarterly. Members in PERS Plan 1 and Plan 2 can elect to withdraw total employee contributions and interest thereon upon separation from PERS-covered employment.

PERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. PERS Plan 3 defined contribution retirement benefits are financed from employee contributions and investment earnings. Members in PERS Plan 3 can elect to withdraw total employee contributions adjusted by earnings and losses from the investment of those contributions upon separation from PERS-covered employment.

PERS Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service.

The monthly benefit is 2 percent of the average final compensation (AFC) per year of service capped at 60 percent. AFC is the monthly average of the 24 consecutive highest-paid service credit months. The monthly benefit is subject to a minimum for PERS Plan 1 retirees who have 25 years of service and have been retired 20 years, or who have 20 years of service and have been retired 25 years. If a survivor option is chosen, the benefit is reduced.

Plan 1 members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. Plan 1 members may elect to receive an optional COLA that provides an automatic annual adjustment based on the Consumer Price Index. The adjustment is capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

Effective June 30, 2011, the automatic annual benefit increase for retirees/beneficiaries in PERS Plan 1 was eliminated, and the Adjusted Minimum Benefit limit was increased to $1,545 per month. Additionally, the minimum employer contribution rates for the unfunded liability were lowered.

PERS Plan 1 provides duty and non-duty disability benefits. Duty disability retirement benefits for disablement prior to the age of 60 consist of a temporary life annuity. The benefit amount is $350 a month, or two-thirds of the monthly AFC, whichever is less. The benefit is reduced by any worker's compensation benefit and is payable as long as the member remains disabled or until the member attains the age of 60, at which time the benefit is converted to the member's service retirement amount.

A member with five years of covered employment is eligible for non-duty disability retirement. Prior to the age of 55, the benefit amount is 2 percent of the AFC for each year of service reduced by 2 percent for each year that the member's age is less than 55. The total benefit is limited to 60 percent of the AFC and is actuarially reduced if a survivor option is chosen. Plan 1 members may elect to receive an optional COLA amount based on the Consumer Price Index, capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 1 members can receive credit for military service while actively serving in the military, if such credit makes them eligible to retire. Members can also purchase up to 24 months of service credit lost because of an on-the-job injury.

The survivor of a Plan 1 member who dies after having earned 10 years of service credit has the option of receiving either a monthly benefit or a lump sum payment of the member's contributions plus interest.

LEOFF Plan 1 members who transferred service credit to PERS Plan 1 between July 1, 1997, and July 1, 1998, are permitted to include the years of transferred service in meeting the 25 years of member service requirement to qualify for up to five years of prior, or non-interruptive, military service credit.

PERS Plan 2 members are vested after completing five years of eligible service. Plan 2 members are eligible for normal retirement at the age of 65 with five years of service. The monthly benefit is 2 percent of the AFC per year of service. AFC is the monthly average of the 60 consecutive highest-paid service months. There is no cap on years of service credit. A COLA is granted based on the Consumer Price Index, capped at 3 percent annually.

Half time service credit is granted for members of PERS Plan 2 and Plan 3 for educational employment prior to January 1, 1987.

PERS Plan 2 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by an early retirement factor (ERF) that varies according to age, for each year before age 65.

PERS Plan 2 members who have 30 or more years of service credit and are at least 55 years old, can retire under one of two provisions:

- With a benefit that is reduced by 3 percent for each year before age 65; or

- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules.

Plan 2 benefits are actuarially reduced if a survivor option is chosen.

The surviving spouse or beneficiary of a PERS Plan 2 member who dies after having earned 10 years of service credit has the option of either a monthly benefit or a lump sum payment of the member's contributions plus interest.

The defined benefit component of PERS Plan 3 provides members a monthly benefit that is 1 percent of the AFC per year of service. AFC is the monthly average of the 60 consecutive highest-paid service months. There is no cap on years of service credit, and Plan 3 provides the same COLA as Plan 2.

Effective June 7, 2006, PERS Plan 3 members are vested in the defined benefit portion of their plan after 10 years of service; or after five years of service, if 12 months of that service are earned after age 44; or after 5 service credit years earned in PERS Plan 2 by June 1, 2003. Plan 3 members are immediately vested in the defined contribution portion of their plan.

Vested Plan 3 members are eligible for normal retirement at age 65, or they may retire early with the following conditions and benefits:

- If they have at least 10 service credit years and are 55 years old, the benefit is reduced by an ERF that varies with age, for each year before age 65;

- If they have 30 service credit years and are at least 55 years old, they have the choice of a benefit that is reduced by 3 percent for each year before age 65; or a benefit with a smaller (or no) reduction factor (depending on age) that imposes stricter return-to-work rules.

Plan 3 benefits are actuarially reduced if a survivor option is chosen. Refer to section J of this note for a description of the defined contribution component of PERS Plan 3.

PERS Plan 2 and Plan 3 provide disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 monthly benefit amount is 2 percent of the AFC per year of service. For Plan 3 the monthly benefit amount is 1 percent of the AFC per year of service. Benefits are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option. There is no cap on years of service credit, and a COLA is granted based on the Consumer Price Index, capped at 3 percent annually.

Beneficiaries of a PERS Plan 2 or Plan 3 member with 10 years of service who is killed in the course of employment receive retirement benefits without actuarial reduction. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

PERS Plan 2 and Plan 3 members may have up to 10 years of interruptive military service credit; five years at no cost, and five years that may be purchased by paying the required contributions. A member who becomes totally incapacitated for continued employment while serving in the uniformed services, or a surviving spouse or eligible children, may request interruptive military service credit.

PERS Plan 2 and Plan 3 members can purchase up to 24 months of service credit lost because of an on-the-job injury. PERS Plan 2 and Plan 3 members who apply for early retirement may, at the time of retirement, purchase up to five years of additional service credit. The cost of the additional service credit is the actuarial equivalent value of the resulting increase in the member's benefit.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a PERS member who dies in the line of service as a result of injuries sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally or proximately out of the member's covered employment, if found eligible by the Director of the Department of Labor and Industries.

PERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and can be used only to provide the member with a monthly annuity that is paid in addition to the member's retirement benefit.

Portability of retirement benefits allows for PERS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Effective after the January 2008 distribution, gain sharing for PERS Plan 1 and Plan 3 members was discontinued.

Additional COLAs were provided to PERS Plan 1 retirees in July 2009 and new alternative early retirement provisions were created for PERS Plan 2 and Plan 3 members.

From January 1, 2007, through December 31, 2007, judicial members of PERS were given the choice to elect participation in the Judicial Benefit Multiplier (JBM) Program enacted in 2006. Justices and judges in PERS Plan 1 and Plan 2 were able to make an irrevocable election to pay increased contributions that would fund a retirement benefit with a 3.5 percent multiplier. The benefit would be capped at 75 percent of AFC.

Judges in PERS Plan 3 could elect a 1.6 percent of pay per year of service benefit, capped at 37.5 percent of AFC.

Members who chose to participate would:

- Accrue service credit at the higher multiplier beginning with the date of their election.
- Be subject to the benefit cap of 75 percent of AFC.
- Stop contributing to the Judicial Retirement Account (JRA).
- Pay higher contributions.
- Be given the option to increase the multiplier on past judicial service.

Members who did not choose to participate would:

- Continue to accrue service credit at the regular multiplier.
- Not be subject to a benefit cap.
- Continue to participate in JRA, if applicable.
- Continue to pay contributions at the regular PERS rate.
- Never be a participant in the JBM program.

Newly elected or appointed justices and judges who chose to become PERS members on or after January 1, 2007, or who had not previously opted into PERS membership, were required to participate in the JBM program.

Members required to join the JBM program would:

- Return to prior PERS Plan if membership had previously been established.
- Be mandated into Plan 2 and not have a Plan 3 transfer choice, if a new PERS member.
- Accrue the higher multiplier for all judicial service.
- Not contribute to JRA.
- Not have the option to increase the multiplier for past judicial service.

Judges and justices who are members of PERS may purchase prior judicial service credit at a higher multiplier at retirement.

Material changes, if any, in PERS benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

Teachers' Retirement System

The Legislature established the Teachers' Retirement System (TRS) in 1938. Eligibility for membership requires service as a certificated public school employee working in an instructional, administrative or supervisory capacity. TRS is comprised principally of non-state agency employees. TRS retirement benefit provisions are established in chapters 41.32 and 41.34 RCW and may be amended only by the Legislature.

TRS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a defined benefit plan with a defined contribution component.

TRS members who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977, and by June 30, 1996, are Plan 2 members unless they exercised an option to transfer their membership to Plan 3. TRS members joining the system on or after July 1, 1996, and those who exercised their transfer option, are members of TRS Plan 3.

Legislation passed in 2007 gives TRS members hired on or after July 1, 2007, 90 days to make an irrevocable choice to become a member of TRS Plan 2 or Plan 3. At the end of 90 days, any member who has not made a choice, becomes a member of Plan 3. Notwithstanding, TRS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill, with less than five years to live.

TRS is comprised of and reported as three separate plans: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members.

Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of this Plan 2/3 defined benefit plan may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for reporting purposes.

TRS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the TRS Plan 1 and Plan 2 defined benefit plans accrue interest at a rate specified by the Director of DRS. During fiscal year 2012, the rate was 5.5 percent compounded quarterly. Members in TRS Plan 1 and Plan 2 can elect to withdraw total employee contributions and interest thereon upon separation from TRS-covered employment.

TRS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. TRS Plan 3 defined contribution benefits are financed from employee contributions and investment earnings. Employees in TRS Plan 3 can elect to withdraw total employee contributions adjusted by earnings and losses from the investment of those contributions upon separation from TRS-covered employment.

TRS Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The monthly benefit is 2 percent of the average final compensation (AFC) for each year of service credit, up to a maximum of 60 percent. AFC is the total earnable compensation for the two consecutive highest-paid fiscal years, divided by two.

The monthly benefit is subject to a minimum for TRS Plan 1 retirees who have at least 25 years of service and have been retired 20 years, or who have 20 years of service and have been retired 25 years. If a survivor option is chosen, the benefit is reduced. Plan 1 members may elect to receive an optional COLA amount based on the Consumer Price Index, capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

Effective June 30, 2011, the automatic annual benefit increase for retirees/beneficiaries in TRS Plan 1 was eliminated, and the Adjusted Minimum Benefit limit was increased to $1,545 per month. Additionally, the minimum employer contribution rates for the unfunded liability were lowered.

TRS Plan 1 provides death, as well as, permanent and temporary disability benefits. TRS Plan 1 members receive the following additional lump sum death benefits: retired members $400 (if retired with 10 years of full-time membership), $400 (if inactive with 10 years of membership), active members $600 (if employed full-time at time of death). The survivor of a TRS Plan 1 member who dies after having earned 10 years of service credit has the option, upon the member's death, of either a monthly survivor benefit or the lump sum of contributions plus interest.

TRS Plan 1 members on temporary disability receive a monthly payment of $180 payable for up to two years, for the same occurrence. After five years of service, members on a disability retirement receive a benefit based on their salary and service to date of disability.

TRS Plan 2 retirement benefits are vested after completing five years of eligible service. Plan 2 members are eligible for normal retirement at the age of 65 with five years of service. The monthly benefit is 2 percent of the AFC per year of service. AFC is the monthly average of the 60 consecutive highest-paid service credit months. There is no cap on years of service credit; and a COLA is granted based on the Consumer Price Index, capped at 3 percent annually.

TRS Plan 2 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by an early retirement factor (ERF) that varies according to age, for each year before age 65.

TRS Plan 2 members who have 30 or more years of service credit and are at least 55 years old, can retire under one of two provisions:

- With a benefit that is reduced by 3 percent for each year before age 65; or

- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules.

TRS Plan 2 retirement benefits are actuarially reduced if a survivor option is chosen. Additionally, the surviving spouse or eligible children of a TRS Plan 2 member who dies after having earned 10 years of service credit has the option of either a monthly benefit or a lump sum payment of the member's contributions plus interest.

The defined benefit portion of TRS Plan 3 provides members a monthly benefit that is 1 percent of the AFC per year of service. AFC is the monthly average of the 60 consecutive highest-paid service credit months. There is no cap on years of service credit; and Plan 3 provides the same COLA as Plan 2.

TRS Plan 3 members are vested in the defined benefit portion of their plan after 10 years of service; or after five years of service if 12 months of that service are earned after age 44; or after five service credit years earned in

TRS Plan 2 by July 1, 1996. Plan 3 members are immediately vested in the defined contribution portion of their plan.

Vested TRS Plan 3 members are eligible for normal retirement at age 65, or they may retire early with the following conditions and benefits:

- If they have at least 10 service credit years and are 55 years old, the benefit is reduced by an ERF that varies according to age, for each year before age 65;

- If they have 30 service credit years and are at least 55 years old, they have the choice of a benefit that is reduced 3 percent for each year before age 65, or a benefit with a smaller (or no) reduction factor (depending on age) that imposes stricter return-to-work rules.

TRS Plan 3 retirement benefits are actuarially reduced if a survivor option is chosen.

Refer to section J of this note for a description of the defined contribution component of TRS Plan 3.

TRS Plan 2 and Plan 3 members who work for at least five months of a six-month period, from September through August, and earn 630 hours or more within that six-month period receive six months of service credit.

Plan 2 and Plan 3 members need to have two years of service credit in order to be eligible to purchase up to seven years of service credit for public education experience earned in another state or with the federal government.

TRS Plan 2 and Plan 3 provide disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 monthly benefit amount is 2 percent of the AFC per year of service. For Plan 3, the monthly benefit amount is 1 percent of the AFC per year of service. These disability benefit amounts are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option. There is no cap on years of service credit, and a COLA is granted based on the Consumer Price Index, capped at 3 percent annually.

TRS members can receive service credit for military service that interrupts employment. Additionally, TRS members who become totally incapacitated for continued employment while serving in the uniformed services, or a surviving spouse or eligible children, may request interruptive military service credit.

TRS members may purchase up to 24 consecutive months of service credit for each period of temporary duty disability. Additionally, TRS Plan 2 and Plan 3 members who have two years of earned service credit may purchase up to seven years of service credit for public education experience earned in another state or with the federal government.

TRS members may also purchase up to five years of additional service credit, once eligible for retirement. This credit can only be purchased at the time of retirement, and can be used only to provide the member with a monthly annuity that is paid in addition to the member's retirement benefit.

Beneficiaries of TRS members killed in the course of employment receive survivor benefits without actuarial reduction. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a TRS member who dies in the line of service as a result of injuries or illness sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Department of Labor and Industries.

Portability of retirement benefits allows for TRS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Effective after the January 2008 distribution, gain sharing for TRS Plan 1 and Plan 3 members was discontinued. Additional COLAs were provided to TRS Plan 1 retirees in July 2009 and new alternative early retirement provisions were created for TRS Plan 2 and Plan 3 members.

From January 1, 2007, through December 31, 2007, judicial members of TRS were given the choice to elect participation in the Judicial Benefit Multiplier (JBM) Program enacted in 2006. Justices and judges in TRS Plan 1 were able to make an irrevocable election to pay increased contributions that would fund a retirement benefit with a 3.5 percent multiplier. The benefit is capped at 75 percent of AFC.

Members who chose to participate would:

- Accrue service credit at the higher multiplier beginning with the date of their election.

- Be subject to the benefit cap of 75 percent of AFC.

- Stop contributing to the Judicial Retirement Account (JRA).

- Pay higher contributions.

- Be given the option to increase the multiplier on past judicial service.

Members who did not choose to participate would:

- Continue to accrue service credit at the regular multiplier.

- Not be subject to a benefit cap.

- Continue to participate in JRA, if applicable.

- Continue to pay contributions at the regular TRS rate.

- Never be a participant in the JBM program.

Newly elected or appointed justices and judges who chose to become TRS members on or after January 1, 2007, were required to participate in the JBM program. Members required to join the JBM program would:

- Return to prior TRS Plan if membership had previously been established.
- Accrue the higher multiplier for all judicial service.

- Not contribute to JRA.

- Not have the option to increase the multiplier for past judicial service.

Material changes, if any, in TRS benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

School Employees' Retirement System

The Legislature established the School Employees' Retirement System (SERS) effective in 2000. Membership in the system includes classified employees of school districts and educational service districts. SERS is comprised principally of non-state agency employees. SERS retirement benefit provisions are established in chapters 41.34 and 41.35 RCW and may be amended only by the Legislature.

SERS is a cost-sharing multiple-employer retirement system comprised of two separate plans for membership purposes: Plan 2 is a defined benefit plan and Plan 3 is a defined benefit plan with a defined contribution component.

As of September 1, 2000, the membership of classified school employees in PERS Plan 2 was transferred to SERS Plan 2. Those who joined on or after October 1, 1977, and by August 31, 2000, are SERS Plan 2 members unless they exercised an option to transfer their membership to Plan 3.

Until June 30, 2007, SERS members joining the system on or after September 1, 2000 became members of SERS Plan 3. Legislation passed in 2007 gives SERS members hired on or after July 1, 2007, 90 days to make an irrevocable choice to become a member of either SERS Plan 2 or Plan 3. At the end of the 90 days, any member who has not made a choice becomes a member of Plan 3. Notwithstanding, SERS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill, with less than five years to live.

SERS is comprised of and reported as two separate plans: Plan 2/3 and Plan 3. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members.

Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of this Plan 2/3 defined benefit plan may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be single plan for reporting purposes.

SERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the SERS Plan 2 defined benefit plan accrue interest at a rate specified by the Director of DRS. During fiscal year 2012, the rate was 5.5 percent compounded quarterly. Members in SERS Plan 2 can elect to withdraw total employee contributions and interest thereon upon separation from SERS-covered employment.

SERS Plan 2 members are vested after completing five years of eligible service. Plan 2 members are eligible for normal retirement at the age of 65 with five years of service. The monthly benefit is 2 percent of the average final compensation (AFC) per year of service. AFC is the monthly average of the 60 consecutive highest-paid service credit months. There is no cap on years of service credit; and a COLA is granted based on the Consumer Price Index, capped at 3 percent annually.

SERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. SERS Plan 3 defined contribution benefits are financed from employee contributions and investment earnings. Employees in SERS Plan 3 can elect to withdraw total employee contributions adjusted by earnings and losses from the investment of those contributions upon separation from SERS-covered employment.

SERS Plan 2 members are vested after completing five years of eligible service. Plan 2 members are eligible for normal retirement at the age of 65 with five years of service. The monthly benefit is 2 percent of the average final compensation (AFC) per year of service. AFC is the monthly average of the 60 consecutive highest paid service credit months. There is no cap on years of service credit; and a COLA is granted based on the Consumer Price Index, capped at 3 percent annually.

Half time service credit is granted for members of SERS Plan 2 and Plan 3 for educational employment prior to January 1, 1987.

SERS Plan 2 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by an early retirement factor (ERF) that varies according to age, for each year before age 65.

SERS Plan 2 members who have 30 service credit years and are at least 55 years old can retire under one of two provisions:

- With a benefit that is reduced by 3 percent for each year before age 65; or

- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules.

SERS Plan 2 retirement benefits are actuarially reduced if a survivor option is chosen.

The surviving spouse or eligible child of a SERS Plan 2 member who dies after having earned 10 years of service credit has the option of either a monthly benefit or a lump sum payment of the member's contributions plus interest.

The defined benefit portion of SERS Plan 3 provides members a monthly benefit that is 1 percent of the AFC per year of service. AFC is the monthly average of the 60 consecutive highest-paid service months. There is no cap on years of service credit, and Plan 3 provides the same COLA as Plan 2.

Effective June 7, 2006, SERS Plan 3 members are vested in the defined benefit portion of their plan after 10 years of service; or after 5 years of service if 12 months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 by September 1, 2000. Plan 3 members are immediately vested in the defined contribution portion of their plan.

Vested SERS Plan 3 members are eligible for normal retirement at age 65, or they may retire early with the following conditions and benefits:

- If they have at least 10 service credit years and are 55 years old, the benefit is reduced by an ERF that varies according to age, for each year before age 65;

- If they have 30 service credit years and are at least 55 years old, they have the choice of a benefit that is reduced by 3 percent for each year before age 65; or a benefit with a smaller (or no) reduction factor (depending on age) that imposes stricter return-to-work rules.

SERS Plan 3 retirement benefits are also actuarially reduced if a survivor option is chosen. Refer to section J of this note for a description of the defined contribution component of SERS Plan 3.

SERS Plan 2 and Plan 3 members may have up to 10 years of interruptive military service credit; five years at no cost and five years that may be purchased by paying the required contributions.

SERS members who become totally incapacitated for continued employment while serving in the uniformed services, or a surviving spouse or eligible children, may request interruptive military service credit.

SERS members may purchase up to 24 consecutive months of service credit for each period of temporary duty disability.

SERS Plan 2 and Plan 3 provide disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 monthly benefit amount is 2 percent of the AFC per year of service. For Plan 3 the monthly benefit amount is 1 percent of the AFC per year of service. These disability benefit amounts are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option. There is no cap on years of service credit and a COLA is granted based on the Consumer Price Index, capped at 3 percent annually.

SERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement and can be used only to provide the member with a monthly annuity that is paid in addition to the member's retirement benefit.

Should any such member die during this active duty, the member's surviving spouse or eligible children may purchase service credit on behalf of the deceased member.

Beneficiaries of a SERS Plan 2 or Plan 3 member with 10 years of service who is killed in the course of employment receive retirement benefits without actuarial reduction. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a SERS member who dies in the line of service as a result of injuries sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Director of the Department of Labor and Industries.

Portability of retirement benefits allows for SERS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Material changes, if any, in SERS benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

Law Enforcement Officers' and Fire Fighters' Retirement System

The Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) was established in 1970 by the Legislature. Membership includes all full-time, fully compensated, local law enforcement commissioned officers, firefighters, and as of July 24, 2005, emergency medical technicians.

LEOFF membership is comprised primarily of non-state employees, with Department of Fish and Wildlife enforcement officers who were first included effective July 27, 2003, being an exception. LEOFF retirement benefit provisions are established in chapter 41.26 RCW and may be amended only by the Legislature.

LEOFF is a cost-sharing multiple-employer retirement system comprised of two separate defined benefit plans. LEOFF members who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977, are Plan 2 members.

Effective July 1, 2003, the LEOFF Plan 2 Retirement Board was established by Initiative 790 to provide governance of LEOFF Plan 2. The Board's duties include adopting contribution rates and recommending policy changes to the Legislature.

LEOFF retirement benefits are financed from a combination of investment earnings, employer and employee contributions, and a special funding situation in which the state pays through legislative appropriations. Employee contributions to the LEOFF Plan 1 and Plan 2 defined benefit plans accrue interest at a rate specified by the Director of DRS. During fiscal year 2012, the rate was 5.5 percent compounded quarterly. Members in LEOFF Plan 1 and Plan 2 can elect to withdraw total employee contributions and interest earnings upon separation from LEOFF-covered employment.

LEOFF Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement with five years of service at the age of 50. The benefit per year of service calculated as a percent of final average salary (FAS) is as follows:

Term of Service	Percent of FAS
20+	2.0%
10-19	1.5%
5-9	1.0%

The FAS is the basic monthly salary received at the time of retirement, provided a member has held the same position or rank for 12 months preceding the date of retirement. Otherwise, it is the average of the highest consecutive 24 months' salary within the last 10 years of service. A COLA is granted based on the Consumer Price Index.

LEOFF Plan 1 provides death and disability benefits. Death benefits for survivors of Plan 1 members on active duty consist of the following: (1) If eligible spouse, 50 percent of the FAS, plus 5 percent of FAS for each eligible surviving child, with a limitation on the combined benefit of 60 percent of the FAS; or (2) If no eligible spouse, eligible children receive 30 percent of FAS for the first child plus 10 percent for each additional child, subject to a 60 percent limitation of FAS, divided equally.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a LEOFF Plan 1 member who dies as a result of injuries or illness sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Department of Labor and Industries.

The LEOFF Plan 1 disability benefit is 50 percent of the FAS plus 5 percent for each child up to a maximum of 60 percent. Upon recovery from disability before the age of 50, a member is restored to service with full credit for service while disabled. Upon recovery after the age of 50, the benefit continues as the greater of the member's disability benefit or service retirement benefit.

LEOFF Plan 1 members may purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and can be used only to provide the member with a monthly annuity that is paid in addition to the member's benefit.

LEOFF Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members are eligible for retirement at the age of 53 with five years of service, or at age 50 with 20 years of service. Plan 2 members receive a benefit of 2 percent of the FAS per year of service (FAS is based on the highest consecutive 60 months), actuarially reduced to reflect the choice of a survivor option. Members who retire prior to the age of 53 receive reduced benefits. If the member has at least 20 years of service and is age 50, the reduction is 3 percent for each year prior to age 53. Otherwise, the benefits are actuarially reduced for each year prior to age 53. A COLA is granted (based on the Consumer Price Index), capped at 3 percent annually.

LEOFF Plan 2 members who apply for retirement may purchase up to five years of additional service credit. The cost of this credit is the actuarial equivalent of the resulting increase in the member's benefit.

LEOFF Plan 2 members can receive service credit for military service that interrupts employment. Additionally, LEOFF Plan 2 members who become totally incapacitated for continued employment while serving in the uniformed services, or a surviving spouse or eligible children may request interruptive military service credit.

Employer authorized shared leave received by LEOFF Plan 2 members from a non-state employer, must receive the same treatment in respect to service credit and FAS that a member would normally receive if using accrued annual leave or sick leave. This applies to directly and indirectly transferred leave, such as through a shared leave pool, and includes leave transferred prior to the effective date of the act providing that retirement contributions were made on the shared leave.

LEOFF Plan 2 provides disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 benefit amount is 2 percent of the FAS for each year of service. Benefits are reduced to reflect the choice of a survivor option and for each year that the member's age is less than 53, unless the disability is duty-related. If the member has at least 20 years of service and is age 50, the reduction is 3 percent for each year prior to age 53.

LEOFF Plan 2 members may also purchase up to 24 consecutive months of service credit for each period of temporary duty disability.

Members of LEOFF Plan 2 who leave service because of a line of duty disability are allowed to withdraw 150 percent of accumulated member contributions. This withdrawal benefit is not subject to federal income tax. Alternatively, members of LEOFF Plan 2 who leave service because of a line of duty disability may be eligible to receive a retirement benefit of at least 10 percent of the FAS and 2 percent per year of service beyond five years. The first 10 percent of the FAS is not subject to federal income tax.

A disability benefit equal to 70 percent of their FAS, subject to offsets for workers' compensation and Social Security disability benefits received, is also available to those LEOFF Plan 2 members who are catastrophically disabled in the line of duty and incapable of future substantial gainful employment in any capacity. Effective June 2010, benefits to LEOFF Plan 2 members who are catastrophically disabled include payment of eligible health care insurance premiums.

LEOFF Plan 2 retirees may return to work in an eligible position covered by another retirement system, choose membership in that system and suspend their pension benefits, or not choose membership and continue receiving pension benefits without interruption.

Beneficiaries of a LEOFF Plan 2 member who is killed in the course of employment receive retirement benefits without actuarial reduction, if found eligible by the Director of the Department of Labor and Industries. Benefits to eligible surviving spouses and dependent children of LEOFF Plan 2 members killed in the course of employment include the payment of health care insurance premiums paid to the Washington state Health Care Authority.

Beginning in 2011, when state General Fund revenues increase by at least 5 percent over the prior biennium's revenues, the State Treasurer will transfer, subject to legislative appropriation, specific amounts into a Local Public Safety Enhancement Account. Half of this transfer will be proportionately distributed to all jurisdictions with LEOFF Plan 2 members. The other half will be transferred to a LEOFF Retirement System Benefits Improvement Account to fund benefit enhancements for LEOFF Plan 2 members.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a LEOFF Plan 2 member who dies as a result of injuries or illness sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Director of the Department of Labor and Industries.

Legislation passed in 2009 provides to the Washington-state-registered domestic partners of LEOFF Plan 2 members the same treatment as married spouses, to the extent that the treatment is not in conflict with federal laws.

The optional lump sum payment payable upon remarriage is increased for LEOFF Plan 2 survivors of a member killed in the course of employment from 24 times the monthly allowance that the member was receiving at the time of remarriage to an amount equal to 36 times the monthly allowance.

Portability of retirement benefits allows for LEOFF Plan 2 members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Department of Fish and Wildlife Enforcement Officers can transfer service credit earned as an enforcement officer in PERS Plan 2 or PERS Plan 3 to LEOFF Plan 2. Member, employer and state contribution rates will increase to the extent necessary to fund the difference in the value of the service credit transferred between the plans and the member contributions transferred into LEOFF Plan 2.

Active LEOFF members can choose whether or not to obtain and pay for Medicare coverage through a "divided referendum" process.

Material changes, if any, in LEOFF benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

Washington State Patrol Retirement System

The Washington State Patrol Retirement System (WSPRS) was established by the Legislature in 1947. Any commissioned employee of the Washington State Patrol is eligible to participate. WSPRS benefits are established in chapter 43.43 RCW and may be amended only by the Legislature.

WSPRS is a single-employer defined benefit retirement system. WSPRS members who joined the system by December 31, 2002, are Plan 1 members. Those who joined on or after January 1, 2003, are Plan 2 members. For financial reporting and investment purposes, however, both plans are accounted for in the same pension fund.

WSPRS retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to WSPRS accrue interest at a rate specified by the Director of DRS. During fiscal year 2012, the rate was 5.364 percent annually, compounded monthly. Members in WSPRS can elect to withdraw total employee contributions and interest earnings thereon upon separation from WSPRS-covered employment.

WSPRS member contribution rates will be no more than 7 percent of pay plus half the cost of any future benefit improvements. The employer will pay the contribution rate required to cover all system costs that are not covered by the member contribution rate. Also a minimum total contribution rate is established for WSPRS, beginning July 1, 2010.

There is no vesting requirement for active WSPRS members. Inactive WSPRS members are vested after the completion of five years of eligible service. Members are eligible for retirement at the age of 55 with five years of service, or after 25 years of service, and must retire at age 65. This mandatory requirement, however, does not apply to the chief of the Washington State Patrol.

The monthly benefit is 2 percent of the average final salary (AFS) per year of service, capped at 75 percent. A cost-of-living allowance is granted, based on the Consumer Price Index, capped at 3 percent annually.

For WSPRS Plan 1 members, AFS is based on the average of the 24 highest-paid service credit months and excludes voluntary overtime. Death benefits for these members, if on active duty, consist of the following: (1) If eligible spouse, 50 percent of the AFS, plus 5 percent of the AFS for each eligible surviving child, with a limitation on the combined benefit of 60 percent of the AFS; or (2) If no eligible spouse, 30 percent of AFS for the first child plus 10 percent for each additional child, subject to a 60 percent limitation of AFS, or (3) If no spouse or eligible children, beneficiary gets refund of contributions and interest.

For WSPRS Plan 2 members, AFS is based on the average of the 60 consecutive highest-paid service credit months and excludes both voluntary overtime and cash-outs of annual and holiday leave. At retirement, these members also have the option of selecting an actuarially reduced benefit in order to provide for post-retirement survivor benefits.

WSPRS members may purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and can be used only to provide the member with a monthly annuity that is paid in addition to the member's retirement benefit.

WSPRS benefit provisions include death benefits; however, the system provides no disability benefits.

Disability benefits may be available from the Washington State Patrol. If disability benefits are received, the member may be eligible to acquire service credit for the period of disability.

Beneficiaries of a WSPRS Plan 2 member who is killed in the course of employment receive retirement benefits without actuarial reduction, if found eligible by the Director of the Department of Labor and Industries. Benefits to eligible surviving spouses and dependents of WSPRS members killed in the course of employment include the payment of on-going health care insurance premiums paid to the Washington State Health Care Authority.

Death benefits for these members, if on active duty, consist of the following: (1) If the member is single or has less than 10 years of service, the return of the member's accumulated contributions; or (2) If the member is married, has an eligible child, or has completed 10 years of service, a reduced benefit reflecting a joint and 100 percent survivor option or 150 percent of the member's accumulated contributions, at the survivor's option.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a WSPRS member who dies as a result of injuries or illness sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Director of the Department of Labor and Industries.

The death benefit amount is adjusted each year by the Seattle Consumer Price Index up to a maximum of 3 percent each year. This applies to all members of WSPRS Plan 2 killed in the course of employment since January 1, 2009.

WSPRS Plan 2 members may receive up to five years of no-cost service credit for military service that interrupts employment. Additionally, WSPRS Plan 2 members who become totally incapacitated for continued employment while serving in the uniformed services, or a surviving spouse or eligible children may request interruptive service credit.

Compensation for members of WSPRS Plans 1 and 2 who become totally disabled during the line of duty includes any payments for premiums for employer-provided medical insurance.

Legislation passed in 2009 provides to the Washington-state-registered domestic partners of WSPRS members the same treatment as married spouses, to the extent that the treatment is not in conflict with federal laws.

Material changes, if any, in WSPRS benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

Public Safety Employees' Retirement System

The Public Safety Employees' Retirement System (PSERS) was created by the 2004 Legislature and became effective July 1, 2006. PSERS retirement benefit provisions have been established by chapter 41.37 RCW and may be only amended by the Legislature.

PSERS is a cost-sharing multiple-employer retirement system comprised of a single defined benefit plan, PSERS Plan 2. PSERS membership includes:

- Full-time employees hired by a covered employer before July 1, 2006, who met at least one of the PSERS eligibility criteria and elected membership during the period of July 1, 2006 to September 30, 2006; and,

- Full-time employees hired on or after July 1, 2006, by a covered employer, that meet at least one of the PSERS eligibility criteria.

A "covered employer" is one that participates in PSERS. Covered employers include:

- State of Washington agencies: Department of Corrections, Department of Natural Resources, Gambling Commission, Liquor Control Board, Parks and Recreation Commission, and Washington State Patrol;
- Washington state counties;

- Corrections departments of Washington state cities except for Seattle, Tacoma and Spokane; and

- Correctional entities formed by PSERS employers under the Interlocal Cooperation Act.

To be eligible for PSERS, an employee must work on a full-time basis and:

- Have completed a certified criminal justice training course with authority to arrest, conduct criminal investigations, enforce the criminal laws of Washington, and carry a firearm as part of the job; or

- Have primary responsibility to ensure the custody and security of incarcerated or probationary individuals; or

- Function as a limited authority Washington peace officer, as defined in RCW 10.93.020; or

- Have primary responsibility to supervise eligible members who meet the above criteria.

PSERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the plan accrue interest at a rate specified by the Director of DRS. During fiscal year 2012, the rate was 5.5 percent compounded quarterly. Members in PSERS Plan 2 can elect to withdraw total employee contributions and interest thereon upon separation from PSERS-covered employment.

PSERS members are vested after an employee completes five years of eligible service. PSERS members may retire with a monthly benefit of 2 percent of the average final compensation (AFC) at the age 65 with five years of service, or at the age of 60 with at least 10 years of PSERS service credit, or at age 53 with 20 years of service. AFC is the monthly average of the member's 60 consecutive highest-paid service credit months. There is no cap on years of service credit; and a cost-of-living allowance is granted based on the Consumer Price Index, capped at 3 percent annually.

PSERS members who retire prior to the age of 60 receive reduced benefits. If retirement is at age 53 or older with at least 20 years of service, a 3 percent per year reduction for each year between the age at retirement and age 60 applies.

PSERS members can receive service credit for military service that interrupts employment. Additionally, PSERS members who become totally incapacitated for continued employment while serving in the uniformed services, or a surviving spouse or eligible children may request interruptive military service credit.

PSERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement, and cannot be used to qualify for any retirement eligibility or benefit reductions based upon years of service. This credit is to be used exclusively to provide the member with a monthly annuity that is paid in addition to the member's retirement allowance.

PSERS Plan 2 provides disability benefits. There is no minimum amount of service credit required for eligibility. The monthly benefit is 2 percent of the average final compensation (AFC) for each year of service. AFC is based on the member's 60 consecutive highest creditable months of service. Benefits are actuarially reduced for each year that the member's age is less than 60 (with 10 or more service credit years in PSERS), or less than 65 (with fewer than 10 service credit years). There is no cap on years of service credit and a cost-of-living allowance is granted based on the Consumer Price Index, capped at 3 percent annually.

PSERS members may purchase up to 24 consecutive months of service credit for each period of temporary duty disability.

Beneficiaries of a PSERS Plan 2 member with 10 years of service who is killed in the course of employment receive retirement benefits without actuarial reduction. This provision applies to any member killed in the course of employment, if found eligible by the Director of the Department of Labor and Industries.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a PSERS member who dies as a result of injuries or illness sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Department of Labor and Industries.

The optional lump sum payment payable upon remarriage is increased for PSERS Plan 2 survivors of a member killed in the course of employment from 24 times the monthly allowance that the member was receiving at the time of remarriage to an amount equal to 36 times the monthly allowance.

Portability of retirement benefits allows for PSERS members' compensation that is reportable in all dual members' systems, except in WSPRS, to be included in the calculation of all dual members' benefits, and removing the "maximum benefit rule" for dual members who have less than 15 years of service in one capped plan and service in one uncapped plan.

Material changes, if any, to PSERS benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

Judicial Retirement System

The Judicial Retirement System (JRS) was established by the Legislature in 1971. Membership includes judges elected or appointed to the Supreme Court, Court of Appeals, and Superior Courts on or after August 9, 1971. The system was closed to new entrants on July 1, 1988, with new judges joining PERS. JRS retirement benefit provisions are established in chapter 2.10 RCW and may be amended only by the Legislature.

JRS is an agent multiple-employer retirement system comprised of a single defined benefit plan. JRS retirement benefits are financed on a pay-as-you-go basis from a combination of investment earnings, employer contributions, employee contributions, and a special funding situation in which the state pays the remaining contributions.

Employee contributions accrue interest at a rate specified by the Director of DRS. During fiscal year 2012, the rate on employee contributions was 5.5 percent, compounded quarterly. JRS members who are vested in the plan may not elect to withdraw their contributions upon termination. However, any JRS member that left the system before July 1, 1988, or his/her spouse, who was ineligible to receive a benefit at that time, may apply and receive a refund of such contributions from DRS, if said contributions have not been already refunded via a sundry claims appropriation from the Legislature.

JRS members are eligible for retirement at the age of 60 with 15 years of service, or at the age of 60 after 12 years of service (if the member left office involuntarily) with at least 15 years after beginning judicial service.

The benefit per year of service calculated as a percent of final average salary (FAS) is shown in the table below. This benefit is capped at 75 percent of FAS, exclusive of cost of living increases.

Term of Service	Percent of FAS
15+	3.5%
10-14	3.0%

Death and disability benefits are also provided. Eligibility for death benefits while on active duty requires 10 or more years of service. A monthly spousal benefit is provided which is equal to 50 percent of the benefit that the member would have received if retired. If the member is retired, the surviving spouse receives the greater of 50 percent of the member's retirement benefit or 25 percent of the FAS. For members with 10 or more years of service, a disability benefit of 50 percent of FAS is provided.

Material changes, if any, in JRS benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

Judges' Retirement Fund

The Judges' Retirement Fund was created by the Legislature on March 22, 1937, pursuant to chapter 2.12 RCW, to provide retirement benefits to judges of the Supreme Court, Court of Appeals, or Superior Courts of the state of Washington. Subsequent legislation required that all judges first appointed or elected to office on or after August 1, 1971, enter the Judicial Retirement System. Judges' retirement benefit provisions are established in chapter 2.12 RCW and may be amended only by the Legislature.

The Judges' Retirement Fund is an agent multiple-employer retirement system comprised of a single defined benefit plan. There are currently no active members in this plan. Retirement benefits are financed on a pay-as-you-go basis from a combination of past employee and employer contributions, and a special funding situation in which the state contributes to the plan.

Material changes, if any, in benefit provisions for Judges for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

The Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund

The Volunteer Fire Fighters' Relief Act was created by the Legislature in 1935 and the pension portion of the act was added in 1945. Membership in the system requires volunteer firefighter service with a fire department of an electing municipality of Washington State, emergency work as an emergency medical technician with an emergency medical service district, or work as a commissioned reserve law enforcement officer. Retirement benefits are established in chapter 41.24 RCW and may be amended only by the Legislature.

The Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFFRPF) is a cost-sharing multiple-employer retirement system that provides death and active duty disability benefits to all members, and optional defined benefit pension plan payments.

VFFRPF retirement benefits are financed from a combination of investment earnings, member contributions, municipality contributions, and a special funding situation where the state pays the remaining contributions. Since retirement benefits cover volunteer service, benefits are paid based on years of service not salary. Members are vested after ten years of service. VFFRPF members accrue no interest on contributions and may elect to withdraw their contributions upon termination.

After 25 years of active membership, members having reached the age of 65 and who have paid their annual retirement fee for 25 years are entitled to receive a monthly benefit of $50 plus $10 per year of service. The maximum monthly benefit is $300. Reduced pensions are available for members under the age of 65 or with less than 25 years of service.

Death and active duty disability benefits are provided at no cost to the member. Death benefits in the line of duty consist of a lump sum of $152,000. Funeral and burial expenses are also paid in a lump sum of $2,000 for members on active duty. Members receiving disability benefits at the time of death shall be paid $500.

Members injured while on active duty shall receive disability payments of $2,550 per month for up to six months; thereafter, payments are reduced. Disabled members receive $1,275 per month, their spouse $255, and dependent children $110.

Effective July 1, 2001, the disability income benefits and the maximum survivor benefits under the Relief Plan are increased for increases in the Consumer Price Index.

Effective July 22, 2007, vocational rehabilitation may be paid for disabled members who are unable to return to their previous employment. Members who qualify are subject to a $4,000 maximum limit and are required to follow certain conditions established by the Board and authorized by chapter 41.24 RCW.

Effective June 10, 2010, members of the VFFRPF retirement system with vested pensions who have reached age 65 may, under certain conditions, retire from service, draw their pensions, and return to service. Additional service does not count toward the pension, and members cannot draw disability compensation. Departments opting to allow their members to participate in the retire-rehire program agree to pay for annual physicals and an additional surcharge.

Material changes, if any, in VFFRPF benefit provisions for the fiscal year ended June 30, 2012, are listed in the table at the end of this section.

Material Legislative Changes to Pension Plans

For the Fiscal Year Ended June 30, 2012

System/Plan Affected	Effective Date	Description of the changes
LEOFF Plan 2, PERS, PSERS, SERS, TRS and WSPRS	7/1/11	DRS is required to include the qualifying foregone compensation during the 2011-2013 biennium in the benefits calculation of retiring government employees in LEOFF Plan 2, PERS, PSERS, SERS, TRS and WSPRS. (Chapter 5, Laws of 2011)
PERS, PSERS, SERS, TRS and Higher Education Retirement Plan Supplemental Benefit Fund	7/1/11 – 1/1/12	Multi-faceted legislation that: • Limits to 867 the post-retirement hours that a PERS Plan 1 or TRS Plan 1 retiree may work prior to suspension of the pension benefit. • Applies the return to work provision of the applicable retirement system to higher education positions eligible for Higher Education Retirement Plans (HERPs). • Prohibits higher education institutions and entities from offering participation in a HERP to any newly hired employee that has retired or is eligible to retire from a DRS administered retirement plan. • Provides, for newly hired employees eligible to participate in a HERP, the option at time of hire to participate in PERS Plan 3, TRS Plan 3 or a HERP. • Creates the Higher Education Retirement Plan Supplemental Benefit Fund. • Requires institutions to contribute a percentage of their HERP-covered employees' salary to DRS to be invested by the Washington State Investment Board. These funds are intended to be used to pay required supplemental benefits to eligible HERP retirees. (Chapter 47, Laws of 2011)
PSERS	7/22/11	The employer definition within PSERS is modified to include correctional entities formed by PSERS employers under the Interlocal Cooperation Act (RCW 39.34). (Chapter 68, Laws of 2011)
PERS Plan 3, SERS Plan 3 and TRS Plan 3	7/22/11	The investment option for new employees who default into membership in PERS Plan 3, SERS Plan 3 or TRS Plan 3 by failing to choose a retirement plan within the allotted 90 days is changed from the Total Allocation Portfolio to a Retirement Strategy Fund, based on the member's birth year and an assumed retirement at age 65. (Chapter 80, Laws of 2011)
All systems, plans	6/7/12*	This legislation allows same-gender couples to marry, and automatically converts certain domestic partnerships to marriages unless the couple marries or dissolves the partnership before June 30, 2014. Under the provisions of this bill, survivor benefits may be available to certain members of the state's retirement systems sooner than under current law. (Chapter 3, Laws of 2012) *This law will remain on hold pending the results of a referendum to take place in November, 2012.
WSPRS	6/7/12	Current WSPRS members who have service credit earned as commercial vehicle enforcement officers within PERS Plan 2 may transfer said credit into the WSPRS. The member must pay the full actuarial cost of the transfer. (Chapter 72, Laws of 2012)

VFFRPF	6/7/12	At any time prior to retirement or at the time of retirement, a member of the VFFRPF may purchase retirement pension coverage for years of eligible service prior to the member's enrollment in the system or for years of service credit lost due to the withdrawal of the member's pension fee contributions. A member choosing to purchase such retirement pension coverage must make a contribution to the system equal to the actuarial value of the resulting benefit increase. (Chapter 239, Laws of 2012)
LEOFF, PERS, PSERS, SERS and TRS	6/7/12	This legislation amends the retirement statutes to clarify that governmental contractors are not employers under the system, unless otherwise qualifying, and that the determination of whether an employee/employer relationship has been established shall be based solely on the relationship between the contracted employee and the governmental employer. (Chapter 236, Laws of 2012)
LEOFF Plan 2	6/7/12	The initial timeline to transfer service credit under RCW 41.26.435 is moved from June 30, 2014 to June 30, 2012. (Chapter 248, Laws of 2012)

C. FUNDING POLICIES

With the exception of LEOFF Plan 2, the Legislature provided for minimum contribution rates for all retirement plans (Chapter 561, Laws of 2009). The LEOFF Plan 2 Retirement Board provided for minimum contribution rates for the LEOFF Plan 2. These minimum rates went into effect beginning with the 2011-13 biennium.

As part of Substitute House Bill 2021, the Legislature reduced the Plan 1 UAAL minimum rates starting in 2015 to 3.5 percent in PERS and to 5.75 percent in TRS.

All employers are required to contribute at the level established by the Legislature. The table at the end of this section provides the required contribution rates for all plans (expressed as a percentage of current year covered payroll) at the close of fiscal year 2012.

Public Employees' Retirement System

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

- Plan 1 - Employee contribution rates are established by statute at 6 percent for state agencies and local government unit employees, and at 7.5 percent for state government elected officials.

- Plan 2/3 - The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3.

- Plan 3 – The employee contribution rates range from 5 to 15 percent, based on member choice. Two of the options are graduated rates dependent on the employee's age.

As a result of the implementation of the Judicial Benefit Multiplier (JBM) Program in January 2007, a second tier of employer and employee rates was developed to fund, along with investment earnings, the increased retirement benefits of those justices and judges who participate in the program.

Teachers' Retirement System

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.32 and 41.45 RCW.

- Plan 1 - Employee contribution rates are established by statute at 6 percent for state agencies and local government unit employees, and at 7.5 percent for state elected officials.

- Plan 2/3 – Employer and employee for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3.

- Plan 3 – Employee contribution rates range from 5 to 15 percent, based on member choice. Two of the options are graduated rated dependent on the employee's age.

As a result of the implementation of the Judicial Benefit Multiplier (JBM) Program in January 2007, a second tier of employee rates were developed to fund the increased retirement benefits of those judges who participate in the program.

School Employees' Retirement System

Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 employer contribution rates. The methods used to determine the contribution requirements are established under state statute in chapters 41.35 and 41.45 RCW.

- Plan 2/3 - Employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3.

- Plan 3 - Employee contribution rates range from 5 to 15 percent, based on member choice. Two of the options are graduated dependent on the employee's age.

Law Enforcement Officers' and Fire Fighters' Retirement System

Employer and employee contribution rates are developed by the Office of the State Actuary to fully fund the plans. Starting on July 1, 2000, Plan 1 employers and employees contribute zero percent, as long as the plan remains fully funded. Plan 2 employers and employees are required to pay at the level adopted by the LEOFF Plan 2 Retirement Board. All employers are required to contribute at the level required by state statute.

The Legislature, by means of a special funding arrangement, appropriates money from the state General Fund to supplement the current service liability and fund the prior service costs of Plan 2 in accordance with the recommendations of the Pension Funding Council and the LEOFF Plan 2 Retirement Board.

However, this special funding situation is not mandated by the State Constitution and this funding requirement could be returned to the employers by a change of statute. For fiscal year 2012, the state contributed $52.8 million to LEOFF Plan 2.

Washington State Patrol Retirement System

Each biennium, the state Pension Funding Council adopts the employee and the state contribution rates, subject to revision by the Legislature. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 43.43 and 41.45 RCW.

The preliminary employee and the state contribution rates are developed by the Office of the State Actuary to fully fund the plan. State statute also requires employees to contribute at a rate of at least 4.85 percent.

Public Safety Employees' Retirement System

Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates. The methods used to determine the contribution requirements are established under state statute in chapters 41.37 and 41.45 RCW.

The employer and employee contribution rates for Plan 2 are developed by the Office of the State Actuary to fully fund Plan 2.

Judicial Retirement System

Contributions made are based on rates set in chapter 2.10 RCW. By statute, employees are required to contribute 7.5 percent with an equal amount contributed by the state. In addition, the state guarantees the solvency of the Judicial Retirement System on a pay-as-you-go basis. Each biennium, the Legislature, through biennial appropriations from the state General Fund, contributes amounts sufficient to meet benefit payment requirements. For fiscal year 2012, the state contributed $8.1 million.

Judges' Retirement Fund

Past contributions were made based on rates set in chapter 2.12 RCW. By statute, employees were required to contribute 6.5 percent with an equal amount contributed by the state. However, there are no active members remaining in the Judges' Retirement Fund.

The state guarantees the solvency of the Judges' Retirement Fund on a pay-as-you-go basis. Each biennium, therefore, the Legislature, through appropriations from the state General Fund, contributes amounts sufficient to meet benefit payment requirements. For fiscal year 2012, however, no such appropriations or contributions were needed or made.

The Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund

The retirement provisions of Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFFRPF) are funded through member contributions of $30 per year, varying employer contributions, and 40 percent of the Fire Insurance Premium Tax, as per chapter 41.24 RCW.

Employers consist of fire departments, emergency medical service districts and law enforcement agencies. The contribution rate for fire districts is set by the Legislature and was $30 per member for the years 2011 and 2012. The rate for emergency medical service districts and law enforcement agencies is set each year by the State Board for Volunteer Fire Fighters' and Reserve Officers' Relief and Pension, based on the actual cost of participation as determined by the Office of the State Actuary. For the year 2012, the rate was $90 per member. Employers may opt to pay the member's fee on their behalf.

VFFRPF members earn no interest on contributions and may elect to withdraw their contributions upon termination.

Administrative expenses are funded through fire insurance premium taxes and are maintained in a separate fund. Amounts not needed for administrative expenses are transferred to VFFRPF.

Required contribution rates (expressed as a percentage of current year covered payroll) for all retirement plans at the close of fiscal year 2012 were as follows:

Required Contribution Rates	Employer			Employee		
	Plan 1	Plan 2	Plan 3	Plan 1	Plan 2	Plan 3
PERS						
Members Not Participating in JBM						
State agencies*	7.08%	7.08%	7.08%**	6.00%	4.64%	***
Local governmental units*	7.08%	7.08%	7.08%**	6.00%	4.64%	***
State govt elected officials*	10.54%	7.08%	7.08%**	7.50%	4.64%	***
Members Participating in JBM						
State agencies*	9.58%	9.58%	9.58%**	9.76%	9.10%	7.50%****
Local governmental units*	7.08%	7.08%	7.08%**	12.26%	11.60%	7.50%****
TRS						
Members Not Participating in JBM						
State agencies*	8.04%	8.04%	8.04%**	6.00%	4.69%	***
Local governmental units*	8.04%	8.04%	8.04%**	6.00%	4.69%	***
State govt elected officials*	8.04%	8.04%	8.04%**	7.50%	4.69%	***
Members Participating in JBM						
State agencies*	8.04%	N/A	N/A	9.76%	N/A	N/A
SERS						
State agencies*	N/A	7.58%	7.58%**	N/A	4.09%	***
Local governmental units*	N/A	7.58%	7.58%**	N/A	4.09%	***
LEOFF						
Ports and universities*	N/A	8.62%	N/A	N/A	8.46%	N/A
Local governmental units*	0.16%	5.24%	N/A	N/A	8.46%	N/A
State of Washington	N/A	3.38%	N/A	N/A	N/A	N/A
WSPRS						
State agencies*	8.07%	8.07%	N/A	6.59%	6.59%	N/A
PSERS						
State agencies*	N/A	8.74%	N/A	N/A	6.36%	N/A
Local governmental units*	N/A	8.74%	N/A	N/A	6.36%	N/A
JRS						
State agencies*	7.50%	N/A	N/A	7.50%	N/A	N/A

* Includes an administrative expense rate of 0.16%.
** Plan 3 defined benefit portion only.
*** Variable from 5% to 15% based on rate selected by the member.
**** Minimum rate.
N/A indicates data not available.

D. EMPLOYER CONTRIBUTIONS REQUIRED AND PAID

The following table presents the state of Washington's required contributions in millions of dollars to cost-sharing plans in accordance with the funding policy. All contributions required by the funding method were paid.

Plans	2012	2011	2010
PERS Plan 1	$124.0	$72.3	$78.2
PERS Plan 2/3	182.8	158.0	160.4
TRS Plan 1	3.1	4.4	5.6
TRS Plan 2/3	1.1	0.7	0.8
PSERS Plan 2	7.4	8.0	7.8
LEOFF Plan 2	52.8	52.9	52.2
VFFRPF	5.6	5.7	5.7

There are no long-term contracts for contributions for any of the retirement plans administered by the state.

E. FUNDED STATUS AND FUNDING PROGRESS

The funded status of each plan as of June 30, 2011, the most recent actuarial valuation date, is as follows (dollars in millions):

Plans	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
PERS Plan 1	$ 8,883.4	$ 12,571.2	$ 3,687.8	71%	$ 431.8	854%
PERS Plan 2/3*	20,996.7	21,626.6	629.9	97%	8,148.4	8%
TRS Plan 1	7,485.0	9,231.8	1,746.8	81%	284.2	615%
TRS Plan 2/3*	7,140.6	7,193.8	53.2	99%	4,085.0	1%
SERS Plan 2/3*	2,872.1	2,956.0	83.9	97%	1,490.0	6%
LEOFF Plan 1	5,565.3	4,144.7	(1,420.6)	134%	24.5	0%
LEOFF Plan 2*	6,620.7	5,941.2	(679.5)	111%	1,534.7	0%
WSPRS Plan 1/2*	949.5	859.4	(90.1)	110%	81.5	0%
PSERS Plan 2*	140.7	126.5	(14.2)	111%	232.8	0%
JRS	5.1	109.3	104.2	5%	0.5	22,574%
Judges	2.3	3.9	1.6	61%	-	N/A
VFFRPF	167.8	167.8	-	100%	N/A	N/A

N/A indicates data not applicable.

Note: Figures may not total due to rounding. Percentages are calculated using unrounded totals.

* These plans use the aggregate actuarial cost method which does not identify or separately amortize unfunded actuarial liabilities. For this reason, the information shown above has been prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress of these plans.

Source: Washington State Office of the State Actuary

Defined Benefit Pension Plans Administered by the State

For the Fiscal Year Ended June 30, 2012

The information was determined as part of the actuarial valuations at the dates indicated below. Additional information as of the latest valuation follows.

	PERS Plan 1	PERS Plan 2/3	TRS Plan 1	TRS Plan 2/3	SERS Plan 2/3
Valuation date	6/30/2011	6/30/2011	6/30/2011	6/30/2011	6/30/2011
Actuarial cost method	Entry age normal [1]	Aggregate [2]	Entry age normal [1]	Aggregate [2]	Aggregate [2]
Amortization method					
Funding	Level % [4]	N/A	Level % [4]	N/A	N/A
GASB	Level $	N/A	Level $	N/A	N/A
Remaining amortization years (closed)	10-year rolling	Open plan	10-year rolling	Open plan	Open plan
Remaining amortization period (closed)	N/A	N/A	N/A	N/A	N/A
Asset valuation method	8-year graded smoothed fair value [5]	8-year graded smoothed fair value [5]	8-year graded smoothed fair value [5]	8-year graded smoothed fair value [5]	8-year graded smoothed fair value [5]
Actuarial assumptions					
Investment rate of return [7]	7.90%	7.90%	7.90%	7.90%	7.90%
Projected salary increases					
Salary inflation at 3.75% [8], plus the merit increases described below:					
Initial salary merit (grades down to 0%)	6.1%	6.1%	5.8%	5.8%	6.9%
Merit period (years of service)	17 yrs	17 yrs	26 yrs	26 yrs	20 yrs
Includes inflation at	N/A	3.00%	N/A	3.00%	3.00%
cost of living adjustments	Minimum COLA [6]	CPI increase, maximum 3%	Minimum COLA [6]	CPI increase, maximum 3%	CPI increase, maximum 3%

N/A indicates data not applicable.

[1] PERS and TRS Plans 1 use a variation of the entry age normal (EAN) cost method, whereas LEOFF Plan 1 uses a variation of the frozen initial liability (FIL) cost method.

[2] The aggregate cost method does not identify or separately amortize unfunded actuarial accrued liabilities.

[3] Pay as you go basis for funding.

[4] Level percent of system payroll, including system growth.

[5] Asset Valuation Method - 8 year smoothed fair value: The actuarial value of assets is calculated under an adjusted market value method by starting with the market value of assets. For subsequent years, the actuarial value of assets is determined by adjusting the market value of assets to reflect the difference between the actual investment return and the expected investment return during each of the last 8 years or, if fewer, the completed years since adoption, at the following rates per year (annual recognition). The VFFRPF annual gain/loss is centered around a 7% expected rate of return instead of 8% and LEOFF Plan 2 around 7.5%.

Annual Gain/Loss Rate of Return	Smoothing Period	Annual Recognition	Annual Gain/Loss Rate of Return	Smoothing Period	Annual Recognition
15% and up	8 years	12.50%	6-7%	2 years	50.00%
14-15%	7 years	14.29%	5-6%	3 years	33.33%
13-14%	6 years	16.67%	4-5%	4 years	25.00%
12-13%	5 years	20.00%	3-4%	5 years	20.00%
11-12%	4 years	25.00%	2-3%	6 years	16.67%
10-11%	3 years	33.33%	1-2%	7 years	14.29%
9-10%	2 years	50.00%	1% and lower	8 years	12.50%
7-9%	1 year	100.00%			

LEOFF Plan 1	LEOFF Plan 2	PSERS Plan 2	WSPRS	JRS	Judges	VFFRPF [9]
6/30/2011	6/30/2011	6/30/2011	6/30/2011	6/30/2011	6/30/2011	6/30/2011
Frozen initial liability [1]	Aggregate [2]	Aggregate [2]	Aggregate [2]	Entry age [3]	Entry age [3]	Entry age [9]
Level % [4]	N/A	N/A	N/A	N/A	N/A	Level $
Level $	N/A	N/A	N/A	Level $	Level $	Level $
13	Open plan	Open plan	Open plan	5-year rolling	5-year rolling	Open plan
6/30/2024	N/A	N/A	N/A	N/A	N/A	15-year rolling
8-year graded smoothed fair value [5]	8-year graded smoothed fair value [5]	8-year graded smoothed fair value [5]	8-year graded smoothed fair value [5]	Market	Market	8-year graded smoothed fair value [5]
7.90%	7.50%	7.90%	7.90%	4.00%	4.00%	7.00%
11.0%	11.0%	6.1%	7.1%	0.0%	0.0%	N/A
21 yrs	21 yrs	17 yrs	26 yrs	N/A	N/A	N/A
3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	N/A
CPI increase	CPI increase maximum 3%	CPI increase, maximum 3%	CPI increase, maximum 3%	CPI increase, maximum 3%	None	None

[6] The PERS Plan 1 and TRS Plan 1 COLA: Qualifying retirees receive an increase in their monthly benefit once a year. The COLA on minimum benefit levels is calculated as the last unrounded minimum COLA amount increased by 3%, rounded to the nearest penny. These are some historical monthly COLA amounts per year of service:

Date	COLA Type	Amount
7/1/2002	Uniform	$1.14
7/1/2003	Uniform	$1.18
7/1/2004	Uniform	$1.21
7/1/2005	Uniform	$1.25
7/1/2006	Uniform	$1.29
7/1/2007	Uniform	$1.33
7/1/2008	Uniform	$1.73
7/1/2009	Uniform	$1.83
7/1/2010	Uniform	$1.88
7/1/2011	Minimum	$1.94
7/1/2012	Minimum	$2.00

[7] The Legislature prescribes the assumed rate of investment return for all plans except Judicial, Judges, and VFFRPF.

[8] WSPRS also assumes a variable salary merit increase for a merit period of 25 years.

[9] VFFRPF uses the entry age funding method for pensions, and the aggregate funding method for the relief costs.

F. ANNUAL PENSION COST AND OTHER RELATED INFORMATION

Current year annual pension cost, net pension obligation (NPO) and related information for the current year for the state's single employer and agent multiple-employer defined benefit plans are as follows (dollars in millions):

Annual Pension Cost and Net Pension Obligation	WSPRS	JRS	Judges
Annual required contribution	$2.9	$22.6	$0.3
Interest on NPO	(1.1)	2.7	(0.0)
Adjustment to annual required contribution	1.8	(14.8)	0.2
Annual pension cost	3.6	10.5	0.4
Less: Contributions made	6.5	8.1	0.0
Increase (decrease) in NPO	(2.9)	2.4	0.4
NPO at beginning of year	(13.9)*	68.6	(0.8)
NPO at end of year	$(16.8)	$71.0	$(0.4)

*Amount restated from prior year's CAFR.

G. THREE YEAR HISTORICAL TREND INFORMATION

The following table presents three-year trend information for the state's single employer and agent multiple-employer defined benefit plans (dollars in millions):

Single and Agent Employer Plans	2012	2011	2010
WSPRS			
Annual pension cost	$3.6	$2.8*	$7.1
% of APC contributed	180.6	187.5*	74.2
NPO	$(16.8)	$(13.9)*	$(11.4)
JRS			
Annual pension cost	$10.5	$7.7	$9.1
% of APC contributed	77.1	141.6	127.5
NPO	$71.0	$68.6	$71.8
Judges			
Annual pension cost	$0.4	$0.3	$0.2
% of APC contributed	0.0	0.0	0.0
NPO	$(0.4)	$(0.8)	$(1.1)

*Amounts restated from prior year's CAFR.

There are no long-term contracts for contributions for any of the retirement plans administered by the state.

H. CHANGES IN ACTUARIAL ASSUMPTIONS AND METHODS

The assumed return on investment earnings was decreased from 8.0 percent for all plans to 7.9 percent (7.5 percent for LEOFF Plan 2).

The assumed general salary growth was decreased from 4.0 percent for all plans to 3.75 percent (4.5 percent for LEOFF Plan 2).

The assumed rate of inflation was decreased from 3.5 percent to 3.0 percent for all plans.

The assumed system growth was decreased from 1.25 percent (0.90 percent for TRS plans) to 0.95 percent (0.80 percent for TRS plans), while the LEOFF plans remained at 1.25 percent.

The medical inflation assumption associated with non-pension benefits payable to members and survivors in LEOFF and WSPRS plans was changed.

I. CHANGES IN BENEFIT PROVISIONS

Effective June 30, 2011, the automatic annual benefit increase for retirees/beneficiaries in PERS Plan 1 and TRS Plan 1 were eliminated, and the Adjusted Minimum Benefit limit was increased to $1,545 per month. Additionally, the minimum employer contribution rates for the unfunded liability of both of these plans were lowered.

J. DEFINED CONTRIBUTION PLANS

Public Employees' Retirement System Plan 3

The Public Employees' Retirement System (PERS) Plan 3 is a combination defined benefit/defined contribution plan administered by the state through the Department of Retirement Systems (DRS). Refer to section B of this note for PERS plan descriptions.

PERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. As established by chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5 to 15 percent of salaries, based on member choice. There are currently no requirements for employer contributions to the defined contribution component of PERS Plan 3.

PERS Plan 3 defined contribution retirement benefits are dependent upon the results of investment activities. Members may elect to self-direct the investment of their contributions. Any expenses incurred in conjunction with self-directed investments are paid by members. Absent a member's self-direction, PERS Plan 3 investments are made in the same portfolio as that of the PERS Plan 2/3 defined benefit plan.

For fiscal year 2012, covered payroll was $1.45 billion, employee contributions required and made were $95.2 million, and plan refunds paid out were $66.2 million.

Teachers' Retirement System Plan 3

The Teachers' Retirement System (TRS) Plan 3 is a combination defined benefit/defined contribution plan administered by the state through the Department of Retirement Systems (DRS). Refer to section B of this note for TRS plan descriptions.

TRS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. As established by chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5 to 15 percent of salaries, based on member choice. There are currently no requirements for employer contributions to the defined contribution component of TRS Plan 3.

TRS Plan 3 defined contribution retirement benefits are dependent upon the results of investment activities. Members may elect to self-direct the investment of their contributions. Any expenses incurred in conjunction with self-directed investments are paid by members. Absent a member's self-direction, TRS Plan 3 investments are made in the same portfolio as that of the TRS Plan 2/3 defined benefit plan.

For fiscal year 2012, covered payroll was $3.38 billion, employee contributions required and made were $255.9 million and plan refunds paid out were $150.4 million.

School Employees' Retirement System Plan 3

The School Employees' Retirement System (SERS) Plan 3 is a combination defined benefit/defined contribution plan administered by the state through the Department of Retirement Systems (DRS). Refer to section B of this note for SERS plan descriptions.

SERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. As established by chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5 to 15 percent of salaries, based on member choice. There are currently no requirements for employer contributions to the defined contribution component of SERS Plan 3.
SERS Plan 3 defined contribution retirement benefits are dependent upon the results of investment activities.

Members may elect to self-direct the investment of their contributions. Any expenses incurred in conjunction with self-directed investments are paid by members. Absent a member's self-direction, SERS Plan 3 investments are made in the same portfolio as that of the SERS Plan 2/3 defined benefit plan.

For fiscal year 2012, covered payroll was $898.8 million, employee contributions required and made were $59.0 million and plan refunds paid out were $60.9 million.

Judicial Retirement Account

The Judicial Retirement Account (JRA) Plan was established by the Legislature in 1988 to provide supplemental retirement benefits. It is a defined contribution plan administered by the state Administrative Office of the Courts, under the direction of the Board for Judicial Administration. Membership includes judges elected or appointed to the Supreme Court, Court of Appeals, and Superior Courts, and who are members of PERS for their services as a judge. Vesting is full and immediate. There are three participating employers in JRA.

From January 1, 2007 through December 31, 2007, any judicial members of the Public Employees' Retirement System (PERS) and the Teachers' Retirement System (TRS) eligible to participate in JRA were able to make a one-time irrevocable election to discontinue future contributions to JRA, in lieu of prospective contributions to the Judicial Benefit Multiplier Program (JBM). Beginning January 1, 2007, any newly elected or appointed Supreme Court justice, Court of Appeals judge or Superior Court judge could no longer participate in JRA and would be enrolled in the JBM Program (enacted in 2006).

JRA plan members are required to contribute 2.5 percent of covered salary. The state, as employer, contributes an equal amount on a monthly basis. The employer and employee obligations to contribute are established per chapter 2.14 RCW. Plan provisions and contribution requirements are established in state statute and may be amended only by the Legislature.

A JRA member who separates from judicial service for any reason is entitled to receive a lump-sum distribution of the accumulated contributions. The administrator of JRA may adopt rules establishing other payment options. If a member dies, the amount of accumulated contributions standing to the member's credit at the time of the member's death is to be paid to the member's estate, or such person or persons, trust or organization as the member has nominated by written designation.

For fiscal year 2012, covered payroll was $1.4 million and the contribution requirement was $76 thousand. Actual employer and employee contributions were $38 and $38 thousand respectively. Plan benefits paid out for fiscal year 2012 totaled $811 thousand.

The Administrator of JRA has entered an agreement with DRS for accounting and reporting services, and the Washington State Investment Board (SIB) for investment services. Under this agreement, DRS is responsible for all record keeping, accounting, and reporting of member accounts and the WSIB is granted the full power to establish investment policy, develop participant investment options and manage the investment funds for the JRA plan, consistent with the provisions of RCW 2.14.080 and 43.84.150.

Higher Education Retirement Plans

The Higher Education Retirement Plans are privately administered defined contribution plans with a supplemental defined benefit plan component. As authorized by chapter 28B.10 RCW, the plans cover higher education faculty and other positions as designated by each institution. The state and regional universities, the state college, and the state community and technical colleges each participate in a plan. Effective June 2010, eligible employees of the Higher Education Coordinating Board have the ability to participate in the Higher Education Retirement Plan instead of the Public Employees' Retirement System.

Contributions to the plans are invested in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Benefits from fund sponsors are available upon separation or retirement at the member's option. Employees have, at all times, a 100 percent vested interest in their accumulations.

RCW 28.B.10.400 et. seq. assigns the authority to establish and amend benefit provisions to: the board of regents of the state universities, the boards of trustees of the regional universities and the state college, and the state board for community colleges.

Employee contribution rates, based on age, range from 5 to 10 percent of salary. The employers match the employee contributions. The employer and employee obligations to contribute are established per chapter 28B.10 RCW.

Effective July 29, 2009, domestic partners registered with the state will be treated the same as married spouses, to the extent that treatment is not in conflict with federal laws.

For fiscal year 2012, covered payroll was $1.96 billion. Employer and employee contributions were $165.6 and $165.6 million respectively, for a total of $331.2 million. These contribution amounts represent approximately 8.4 percent each of covered payroll for employers and employees.

The plans have a supplemental payment component which guarantees a minimum retirement benefit based upon a one-time calculation at each employee's retirement date. Institutions make direct payments to qualifying retirees when the retirement benefits provided by the fund sponsors do not meet the benefit goals. The supplemental component is financed on a pay-as-you-go basis.

An actuarial valuation of the supplemental component of the Higher Education Retirement plans was done at the end of fiscal year 2011. The previous valuation was performed in 2009.

The Unfunded Actuarial Accrued Liability (UAAL) calculated as of June 30, 2011, and 2009, was $357.4 million and $336.5 million, respectively, and is amortized over a 13 year period. The Annual Required Contribution (ARC) of $49.8 million consists of amortization of the UAL ($28.9 million) and normal cost (or current cost) ($19.9 million).

The UAL and ARC were established using the entry age normal cost method. The actuarial assumptions included an investment rate of return of 4.3 to 8 percent and projected salary increases ranging from 2 to 4 percent. Approximately $1.91 billion and $1.79 billion of payroll were covered under these plans during 2011 and 2009, respectively.

A 0.25 percent of pay employer contribution rate was initiated in January 1, 2012 for employees covered by higher education retirement plans. The contributions are deposited in the Higher Education Retirement Plan Supplemental Benefit Fund administered by the Department of Retirement Systems and invested by the State Investment Board. The contribution rate increases to 0.5 percent of pay beginning January 1, 2013.

The following table reflects the activity in the Net Pension Obligation (NPO) for the years ended June 30 (expressed in millions):

Net Pension Obligation	2012	2011	2010
Annual required contribution	$ 49.8	$ 49.8	$ 43.5
Payments to beneficiaries	(4.1)	(3.7)	(3.7)
Increase (decrease) in NPO	45.7	46.1	39.8
NPO at beginning of year	165.7	119.6	79.8
NPO at end of year	$211.4	$165.7	$119.6

K. PLAN NET ASSETS AND CHANGES IN PLAN NET ASSETS

The Combining Statement of Plan Net Assets that follows presents the principal components of receivables, investments, and liabilities. The Combining Statement of Changes in Plan Net Assets presents the additions and deductions to plan net assets.

Combining Statement of Plan Net Assets
Pension and Other Employee Benefit Funds

June 30, 2012

(expressed in thousands)

continued

	PERS Plan 1	PERS Plan 2/3 Defined Benefit	PERS Plan 3 Defined Contribution	TRS Plan 1	TRS Plan 2/3 Defined Benefit
ASSETS					
Cash and pooled investments	$ 656	$ 4,405	$ 240	$ 1,160	$ 5,013
Receivables:					
Employer accounts receivable	4,144	46,269	4,681	2,436	25,362
Member accounts receivable (net of allowance)	752	180	-	464	23
Due from other funds	-	-	-	-	-
Due from other pension and other employee benefit funds	-	420	240	-	2,705
Interest and dividends	21,598	60,313	2,904	18,130	20,614
Investment trades pending	127,579	356,587	17,171	107,104	121,847
Total Receivables	154,073	463,769	24,996	128,134	170,551
Investments, Noncurrent:					
Public equity	2,673,213	7,471,712	1,084,388	2,244,179	2,553,113
Fixed income	1,500,936	4,195,153	202,015	1,260,045	1,433,495
Private equity	1,920,747	5,368,536	258,518	1,612,479	1,834,443
Real estate	1,026,165	2,868,158	138,114	861,472	980,057
Liquidity	173,322	492,426	27,794	145,422	173,472
Tangible assets	99,432	277,915	13,383	83,474	94,964
Total Investments, Noncurrent	7,393,815	20,673,900	1,724,212	6,207,071	7,069,544
Total Assets	7,548,544	21,142,074	1,749,448	6,336,365	7,245,108
LIABILITIES					
Accrued liabilities	171,320	462,438	25,021	144,452	157,947
Due to other funds	67	689	-	27	385
Due to other pension and other employee benefit funds	2,962	240	-	2,475	-
Unearned revenues	59	412	-	167	9
Total Liabilities	174,408	463,779	25,021	147,121	158,341
NET ASSETS					
Net assets held in trust for:					
Pension Benefits (Schedule of Funding Progress by Plan begins on Page 167)	7,374,136	20,678,295	1,724,427	6,189,244	7,086,767
Deferred compensation participants	-	-	-	-	-
Total Net Assets	$ 7,374,136	$ 20,678,295	$ 1,724,427	$ 6,189,244	$ 7,086,767

Combining Statement of Plan Net Assets
Pension and Other Employee Benefit Funds

June 30, 2012

(expressed in thousands)

continued

	TRS Plan 3 Defined Contribution	SERS Plan 2/3 Defined Benefit	SERS Plan 3 Defined Contribution	LEOFF Plan 1	LEOFF Plan 2
ASSETS					
Cash and pooled investments	$ 4,268	$ 3,499	$ 995	$ 229	$ 995
Receivables:					
Employer accounts receivable	22,427	9,774	5,122	-	16,995
Member accounts receivable (net of allowance)	-	9	-	73	50
Due from other funds	-	-	-	-	8
Due from other pension and other employee benefit funds	-	2,677	-	-	-
Interest and dividends	9,051	8,222	2,742	14,348	19,342
Investment trades pending	53,523	48,598	16,214	84,791	114,351
Total Receivables	85,001	69,280	24,078	99,212	150,746
Investments, Noncurrent:					
Public equity	3,163,308	1,018,291	673,503	1,776,663	2,396,046
Fixed income	629,680	571,737	190,759	997,547	1,345,314
Private equity	805,802	731,651	244,114	1,276,561	1,721,597
Real estate	430,502	390,887	130,419	682,007	919,769
Liquidity	84,910	67,320	25,078	114,793	165,159
Tangible assets	41,714	37,876	12,637	66,084	89,123
Total Investments, Noncurrent	5,155,916	2,817,762	1,276,510	4,913,655	6,637,008
Total Assets	5,245,185	2,890,541	1,301,583	5,013,096	6,788,749
LIABILITIES					
Accrued liabilities	74,106	63,122	23,596	109,890	147,861
Due to other funds	-	140	-	12	164
Due to other pension and other employee benefit funds	230	-	140	-	-
Unearned revenues	-	5	-	-	227
Total Liabilities	74,336	63,267	23,736	109,902	148,252
NET ASSETS					
Net assets held in trust for:					
Pension Benefits	5,170,849	2,827,274	1,277,847	4,903,194	6,640,497
(Schedule of Funding Progress by Plan begins on Page 167)					
Deferred compensation participants	-	-	-	-	-
Total Net Assets	$ 5,170,849	$ 2,827,274	$ 1,277,847	$ 4,903,194	$ 6,640,497

Combining Statement of Plan Net Assets
Pension and Other Employee Benefit Funds

June 30, 2012

(expressed in thousands)

continued

	WSPRS Plan 1/2	PSERS Plan 2	JRS	JRA	Judges
ASSETS					
Cash and pooled investments	$ 629	$ 252	$ 3,490	$ 9	$ 1,869
Receivables:					
Employer accounts receivable	504	1,925	2	-	-
Member accounts receivable (net of allowance)	2	-	2	2	-
Due from other funds	-	-	-	-	-
Due from other pension and other employee benefit funds	-	5	-	-	-
Interest and dividends	2,569	497	-	-	-
Investment trades pending	15,186	2,938	-	-	-
Total Receivables	18,261	5,365	4	2	-
Investments, Noncurrent:					
Public equity	318,183	61,557	-	12,257	-
Fixed income	178,650	34,562	-	-	-
Private equity	228,619	44,229	-	-	-
Real estate	122,141	23,630	-	-	-
Liquidity	20,622	6,374	5	-	3
Tangible assets	11,835	2,290	-	-	-
Total Investments, Noncurrent	880,050	172,642	5	12,257	3
Total Assets	898,940	178,259	3,499	12,268	1,872
LIABILITIES					
Accrued liabilities	19,834	3,793	31	-	2
Due to other funds	18	20	-	-	-
Due to other pension and other employee benefit funds	-	-	-	-	-
Unearned revenues	4	-	-	-	-
Total Liabilities	19,856	3,813	31	-	2
NET ASSETS					
Net assets held in trust for:					
Pension Benefits (Schedule of Funding Progress by Plan begins on Page 167)	879,084	174,446	3,468	12,268	1,870
Deferred compensation participants	-	-	-	-	-
Total Net Assets	$ 879,084	$ 174,446	$ 3,468	$ 12,268	$ 1,870

Combining Statement of Plan Net Assets
Pension and Other Employee Benefit Funds

June 30, 2012
(expressed in thousands)

concluded

	VFFRPF	Deferred Compensation	Higher Ed Supplemental	Total
ASSETS				
Cash and pooled investments	$ 13,495	$ 2,611	$ 14	$ 43,829
Receivables:				
Employer accounts receivable	-	-	479	140,120
Member accounts receivable (net of allowance)	-	1,555	-	3,112
Due from other funds	-	-	-	8
Due from other pension and other employee benefit funds	-	-	-	6,047
Interest and dividends	440	-	6	180,776
Investment trades pending	2,601	-	34	1,068,524
Total Receivables	3,041	1,555	519	1,398,587
Investments, Noncurrent:				
Public equity	54,509	2,931,869	711	28,433,502
Fixed income	30,605	-	399	12,570,897
Private equity	39,166	-	511	16,086,973
Real estate	20,924	-	273	8,594,518
Liquidity	3,450	4	529	1,500,683
Tangible assets	2,027	-	27	832,781
Total Investments, Noncurrent	150,681	2,931,873	2,450	68,019,354
Total Assets	167,217	2,936,039	2,983	69,461,770
LIABILITIES				
Accrued liabilities	3,371	1,762	44	1,408,590
Due to other funds	4	-	-	1,526
Due to other pension and other employee benefit funds	-	-	-	6,047
Unearned revenues	-	-	-	883
Total Liabilities	3,375	1,762	44	1,417,046
NET ASSETS				
Net assets held in trust for:				
Pension Benefits (Schedule of Funding Progress by Plan begins on Page 167)	163,842	-	2,939	65,110,447
Deferred compensation participants	-	2,934,277	-	2,934,277
Total Net Assets	$ 163,842	$ 2,934,277	$ 2,939	$ 68,044,724

Combining Statement of Changes in Plan Net Assets
Pension and Other Employee Benefit Funds

For the Fiscal Year Ended June 30, 2012

(expressed in thousands)

continued

	PERS Plan 1	PERS Plan 2/3 Defined Benefit	PERS Plan 3 Defined Contribution	TRS Plan 1	TRS Plan 2/3 Defined Benefit
ADDITIONS					
Contributions:					
Employers	$ 257,196	$ 385,253	$ -	$ 111,937	$ 213,852
Members	31,601	326,129	95,172	17,820	31,175
State	-	-	-	-	-
Participants	-	-	-	-	-
Total Contributions	288,797	711,382	95,172	129,757	245,027
Investment Income:					
Net appreciation (depreciation) in fair value	(68,907)	(125,498)	(14,778)	(57,185)	(42,948)
Interest and dividends	187,954	495,364	24,908	157,833	168,836
Less: investment expenses	(32,680)	(85,208)	(4,755)	(27,450)	(29,490)
Net investment income (loss)	86,367	284,658	5,375	73,198	96,398
Transfers from other pension plans	97	270	1,432	38	16
Other additions	-	-	-	-	-
Total Additions	375,261	996,310	101,979	202,993	341,441
DEDUCTIONS					
Pension benefits	1,173,683	377,000	321	913,864	91,400
Pension refunds	4,554	35,715	66,245	1,552	2,170
Transfers to other pension plans	-	1,376	338	-	213
Administrative expenses	659	650	-	293	89
Distributions to participants	-	-	-	-	-
Total Deductions	1,178,896	414,741	66,904	915,709	93,872
Net Increase (Decrease)	(803,635)	581,569	35,075	(712,716)	247,569
Net Assets - Beginning	8,177,771	20,096,726	1,689,352	6,901,960	6,839,198
Net Assets - Ending	$ 7,374,136	$ 20,678,295	$ 1,724,427	$ 6,189,244	$ 7,086,767

Combining Statement of Changes in Plan Net Assets
Pension and Other Employee Benefit Funds

For the Fiscal Year Ended June 30, 2012

(expressed in thousands)

continued

	TRS Plan 3 Defined Contribution	SERS Plan 2/3 Defined Benefit	SERS Plan 3 Defined Contribution	LEOFF Plan 1	LEOFF Plan 2
ADDITIONS					
Contributions:					
Employers	$ -	$ 74,640	$ -	$ 3	$ 80,480
Members	255,867	24,316	59,022	1,410	139,119
State	-	-	-	-	52,770
Participants	-	-	-	-	-
Total Contributions	255,867	98,956	59,022	1,413	272,369
Investment Income:					
Net appreciation (depreciation) in fair value	(27,593)	(17,300)	(8,731)	(39,971)	(38,039)
Interest and dividends	76,096	67,492	23,235	122,274	158,003
Less: investment expenses	(14,438)	(11,744)	(4,132)	(21,157)	(27,101)
Net investment income (loss)	34,065	38,448	10,372	61,146	92,863
Transfers from other pension plans	618	11	407	-	10
Other additions	-	-	-	-	-
Total Additions	290,550	137,415	69,801	62,559	365,242
DEDUCTIONS					
Pension benefits	1,150	53,630	302	343,438	78,152
Pension refunds	150,404	2,516	60,929	435	11,214
Transfers to other pension plans	520	306	163	-	44
Administrative expenses	-	59	-	162	1,095
Distributions to participants	-	-	-	-	-
Total Deductions	152,074	56,511	61,394	344,035	90,505
Net Increase (Decrease)	138,476	80,904	8,407	(281,476)	274,737
Net Assets - Beginning	5,032,373	2,746,370	1,269,440	5,184,670	6,365,760
Net Assets - Ending	$ 5,170,849	$ 2,827,274	$ 1,277,847	$ 4,903,194	$ 6,640,497

Combining Statement of Changes in Plan Net Assets
Pension and Other Employee Benefit Funds

For the Fiscal Year Ended June 30, 2012
(expressed in thousands)

continued

	WSPRS Plan 1/2	PSERS Plan 2	JRS	JRA	Judges
ADDITIONS					
Contributions:					
Employers	$ 6,454	$ 15,285	$ 31	$ 38	$ -
Members	7,030	15,298	31	38	-
State	-	-	8,100	-	-
Participants	-	-	-	-	-
Total Contributions	13,484	30,583	8,162	76	-
Investment Income:					
Net appreciation (depreciation) in fair value	(6,345)	(388)	6	(136)	5
Interest and dividends	21,535	3,811	13	126	13
Less: investment expenses	(3,712)	(647)	(8)	(18)	-
Net investment income (loss)	11,478	2,776	11	(28)	18
Transfers from other pension plans	53	8	-	-	-
Other additions	-	-	-	4	-
Total Additions	25,015	33,367	8,173	52	18
DEDUCTIONS					
Pension benefits	40,368	70	9,765	811	482
Pension refunds	262	1,920	-	-	-
Transfers to other pension plans	-	-	-	-	-
Administrative expenses	50	4	-	-	-
Distributions to participants	-	-	-	-	-
Total Deductions	40,680	1,994	9,765	811	482
Net Increase (Decrease)	(15,665)	31,373	(1,592)	(759)	(464)
Net Assets - Beginning	894,749	143,073	5,060	13,027	2,334
Net Assets - Ending	$ 879,084	$ 174,446	$ 3,468	$ 12,268	$ 1,870

Combining Statement of Changes in Plan Net Assets
Pension and Other Employee Benefit Funds

For the Fiscal Year Ended June 30, 2012
(expressed in thousands)

concluded

	VFFRPF	Deferred Compensation	Higher Ed Supplemental	Total
ADDITIONS				
Contributions:				
Employers	$ 882	$ -	$ 2,935	$ 1,148,986
Members	88	-	-	1,004,116
State	5,602	-	-	66,472
Participants	-	178,449	-	178,449
Total Contributions	6,572	178,449	2,935	2,398,023
Investment Income:				
Net appreciation (depreciation) in fair value	(933)	(34,609)	(6)	(483,356)
Interest and dividends	3,730	26,474	12	1,537,709
Less: investment expenses	(625)	(4,171)	(2)	(267,338)
Net investment income (loss)	2,172	(12,306)	4	787,015
Transfers from other pension plans	-	-	-	2,960
Other additions	-	794	-	798
Total Additions	8,744	166,937	2,939	3,188,796
DEDUCTIONS				
Pension benefits	9,907	-	-	3,094,343
Pension refunds	12	-	-	337,928
Transfers to other pension plans	-	-	-	2,960
Administrative expenses	1,255	-	-	4,316
Distributions to participants	-	171,740	-	171,740
Total Deductions	11,174	171,740	-	3,611,287
Net Increase (Decrease)	(2,430)	(4,803)	2,939	(422,491)
Net Assets - Beginning	166,272	2,939,080	-	68,467,215
Net Assets - Ending	$ 163,842	$ 2,934,277	$ 2,939	$ 68,044,724

Note 12
Other Postemployment Benefits

Plan Description and Funding Policy

In addition to pension benefits as described in Note 11, the state, through the Health Care Authority (HCA), administers an agent multiple-employer other postemployment benefit plan (OPEB). Per RCW 41.05.065, the Public Employees Benefits Board (PEBB) created within the Health Care Authority, is authorized to design benefits and determine the terms and conditions of employee and retired employee participation and coverage, including establishment of eligibility criteria for both active and retired employees. PEBB programs include medical, dental, life and long-term disability.

Employers participating in the PEBB plan include the state (which includes general government agencies and higher education institutions), 54 of the state's K-12 schools and educational service districts (ESDs) and 207 political subdivisions and tribal governments. Additionally, the PEBB plan is available to the retirees of the remaining 246 K-12 schools and ESDs. As of June 2012, membership in the PEBB plan consisted of the following:

	Active Employees	Retirees [1]	Total
State	106,255	27,807	134,062
K-12 schools and ESDs [2]	1,800	29,245	31,045
Political subdivisions	11,375	1,261	12,636
Total	119,430	58,313	177,743

[1] Retirees include retired employees, surviving spouses, and terminated members entitled to a benefit.
[2] In fiscal year 2012, there were 98,349 full-time equivalent active employees in the 246 K-12 schools and ESDs that elected to limit participation in PEBB only to their retirees.

For fiscal year 2012, the estimated monthly cost for PEBB benefits for active employees (average across all plans and tiers) is as follows:

Required Premium [3]	
Medical	$880
Dental	83
Life	5
Long-term disability	2
Total	$970
Employer contribution	$852
Employee contribution	118
Total	$970

[3] Per 2012 Index Rate Model 3.60.

The relationship between the PEBB OPEB plan and its member employers and their employees and retirees is not formalized in a contract or plan document. Rather, the benefits are provided in accordance with a substantive plan. A substantive plan is one in which the plan terms are understood by the employers and plan members. This understanding is based on communications between the HCA, employers and plan members and the historical pattern of practice with regard to the sharing of benefit costs.

The PEBB retiree OPEB plan is available to employees who elect to continue coverage and pay the administratively established premiums at the time they retire under the provisions of the retirement system to which they belong. Retirees' access to PEBB plans depends on the retirement eligibility of their respective retirement system. PEBB members are covered in the following retirement systems: PERS, PSERS, TRS, SERS, WSPRS, and Higher Education.

Per RCW 41.05.022, retirees who are not yet eligible for Medicare benefits may continue participation in the state's non-Medicare community-rated health insurance risk pool on a self-pay basis. Retirees in the non-Medicare risk pool receive an implicit subsidy. The implicit subsidy exists because retired members pay a premium based on a claims experience for active employees and other non-Medicare retirees. The subsidy is valued using the difference between the age-based claims costs and the premium. In calendar year 2011, the average weighted implicit subsidy was valued at $301 per member per month, and in calendar year 2012, the average weighted implicit subsidy is projected to be $326 per member per month.

Retirees who are enrolled in both Parts A and B of Medicare may participate in the state's Medicare community-rated health insurance risk pool. Medicare retirees receive an explicit subsidy in the form of reduced premiums. Annually, the Health Care Authority administrator recommends an amount for the next calendar year's explicit subsidy for inclusion in the Governor's budget. In calendar year 2011, the explicit subsidy was $183 per member per month, and in calendar year 2012, the explicit subsidy is $150 per member per month.

Retirees participating in the PEBB life insurance program received an explicit subsidy of $5 per member per month in calendar year 2011. The retiree subsidy of life insurance was eliminated effective January 2012.

Administrative costs as well as implicit and explicit subsidies are funded by required contributions from participating employers. The subsidies provide monetary assistance for medical and life insurance benefits.

Contributions are set each biennium as part of the budget process. In fiscal year 2012, the cost of the subsidies was approximately 6.5 percent of the cost of benefits for active employees. The benefits are funded on a pay-as-you-go basis.

Each participating employer in the plan is required to disclose additional information with regard to funding policy, the employer's annual OPEB costs and contributions made, the funded status and funding progress of the employers individual plan and actuarial methods and assumptions used.

The PEBB OPEB plan is accounted for as an agency fund on an accrual basis. The plan has no investments or other assets. The PEBB OPEB plan does not issue a publicly available financial report.

For information on the results of an actuarial valuation of the employer provided subsidies associated with the PEBB plan, refer to: http://osa.leg.wa.gov/Actuarial_services/OPEB/OPEB.htm.

Annual OPEB Cost and Net OPEB Obligation

The state's (general government agencies and higher education institutions) annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC) of the state as the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45.

The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

The following tables show the components of the state's annual OPEB cost for fiscal year 2012, the amount contributed to the plan, and changes in the state's Net OPEB Obligation (NOO) (expressed in thousands):

Annual required contribution	$ 320,991
Interest on Net OPEB Obligation	46,250
Amortization of Net OPEB Obligation	(36,954)
Annual OPEB cost (expense)	330,286
Contributions made	(78,673)
Increase in Net OPEB Obligation	251,613
Net OPEB Obligation - beginning of year	1,027,767
Net OPEB Obligation - end of year*	$1,279,381
*estimated	

The state's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB Significant methods and assumptions were as follows: obligation for fiscal years 2010, 2011 and 2012 were as follows (expressed in thousands):

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
6/30/12	$330,286	23.8%	$1,279,381
6/30/11	328,568	23.9%	1,027,767
6/30/10	354,420	19.8%	777,872

Funded Status and Funding Progress

The funded status of the plan as of January 1, 2011, the latest date for which information is available, was as follows (expressed in thousands):

Actuarial accrued liability (AAL)	$3,491,970
Actuarial value of plan assets	-
Unfunded actuarial accrued liability (UAAL)	$3,491,970
Funded ratio (actuarial value of plan assets/AAL)	0.00%
Covered payroll (active plan members)	$5,937,061
UAAL as a percentage of covered payroll	58.8%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the terms of the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

Actuarial valuation date	January 1, 2011
Actuarial cost method	Projected Unit Credit (PUC)
Amortization method	Closed, level percentage of projected payroll amortization method
Remaining amortization period	30 years
Asset valuation method	N/A - no assets
Actuarial assumptions:	
Investment rate of return	4.5%
Projected salary increases	4.0%
Health care inflation rate	7.0% initial rate, 5% ultimate rate in 2083
Inflation rate	3.5%

In addition to the assumptions above, several factors also significantly contributed to the actuarial results. The PEBB voted to permanently eliminate the subsidy paid for life insurance premiums beginning in January 2012. Also in January 2012, explicit subsidies for retirees enrolled in Medicare Parts A and B were reduced from $183 per month to $150 per month.

Note 13

Commitments and Contingencies

A. CONSTRUCTION AND OTHER COMMITMENTS

Capital Commitments

Outstanding commitments related to state infrastructure and facility construction, improvement, and/or renovation totaled $5.04 billion at June 30, 2012.

Encumbrances

Encumbrances, which represent commitments related to unperformed contracts for goods or services, are included in restricted, committed or assigned fund balance, as appropriate. Operating encumbrances lapse at the end of the applicable appropriation. Capital outlay encumbrances lapse at the end of the biennium unless reappropriated by the Legislature in the ensuing biennium. Encumbrances outstanding against continuing appropriations at the end of fiscal year 2012 are (in thousands):

General Fund	$ 1,581
Higher Education Special Revenue Fund	169
Nonmajor Governmental Funds	21,223

B. SUMMARY OF SIGNIFICANT LITIGATION

Pending Litigation

The state and its agencies are parties to numerous routine legal proceedings that normally occur in governmental operations. In addition, at any given point, there may be numerous lawsuits involving the implementation, reduction, or elimination of specific state programs that could significantly impact expenditures, revenues, and potentially have future budgetary impact. This summary considers significant litigation not covered by tort insurance. Tort case liabilities are disclosed in Note 7E, Claims and Judgments, Risk Management.

The state is the defendant in a number of cases alleging inadequate funding of state programs or services. Claims include: funding inadequacies and inequities in basic education; inadequate funding for care of foster children, the disabled and elderly, and inadequate funding for the provision of, daily personal care, medical and mental health services to children, the elderly and the disabled. Collective claims in these programmatic and service cases exceed $650 million exclusive of the basic education case, which could be substantial but is difficult to quantify at this juncture. In addition, adverse rulings in some of these cases could result in significant future costs.

The state is also a defendant in a number of cases contesting: the denial of health care benefits to seasonal and part-time state employees; the methodologies used to calculate reimbursement rates to certain health care providers, and the scope of covered care. Claims in this category exceed $258 million.

The Department of Revenue routinely has claims for refunds in various stages of administrative and legal review. Cases involving claims for refunds currently total approximately $95 million, though an adverse ruling could result in additional claims being brought by similarly situated taxpayers. In addition, the state is defending cases challenging the constitutionality of certain taxes that fund discrete state programs.

The state is a defendant in a number of lawsuits related to: habitat restoration and environmental clean-up arising out of highway/roadway construction and maintenance and historic mining activity. While estimates are not available for all lawsuits, claims for damages equate to approximately $254 million.

The state is a defendant in a number of lawsuits by employees and employee unions alleging various infractions of law or contract. These suits claim back pay, damages, or future entitlements in excess of $760 million. Of the $760 million, $243 million is associated with a single case challenging the legislative repeal of the so-called gain-sharing benefit offered to members of certain state retirement plans. Pursuant to the legislative repeal, replacement benefits were offered in lieu of gain-sharing. It is estimated that if the gain-sharing benefit is restored and replacement benefits are retained, the biennial cost to the state would be approximately $243 million for the 2013-15 biennium. A second retirement benefits case challenges the legislative discontinuation of annual cost of living increases for PERS and TRS Plan 1 retirees. The anticipated biennial cost-savings to the state associated with the challenged legislation is estimated to be approximately $500 million for the 2013-15 biennium.

The state is contesting these lawsuits and the outcomes are uncertain at this time.

Tobacco Settlement

In November 1998, Washington joined 45 other states in a Master Settlement Agreement (MSA) with the nation's largest tobacco manufacturers to provide restitution for monies spent under health care programs for the treatment of smoking-related illnesses. Washington's share of the settlement was approximately $112.9 million in fiscal year 2012 and is subject to various offsets, reductions, and adjustments. Beginning in 2008, Washington received the first of ten "strategic contribution payments" under the MSA. This payment is subject to the same offsets, reductions, and adjustments as are applicable to the base payment. The 2012 strategic contribution payment was approximately $36.5 million.

In 2006, 2007, 2008, and 2009, determinations were made that disadvantages experienced by manufacturers as a result of participating in the MSA were a "significant factor" contributing to market share losses by those manufacturers. These determinations related to sales data for the years 2003, 2004, 2005, and 2006. Washington faces a potential "nonparticipating manufacturer (NPM) adjustment" in its share of between $0 and $130 million for the year 2003, $0 and $137 million for the year 2004, $0 and $131 million for the year 2005, and $0 and $119 million for the year 2006.

In addition, the states and the participating manufacturers have entered into an agreement under which the states will not contest that the disadvantages experienced by manufacturers as a result of participating in the MSA were a significant factor contributing to market share losses for the years 2007, 2008 and 2009, respectively. Washington faces a potential NPM adjustment of between $0 and $123 million for the year 2007, $0 and $173 million for the year 2008, and $0 and $176 million for the year 2009.

Washington and 37 other states each filed court actions seeking declarations that they had diligently enforced their escrow statutes – a defense to the adjustment claim. Thirty-six of the 37 states are participating in a single national arbitration of the NPM adjustment dispute.

The dispute is being presented to a three-member panel of retired judges. The panel is in place and some preliminary hearings have been held. The arbitration will comprise some presentations made by the states collectively and individually. The Washington specific hearing will begin in December 2012 and hearings will conclude in 2013. The panel will not issue its decision as to any individual state until the entire arbitration with all states has been completed.

C. FEDERAL ASSISTANCE

The state has received federal financial assistance for specific purposes that are generally subject to review or audit by the grantor agencies.

Entitlement to this assistance is generally conditional upon compliance with the terms and conditions of grant agreements and applicable federal regulations, including the expenditure of assistance for allowable purposes. Any disallowance resulting from a review or audit may become a liability of the state.

The state does estimate and recognize a claims and judgments liability for disallowances when determined by the grantor agency or for probable disallowances based on experience pertaining to these grants; however, these recognized liabilities and any unrecognized disallowances are considered immaterial to the state's overall financial condition.

D. ARBITRAGE REBATE

Rebatable arbitrage is defined by the Internal Revenue Service Code Section 148 as earnings on investments purchased from the gross proceeds of a bond issue that are in excess of the amount that would have been earned if the investments were invested at a yield equal to the yield on the bond issue.

The rebatable arbitrage must be paid to the federal government. State agencies and universities responsible for investments from bond proceeds carefully monitor their investments to restrict earnings to a yield less than the bond issue, and therefore limit any state arbitrage liability. The state estimates that rebatable arbitrage liability, if any, will be immaterial to its overall financial condition.

E. OTHER COMMITMENTS AND CONTINGENCIES

School Bond Guarantee Program

Washington voters passed a constitutional amendment in November 1999, creating the Washington State School Bond Guarantee Program.

The program's purpose is to provide savings to state taxpayers by pledging the full faith and credit of the state of Washington to the full and timely payment of voter-approved school district general obligation bonds in the event a school district is unable to make a payment.

The issuing school district remains responsible for the repayment of the bonds, including any payment the state makes under the guarantee.

The State Treasurer introduced the School Bond Guarantee Program in March 2000. At the end of fiscal year 2012, the state had guaranteed 212 school districts' voter-approved general obligation debt with 185 districts having a total outstanding principal of $8.33 billion. The state estimates that the school bond guarantee liability, if any, will be immaterial to its overall financial condition.

Local Option Capital Asset Lending Program

On September 1, 1998, the state lease-purchase program was extended to local governments seeking low cost financing of essential equipment and in the year 2000 for real estate. The Local Option Capital Assets Lending (LOCAL) program allows local governments to pool their financing requests together with Washington State agencies in Certificates of Participation (COPs). Refer to Note 7.B for the state's COP disclosure.

These COPs do not constitute a debt or pledge of the faith and credit of the state; rather, local governments pledge their full faith and credit in a general obligation pledge.

In the event that any local government fails to make any payment, the state is obligated to withhold an amount sufficient to make such payment from the local government's share, if any, of state revenues or other amounts authorized or required by law to be distributed by the state to such local government, if otherwise legally permissible.

Upon failure of any local government to make a payment, the state is further obligated, to the extent of legally available appropriated funds to make such payment on behalf of such local government. The local government remains obligated to make all COP payments and reimburse the state for any conditional payments.

As of June 30, 2012, outstanding certificates of participation notes totaled $78 million for 188 local governments participating in LOCAL. The state estimates that the LOCAL program liability, if any, will be immaterial to its overall financial condition.

Note 14
Subsequent Events

A. BOND ISSUES

In July 2012, Western Washington University issued $9.2 million in revenue bonds to refund a portion of the University's Housing and Dining System Revenue Bonds, Series 2003.

In August 2012, Washington State University issued $27.4 million in general revenue bonds to partially fund construction of the Spokane Biomedical and Health Sciences Building.

In July 2012, the state issued:

- $78.3 million in refunding taxable general obligation bonds.

In August 2012, the state issued:

- $205.4 million in motor vehicle fuel tax general obligation bonds for various transportation projects.
- $273.5 million in general obligation bonds for various capital projects.
- $40.5 million in taxable general obligation bonds for various capital projects.

In September 2012, the state issued:

- $352.2 million in various general obligation refunding bonds.
- $380.4 million in motor vehicle fuel tax general obligation refunding bonds.

In November 2012, the University of Washington is planning to issue general revenue bonds of $330.0 million. The bonds will provide partial funding for renovations to Husky Stadium, student residence halls and apartments, construction of a science building at the Bothell campus, and pay off $50 million in commercial paper.

B. CERTIFICATES OF PARTICIPATION

In August 2012, the state issued $81.2 million in Certificates of Participation.

C. GENERAL ELECTION

There were measures on the state's November 6, 2012, general election ballot that addressed state laws related to state revenues requiring legislative approval for increases to taxes and fees; authorizing charter schools; modifying the state debt limit calculation; investment of funds of certain four-year public institutions of higher education; and the regulation and taxation of marijuana production and distribution. These measures, if passed, could impact the state fiscally.

Election results are not final or official until certified. By law December 6, 2012, is the last day for the Office of the Secretary of State to certify general election returns.

Information is posted as available on the Secretary of State's website at: http://www.sos.wa.gov.