LEOFF 1 Survivor Benefits

Issue

Should benefits be improved for survivors of the Law Enforcement Officers' and Fire Fighters' (LEOFF) 1 members who die prior to retirement?

Members who die prior to retirement receive benefits that are not based on service credit, and some survivors receive less than the member had accrued at the time of death. Under the proposal, a survivor of a duty-related death would have the choice of the current benefit (up to 60 percent of average salary at the time of death), or full retirement benefits, as if the member had retired on the date of death. A survivor of a non-duty related death would automatically receive the greater of those same options.

Background and Committee Activity

In the 2009 Legislative Session, a non-SCPP bill (SB 6078) was offered to advance this proposal. The bill was referred to Senate Ways and Means but did not receive a hearing. Senator Prentice asked the SCPP to evaluate the proposal during the 2009 interim. The SCPP held a work session on this issue in November. At that meeting, the Executive Committee directed staff to update the bill and fiscal analysis for public hearing and possible executive action at the December meeting.

Policy Considerations

- Current provisions reflect a trade-off in plan design.
- LEOFF 1 is closed to new members, and most members are retired. This change would benefit only the few remaining active members.
- LEOFF 1 is currently projected to be out of surplus in the next decade.
    - Any increased cost could bring the plan out of surplus sooner.
    - Contributions may have to recommence.
- Creating new options for only one system would create an inconsistency.
- Creating new options that only apply prospectively to future survivors may create an inconsistency.
- Creating a benefit that was not funded over the working lives of the members may violate intergenerational equity.
- Current provisions may create a disincentive for experienced personnel to stay active past the earliest retirement date.

New Information and Attachments

- An updated bill draft is attached.
  - Effective dates have been changed, and statutory changes from the previous session have been incorporated.
- An updated fiscal note is attached.
  - The fiscal note is updated to reflect the results of the 2008 Actuarial Valuation Report.
- Preliminary pricing for a possible retroactive application will be presented at the meeting.
  - The increase would apply to current survivors, not just future survivors.

What is the Next Step?

Options include:

- Take no further action.
- Recommend the bill, with either prospective or retroactive application.

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LEOFF 1 Survivor Benefits

In Brief

Issue

LEOFF 1 provides guaranteed benefits for members who die prior to retirement. Guaranteed benefits provide members with benefits that are not based on service credit. In some cases, survivors receiving guaranteed benefits receive less than the member had accrued at the time of death. Stakeholders are asking that survivors be given the ability to receive the better of guaranteed benefits, or the amount the member would have received if the member had retired on the date of death.

Member Impact

Stakeholders have advocated changes to benefits for surviving active members of LEOFF 1. LEOFF 1 is a closed plan, with approximately 421 active members.

Aaron Gutierrez
Temporary Policy Analyst
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This report was updated in November 2009 to reflect new SCPP Executive Committee action. The remainder of the report is unchanged from October 2009.

Current Situation

The Law Enforcement Officers' and Fire Fighters' Retirement System Plan 1 (LEOFF 1) provides guaranteed benefits for members who die prior to retirement. Guaranteed benefits provide members with benefits that are not based on service credit. In some cases, survivors receiving guaranteed benefits receive less than the member had accrued at the time of death.

Survivors receive 50 percent of the member's average salary at the time of death. In contrast, a retiring member would have to accrue at least 25 years of service credit to receive the same level of benefits.

Thus, as a general rule the survivor of a member who dies early in his or her career may receive more benefits than the member has actually accrued. Conversely, the survivor of a member who dies later in his or her career, but still before retirement, may receive fewer benefits than the member has actually accrued.

Stakeholders are asking that survivors of LEOFF 1 members who die later in their careers, but before retirement, receive full retirement benefits, as if the member had retired on the date of death.

Background

Under current law, when a member retires, the member receives the full benefits based on service credit. If a member dies prior to retirement, the survivor receives different benefits based on the member's status at the time of death.

- **Active Status**

  If the member is on active status at the time of death, then the qualified survivor receives benefits equaling 50 percent of the member's average salary at the time of death.

- **Inactive, but Vested with 20 or More Years of Service**

  The qualified survivor receives the amount of benefits the member would have received at age 50.

- **Disability Retirement Status**

  If the member is retired for duty-connected disability at the time of death, the qualified survivor receives the amount of benefits the member was receiving at the time of death.

If the member's death was duty-related, any benefits received are not taxable.[1] An additional 5 percent of average salary is available for each qualifying child, up to a maximum of 60 percent of salary average.

In 1977, LEOFF 1 was closed to new members. The plan is currently in surplus, but is projected to be out of surplus in the next decade. Under the current funding policy no contributions are being made to the system. Preliminary numbers show there are 421 remaining active members in LEOFF 1. Most LEOFF 1 members are already retired, and with an average age of 57.8 years, most of the remaining active members are eligible for retirement.

[1]See 26 USC §101(h). Only the portion of benefits earned as a public safety officer exempt from taxation.

Legislative History

In the 2009 Legislative Session, a non-SCPP bill was submitted for consideration by the Legislature that would have changed the provisions regarding death before retirement. For duty-related death of a member on active status, the bill (SB 6078) would have allowed the survivor to choose between the following:

- Fifty percent of the member's average salary at the time of death.
- Full retirement benefits, as if the member had retired on the date of death.

If the member's death is not duty-related, the bill would have given the survivor the greater of those same options.

The bill was referred to the Senate Committee on Ways and Means, but did not receive a hearing.

Other states

Survivor benefits are complex, and vary greatly between states.

Survivor benefits for members who die prior to retirement are complex, and vary greatly between peer states. For the purpose of comparison, some general principles can be extracted. Please note, these are broad generalizations of survivor benefits in these states and will not apply to all members in all situations.

Colorado and Minnesota provide survivors with guaranteed benefits that are not connected to service credit. Benefits in these states are set at 40 percent and 50 percent, respectively, of average salary.[2] This is very similar to Washington and carries the same potential for receiving more or less benefits than the member has accrued at the time of death.

California provides a hybrid between guaranteed benefits and earned benefits, in that survivors receive 2.5 percent of salary average for every year or service credit, but with a guaranteed minimum of 40 percent and a maximum of 75 percent of salary average.

Instead of a guaranteed benefit, Ohio, Oregon, and Wisconsin provide for the return of contributions. Depending on the member's expected benefits at retirement, investment earnings from those contributions, and optional modifiers,[3] survivors might receive less than they would have earned at retirement.

Generally, all peer states have multiple options for determining the amount of benefits, but members are not allowed to choose. Instead, options are determined by the member's circumstances at the time of death. In some cases, survivors will automatically receive whichever option is largest. For example, in Iowa, survivors receive the greater of the actuarial present value of benefits, or a combination of contributions and earned benefits calculated via a formula.[4]

Though they do not allow members to choose how the benefits are calculated, several peer states do allow members or survivors to choose how the benefits are distributed. For example, if a vested police officer in Idaho dies before retirement, the survivor receives a default option of a lump sum payment of double the base plan contributions, plus interest. However, survivors may choose to waive this lump sum benefit in favor of a lifetime annuity.

[2] *Plus additional modifiers for qualifying dependants.*

[3] *Such as a doubling of contributions for duty-related death.*

[4] *The formula is as follows:* $Benefits = C + (\frac{HS}{D})$*, where C is the amount of contributions, H is the highest yearly salary, S is total service credit, and D is a denominator determined by job classification.*

Policy Analysis

There are five areas the SCPP may wish to consider regarding a possible change in LEOFF 1 survivor benefits:

- Plan design.
- Benefit improvements in a closed plan.
- Implications for surplus.

- ❖ Consistency.
- ❖ Human resource implications.

Plan Design

Typically, a survivor of a member who dies early in his or her career will receive more benefits than the member has accrued. Conversely, a survivor of a member who dies later in his or her career, but still before retirement, will receive less than the member has accrued.

Guaranteed benefits provide members with benefits that are not based on service credit, ensuring that a member receives at least a certain minimum amount no matter how long that member has been working. Generally, public safety officers have a greater likelihood of on-the-job injury or death than most other job classes. Thus, guaranteed benefits can offer greater peace of mind to officers in the earlier years of their career.

Under current LEOFF 1 provisions, the survivor of a member who dies in his or her first year of duty receives 50 percent of the member's average salary; the equivalent of retiring with 25 years of service credit.[5] In contrast, the survivor of a member who has crossed the 25-year mark, but still dies before retirement, will receive less benefits than the officer has accrued.

This contrast reflects a trade-off in plan design. In essence, current provisions protected benefits for junior officers, and were to some extent financed by senior officers. It could be argued that senior officers benefitted from this protection earlier in their career, even though they were fortunate enough not to need it. Conversely, it could be argued that senior officers are being penalized for working longer.

As most active members have more than 25 years, the Committee may wish to consider if this guaranteed benefit plan design is still appropriate.

[5]At retirement, benefits are calculated using a modifier that increases with years of service. Benefits for a member with more than 20 years of service are calculated as follows: 2% x Average Salary x Service Credit Years. As such, 50 percent of salary average corresponds to 25 years of service. Almost all LEOFF 1 members would currently qualify for 2 percent.

Benefit Improvements in a Closed Plan

LEOFF 1 is a closed system, and it is possible that few, if any, of the remaining active members will die before retirement. However, if they do, an increase in benefits for those members will add cost to the system.

LEOFF 1 is in the later stages of its life cycle. Most members have retired, and only a small number are still active.

As fewer and fewer members are on active status, any benefit improvements for only active members may seem relatively inexpensive. However, since most of the plan members are now retired, some policy makers may question whether it is appropriate to start down a path of increasing benefits for the few remaining active members.

Implications for Surplus

No new members are entering LEOFF 1, and it is possible that few, if any, of the remaining active members will die before retirement. However, if they do, an increase in benefits for those members will add cost to the system.

LEOFF 1 is currently in surplus, and it is possible the surplus could absorb the extra cost.[6] If the increased cost exceeds the surplus, contributions will have to recommence. LEOFF 1 is currently projected to be out of surplus in the next decade, and any increased cost could bring the plan out of surplus sooner.

The current surplus is the product of past contributions from three sources: members, employers, and the state. Policy makers may wish to consider whether the surplus should be paid down to increase benefits for active members.

[6]See the fiscal note for SB 6078 (2009).

Consistency

Between Members

The structure of LEOFF 1 survivor benefits has remained substantially the same since the 1970s, and there are currently as many as 28 survivors who are receiving less benefits than they would have received if the member had retired prior to death. Benefit increases could create an inconsistency between current and future survivors. Policy makers may wish to consider whether any increase in benefits should apply only to current active members.

Between Systems

Increasing benefits for active members could create inconsistency between members and systems.

Both LEOFF 1 and the Washington State Patrol Retirement System Plan 1 (WSPRS 1) provide guaranteed benefits for death prior to retirement. Creating new options for one system would create an inconsistency between the two. The Committee may wish to consider if any changes should also be applied to WSPRS 1.

Human Resource Implication

Active members may feel that the current structure of survivor benefits creates a disincentive for experienced personnel to stay active past the earliest available retirement date. In particular, a member diagnosed with a terminal illness may choose to retire as soon as possible so as to not risk losing any accrued benefits.

The Committee may wish to consider if changes should be applied to eliminate this potential disincentive.

Conclusion

At opposing ends of the spectrum, increasing survivor benefits for LEOFF 1 members at later stages in their career might be viewed as either giving members the benefits they've earned, or as enriching the few remaining active members of a closed plan.

The current structure represents a trade-off in plan design, and members have benefitted from this design earlier in their careers. However, members may feel that survivors of members with more years of service are being penalized by receiving less than the member had accrued. Additionally, members may feel that the current structure creates a disincentive for experienced personnel to remain active.

Any increase in benefits will have implications for the surplus. No new members are being added to the plan, no contributions are going in, and many of the few remaining active members are near retirement. Any increase in costs could bring the plan out of surplus sooner or require contributions to resume. Policy makers may wish to consider whether the surplus should be paid down to increase benefits for active members.

Benefit increases could create an inconsistency between current and future survivors. Increases could also create an inconsistency between similar plans. The Committee may wish to consider whether any increases should apply only to active members of LEOFF 1.

Committee Activity

The SCPP held a work session on this issue in October. At that meeting, the Executive Committee directed staff to update the bill draft and fiscal note from the previous session for public hearing and possible executive action at the December meeting. The Executive Committee also directed staff to provide preliminary pricing for possible retroactive application of the bill.

Possible Next Steps

- Take no further action.
- Recommend the bill, with either prospective or retroactive application.

Attachments

- An updated bill draft is attached.
  - The bill provides survivors of a duty-related death with a choice of guaranteed benefits, or the amount the member would have received if the member had retired on the date of death. Survivors of non-duty related death receive the greater of the two.
  - Effective dates have been changed, and statutory changes from the previous session have been incorporated.
- An updated fiscal note is attached.
  - The fiscal note is updated to reflect the results of the 2008 Actuarial Valuation Report.
- Preliminary pricing for a possible retroactive application will be presented at the meeting.
- Stakeholder input

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Wallis, Keri

From: Prentice, Sen. Margarita
Sent: Tuesday, May 12, 2009 8:13 PM
To: Office State Actuary, WA
Cc: Grazzini Smith, Alison
Subject: Please review and comment for the Senator - thanks! FW: LEOFF I pension program

Hello!

On behalf of Senator Prentice, would you please consider having the Select Committee on Pension Policy review the request below. Her prime sponsored SB 6078 addressed this but wasn't well received because it had not been considered by the SCPP.

Thank you for your thoughts and any information.

Sincerely,

Mary Anne Ross

Senior Executive Legislative Assistant
Senator Margarita Prentice
11th Legislative District
360-786-7616
http://www1.leg.wa.gov/senate/prentice/

-----Original Message-----
From: running4renton@msn.com [mailto:running4renton@msn.com]
Sent: Sunday, December 28, 2008 12:07 PM
To: Prentice, Sen. Margarita
Subject: LEOFF I pension program

SENATE INTERNET E-MAIL DELIVERY SERVICE

TO: Senator Margarita Prentice

FROM: Rosemary Quesenberry

STREET ADDRESS:
3609 Se 18 Court
Renton, WA 98058

E-MAIL: running4renton@msn.com

PHONE: (425) 271 - 4396

SUBJECT: LEOFF I pension program

MESSAGE:

Just a reminder regarding the pension program for LEOFF I officers. I appreciate you placing this matter on your priority list.

As we discussed, if officer Jim Laing, which has 40 years on with the Seattle Police department , if he would retired tomorrow and were then to die, his wife would receive the full pension he had accured over his many years of service.

However, if he would die while still employed his wife would receive only 50% of his final average salary. Jim recently contacted Representative Al O'Brien regarding this matter as well.

The LEOFF I pension reservoir could more than adequately supply the funds necessary to provide the spouses of active LEOFF I officers with the full pension based on years of service of the LEOFF I officer.

There is no cost to the State and to provide full pension benefits to spouses based on the years of service would keep some experienced officers on the job. In fact, there would be some savings to the State because eligible officers may continue to work and not draw on their pension.

Providing ACTIVE members of LEOFF I pension benefits equal to their years of service is the right thing to do. I appreciate your addressing this matter. It is always a pleasure to speak with you.

Happy New Year. If I can be of any service to you over the year, please just let me know!   God Bless.

NOTE: We are 99% sure that this constituent is in your district

RESPONSE REQUESTED: Rosemary has requested a response to this message.

DRAFT ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/04/09**	**LEOFF 1 Survivor Benefits**

WHAT THE READER SHOULD KNOW

The Office of the State Actuary ("we") prepared this draft fiscal note based on our understanding of the proposal as of the date shown above. We intend this draft fiscal note to be used by the Select Committee on Pension Policy during the 2009 Interim only. If a legislator introduces this proposal as a bill during the next Legislative Session, we will prepare a final fiscal note based on that bill language. The actuarial results shown in this draft fiscal note may change when we prepare our final version for the Legislature.

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

SUMMARY OF RESULTS

This proposal provides additional benefits to the surviving spouse of a Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 1 member who dies while an active member.

Impact on Pension Liability			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Today's Value of All Future Pensions	$70,619	$1.4	$70,621
Earned Pensions Not Covered by Today's Assets	$5,411	$1.4	$5,413

Impact on Contribution Rates: (Effective 09/01/2010)	
2010-2011 State Budget	**LEOFF**
Employee (Plan 2)	0.00%
Employer:	
Current Annual Cost	0.00%
Plan 1 Past Cost	0.00%
Total	0.00%
State	0.00%

Budget Impacts			
(Dollars in Millions)	**2010-2011**	**2011-2013**	**25-Year**
General Fund-State	$0.0	$0.0	$3.0
Total Employer	$0.0	$0.0	$3.0

See the Actuarial Results section of this draft fiscal note for additional detail.

WHAT IS THE PROPOSED CHANGE?

Summary Of Benefit Improvement

This proposal impacts the LEOFF Plan 1 by providing additional benefits to surviving spouses of members who die while still in active service.

If the active member dies in the line of duty, the surviving spouse would get the choice between an on-going benefit equal to 50 percent of the final average salary (FAS) at the date of death, or the monthly benefit the member would have received had he or she retired on the date of death.

If the active member dies a non-duty related death, the surviving spouse would get the greater of an on-going benefit equal to 50 percent of the FAS at the date of death, or the monthly benefit the member would have received had he or she retired on the date of death.

Effective Date: 90 days after session.

What Is The Current Situation?

An eligible spouse of a LEOFF Plan 1 member who dies while still in active service receives an on-going allowance equal to 50 percent of the member's FAS on his or her date of death. This amount is provided regardless of whether the cause of death is duty related or not. However, if the death is in the line of duty, the benefit is not subject to federal income tax. The surviving spouse is also eligible for an additional 5 percent of FAS for each qualifying dependent child, up to a combined maximum of 60 percent of FAS.

Who Is Impacted And How?

We estimate this proposal could affect any of the 421 active members in this plan through improved benefits. Furthermore, we expect less than two members per year will actually receive improved benefits.

We estimate this proposal will increase the benefits for a typical member by providing an increased survivor annuity for active member deaths. The average active LEOFF Plan 1 member has approximately 33.5 years of service and an $88,000 annual salary. Given these averages, under current law the survivor would receive an initial benefit of about $44,000 annually for the 50 percent of FAS annuity, whereas under this proposal, the standard retirement benefit formula would provide a benefit of approximately $59,000 annually.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This proposal will increase the survivor benefits we expect the plan to pay.

Under this proposal the survivor may receive either the accrued retirement benefit or the 50 percent of FAS annuity. The non-duty related benefit simply provides the greater of these two benefits, whereas the duty-related benefit provides the survivor with a choice between these two options. For the duty-related benefit, we assume that the survivor will choose the more valuable annuity. The remaining active LEOFF Plan 1 members average about 33.5 years of service. Therefore, the increase in cost results from paying the more valuable retirement benefit instead of the 50 percent of FAS annuity.

Who Will Pay For These Costs?

LEOFF Plan 1 closed to new entrants in 1977 and does not receive contributions from active members or their employers under current funding policy. Currently the plan has a funding surplus when comparing the assets to the liabilities. As long as such a surplus exists, the cost will be paid for through a decrease in the plan's surplus.

Based on our latest projections, we expect LEOFF Plan 1 to come out of its funding surplus in about 2016. Current statute does not address how LEOFF 1 will be funded if it comes out of surplus. We assume reinstatement of the prior LEOFF 1 funding policy. Under the prior policy, members and local employers each contribute 6 percent of the members' salaries, and the state pays any excess contributions required to fully fund the plan by June 30, 2024. These unfunded actuarial accrued liability (UAAL) contributions would be collected over all salaries in LEOFF Plans 1 and 2. Also, when LEOFF 1 contributions commence, the state portion of the Plan 2 normal cost rates will be collected over Plan 1 salaries in addition to Plan 2 salaries.

HOW WE VALUED THESE COSTS

Assumptions We Made

We assumed an overall 20 percent tax rate based on the average active salary for LEOFF Plan 1 members. Otherwise, we developed these costs using the same assumptions as disclosed in the June 30, 2008, Actuarial Valuation Report (AVR).

How We Applied These Assumptions

Under current law, survivors of active member deaths receive the 50 percent of FAS annuity. We split this benefit into duty and non-duty related death components. For the non-duty related death benefit, we paid the greater of the accrued retirement benefit and the 50 percent of FAS annuity. For the duty-related benefit, we compared the after-tax retirement benefit to the tax-free 50 percent of FAS annuity to determine which annuity provides more value to the member. However, the plan will pay the full pre-tax cost of these benefits.

Otherwise, we developed these costs using the same methods as disclosed in the AVR.

Special Data Needed

We used asset returns through June 30, 2009, from the Washington State Investment Board (WSIB), when determining whether LEOFF 1 would come out of surplus in the future.

Otherwise, we developed these costs using the same assets and data as disclosed in the AVR.

ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of LEOFF Plan 1 by increasing the present value of future benefits payable under the system as shown below.

Impact on Pension Liability			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits			
(The Value of the Total Commitment to all Current Members)			
LEOFF 1	$4,383	$1.4	$4,384
Unfunded Actuarial Accrued Liability			
(The Portion of the Plan 1 Liability that is Amortized to 2024)			
LEOFF 1	($1,209)	$1.4	($1,208)
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)			
LEOFF 1	($1,238)	$1.0	($1,237)

Note: Totals may not agree due to rounding.

How Contribution Rates Changed

The proposal will not affect contribution rates in the current biennium because the plan remains in a surplus funded position initially. However, we estimate a 0.02 percent UAAL rate increase when LEOFF 1 is expected to come out of surplus in the future. We used this rate increase to measure the budget changes in future biennia.

Impact on Contribution Rates: (Effective 07/01/2010)	
System/Plan	**LEOFF**
Current Members	
Employee (Plan 2)	0.000%
Employer:	
Normal Cost	0.000%
Plan 1 UAAL	0.000%
Total	0.000%
State	0.000%
New Entrants*	
Employee (Plan 2)	0.000%
Employer:	
Normal Cost	0.000%
Plan 1 UAAL	0.000%
Total	0.000%
State	0.000%

**Rate change applied to future new entrant payroll and used to determine budget impacts only. Current members and new entrants pay the same contribution rate.*

How This Impacts Budgets And Employees

Budget Impacts	
(Dollars in Millions)	**LEOFF**
2010-2011	
General Fund	$0.0
Non-General Fund	0.0
Total State	**$0.0**
Local Government	0.0
Total Employer	**$0.0**
Total Employee	**$0.0**
2011-2013	
General Fund	$0.0
Non-General Fund	0.0
Total State	**$0.0**
Local Government	0.0
Total Employer	**$0.0**
Total Employee	**$0.0**
2010-2035	
General Fund	$3.0
Non-General Fund	0.0
Total State	**$3.0**
Local Government	0.0
Total Employer	**$3.0**
Total Employee	**$0.0**

Note: Totals may not agree due to rounding.

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

As with the costs developed in the actuarial valuation, the emerging costs of the system will vary from those presented in the AVR or this draft fiscal note to the extent that actual experience differs from the actuarial assumptions.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

To determine the sensitivity of the actuarial results to the best-estimate assumptions or methods selected for this pricing we varied the following method:

- A deterministic investment return of 8 percent per year.

We used our projections as described in Appendix A to develop optimistic and pessimistic budget impacts for this proposal.

In the optimistic case, investment returns tend to be higher on average and we do not expect LEOFF 1 to come out of its surplus status, either with or without the inclusion of the proposed benefit improvement. Therefore, under optimistic conditions, this proposal has no budget impact.

Under pessimistic conditions, investment returns are lower than expected on average, there is less surplus available to fund the proposed benefit improvement, and contribution rates and budget costs increase. Our projections suggest that UAAL contributions would commence two years earlier under pessimistic conditions than they would under expected conditions. If we started the 0.02 percent contribution rate increase a biennium earlier than in our expected case presented in this draft fiscal note, the pessimistic 25-year budget cost would be $3.9 million. Please see Appendix A for more details on our projections.

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost and asset valuation methods are appropriate for the purposes of this pricing exercise.
2. The actuarial assumptions used are appropriate for the purposes of this pricing exercise.
3. The data on which this draft fiscal note is based are sufficient and reliable for the purposes of this pricing exercise.
4. Use of another set of methods and assumptions may also be reasonable, and might produce different results.
5. We prepared this draft fiscal note for the Select Committee on Pension Policy.
6. We prepared this draft fiscal note and provided opinions in accordance with Washington State law and accepted actuarial standards of practice as of the date shown on page 1 of this draft fiscal note.

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

Matthew M. Smith, FCA, EA, MAAA
State Actuary

APPENDIX A – HOW WE DEVELOPED AND VARIED OUR PROJECTIONS

How We Develop Our Projections

To produce the projections used in this draft fiscal note, we relied on the 2008 Actuarial Valuation Report (AVR). We also relied on the Washington State Investment Board's (WSIB) capital market assumptions (CMAs) and reported returns through June 30, 2009.

"Our projections" refers to the projections we produce by taking the most recent AVR and projecting it forward 50 years. For each future year, we look at the data, assets, and liabilities as though we were producing a new AVR in that year. The data reflects the current population and includes new entrants for open plans. From the group of members currently active, we expect some to remain active, some to retire, some to quit, and terminate service, etc. When members leave the active workforce, we replace them with new entrants. We assume future new entrants will have the same demographics as recent new entrants. Over time those new entrants also leave active status, and the cycle continues for each projected year. The result is a 50 year projection of valuation results that we use to generate future contribution rates.

Aside from the characteristics of new entrants, we made other assumptions to produce our projections. We assume no new benefit improvements throughout the projection beyond the improvement cited in this draft fiscal note. We assume all required member and employer contributions get made, regardless of their amounts. We assume no changes in WSIB asset allocation or CMAs.

Since the future is uncertain and future rates of investment return cause most of the variation we see in contribution rates, we vary the rate of return earned on plan assets in each year of our projections. This gives us a good idea of the range of results we can expect based on the current asset allocation. We adjusted WSIB's CMAs for the time horizon of the pension systems (see the Report On Long-Term Economic Assumptions for more detail about how we adjusted the CMAs). Using these assumptions we produced a distribution of annual asset returns that could arise given the asset allocation targets of the current WSIB comingled trust fund (CTF) portfolio.

When we vary the annual rates of return earned by the plan, our projections produce different contribution rates. For LEOFF 1, our projections produce different points in time when the plan falls out of surplus. We generated and compared the results of over ten thousand scenarios. In theory, each simulation has an equally likely chance of occurring. We relied on this fact to sort and compare the results.

For each scenario, we randomly selected a rate of return for each year of the projection. Since each scenario used 50 random returns, we saw some scenarios with very high returns and some with very low returns. Since we looked at a very large number of scenarios, we feel confident that the spectrum of results represents the possible futures. We looked at the 25th and 75th percentile of possible future scenarios. We refer to results labeled Pessimistic and Optimistic using the 25th and 75th percentiles, respectively, of the distribution of future scenarios. See the section, How the Results Change When the Assumptions Change, to see how we used the optimistic and pessimistic results of our projections for this proposal.

Unless otherwise stated, all other data, methods, and assumptions are consistent with the AVR.

GLOSSARY OF ACTUARIAL TERMS

Actuarial Accrued Liability: Computed differently under different funding methods, the actuarial accrued liability generally represents the portion of the present value of fully projected benefits attributable to service credit that has been earned (or accrued) as of the valuation date.

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of actuarial assumptions (i.e. interest rate, rate of salary increases, mortality, etc.).

Aggregate Funding Method: The Aggregate Funding Method is a standard actuarial funding method. The annual cost of benefits under the Aggregate Method is equal to the normal cost. The method does not produce an unfunded liability. The normal cost is determined for the entire group rather than on an individual basis.

Entry Age Normal Cost Method (EANC): The EANC method is a standard actuarial funding method. The annual cost of benefits under EANC is comprised of two components:

- Normal cost.
- Amortization of the unfunded liability.

The normal cost is determined on an individual basis, from a member's age at plan entry, and is designed to be a level percentage of pay throughout a member's career.

Normal Cost: Computed differently under different funding methods, the normal cost generally represents the portion of the cost of projected benefits allocated to the current plan year.

Projected Unit Credit (PUC) Liability: The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date (past service).

Projected Benefits: Pension benefit amounts which are expected to be paid in the future taking into account such items as the effect of advancement in age as well as past and anticipated future compensation and service credits.

Unfunded PUC Liability: The excess, if any, of the Present Value of Benefits calculated under the PUC cost method over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.

Unfunded Actuarial Accrued Liability (UAAL): The excess, if any, of the actuarial accrued liability over the actuarial value of assets. In other words, the present value of benefits earned to date that are not covered by plan assets.

BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #:	Z-1011.1/10
ATTY/TYPIST:	AI:cro
BRIEF DESCRIPTION:	Modifying death benefit provisions under the law enforcement officers' and firefighters' retirement system, plan 1.

AN ACT Relating to death benefits under the law enforcement officers' and firefighters' retirement system, plan 1; and amending RCW 41.26.160 and 41.26.161.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

Sec. 1. RCW 41.26.160 and 2009 c 226 s 1 are each amended to read as follows:

(1) In the event of the duty connected death of any member who is in active service, or who has vested under the provisions of RCW 41.26.090 with twenty or more service credit years of service, or who is on duty connected disability leave or retired for duty connected disability, or upon the death of a member who has left the employ of an employer due to service in the national guard or military reserves and dies while honorably serving in the national guard or military reserves during a period of war as defined in RCW 41.04.005, the surviving spouse shall become entitled, subject to RCW 41.26.162, to receive a monthly allowance equal to: If active, the choice of fifty percent of the final average salary at the date of death ((~~if active,~~)) or the amount of the retirement allowance the vested member would have received if he or she had retired on the date of death; or the amount

of retirement allowance the vested member would have received at age fifty((~~,~~)); or the amount of the retirement allowance such retired member was receiving at the time of death if retired for duty connected disability. The amount of this allowance will be increased five percent of final average salary for each child as defined in RCW 41.26.030((~~(7)~~)) (6), subject to a maximum combined allowance of sixty percent of final average salary: PROVIDED, That if the child or children is or are in the care of a legal guardian, payment of the increase attributable to each child will be made to the child's legal guardian or, in the absence of a legal guardian and if the member has created a trust for the benefit of the child or children, payment of the increase attributable to each child will be made to the trust.

(2) If at the time of the duty connected death of a vested member with twenty or more service credit years of service as provided in subsection (1) of this section or a member retired for duty connected disability, or at the time of the death of a member who has left the employ of an employer due to service in the national guard or military reserves and dies while honorably serving in the national guard or military reserves during a period of war as defined in RCW 41.04.005, the surviving spouse has not been lawfully married to such member for one year prior to retirement or separation from service if a vested member, the surviving spouse shall not be eligible to receive the benefits under this section: PROVIDED, That if a member dies as a result of a disability incurred in the line of duty or while honorably serving in the national guard or military reserves during a period of war as defined in RCW 41.04.005, then if he or she was married at the time he or she was disabled or left the employ of an employer due to service in the national guard or military reserves during a period of war as defined in RCW 41.04.005, the surviving spouse shall be eligible to receive the benefits under this section.

(3) If there be no surviving spouse eligible to receive benefits at the time of such member's duty connected death, then the child or children of such member shall receive a monthly allowance equal to thirty percent of final average salary for one child and an additional ten percent for each additional child subject to a maximum combined payment, under this subsection, of sixty percent of final average salary. When there cease to be any eligible children as defined in RCW 41.26.030((~~(7)~~)) (6), there shall be paid to the legal heirs of the

member the excess, if any, of accumulated contributions of the member at the time of death over all payments made to survivors on his or her behalf under this chapter: PROVIDED, That payments under this subsection to children shall be prorated equally among the children, if more than one. If the member has created a trust for the benefit of the child or children, the payment shall be made to the trust.

(4) In the event that there is no surviving spouse eligible to receive benefits under this section, and that there be no child or children eligible to receive benefits under this section, then the accumulated contributions shall be paid to the estate of the member.

(5) If a surviving spouse receiving benefits under this section remarries after June 13, 2002, the surviving spouse shall continue to receive the benefits under this section.

(6) If a surviving spouse receiving benefits under the provisions of this section thereafter dies and there are children as defined in RCW 41.26.030((~~(7)~~)) (6), payment to the spouse shall cease and the child or children shall receive the benefits as provided in subsection (3) of this section.

(7) The payment provided by this section shall become due the day following the date of death and payments shall be retroactive to that date.

Sec. 2. RCW 41.26.161 and 2005 c 62 s 2 are each amended to read as follows:

(1) In the event of the nonduty connected death of any member who is in active service, or who has vested under the provisions of RCW 41.26.090 with twenty or more service credit years of service, or who is on disability leave or retired, whether for nonduty connected disability or service, the surviving spouse shall become entitled, subject to RCW 41.26.162, to receive a monthly allowance equal to: If active, the greater of fifty percent of the final average salary at the date of death ((~~if active,~~)) or the amount of the retirement allowance the vested member would have received if he or she had retired on the date of death; or the amount of retirement allowance the vested member would have received at age fifty((~~,~~)); or the amount of the retirement allowance such retired member was receiving at the time of death if retired for service or nonduty connected disability. The amount of this allowance will be increased five percent of final average salary

for each child as defined in RCW 41.26.030((~~(7)~~)) (6), subject to a maximum combined allowance of sixty percent of final average salary: PROVIDED, That if the child or children is or are in the care of a legal guardian, payment of the increase attributable to each child will be made to the child's legal guardian or, in the absence of a legal guardian and if the member has created a trust for the benefit of the child or children, payment of the increase attributable to each child will be made to the trust.

(2) If at the time of the death of a vested member with twenty or more service credit years of service as provided in subsection (1) of this section or a member retired for service or disability, the surviving spouse has not been lawfully married to such member for one year prior to retirement or separation from service if a vested member, the surviving spouse shall not be eligible to receive the benefits under this section.

(3) If there be no surviving spouse eligible to receive benefits at the time of such member's death, then the child or children of such member shall receive a monthly allowance equal to thirty percent of final average salary for one child and an additional ten percent for each additional child subject to a maximum combined payment, under this subsection, of sixty percent of final average salary. When there cease to be any eligible children as defined in RCW 41.26.030((~~(7)~~)) (6), there shall be paid to the legal heirs of the member the excess, if any, of accumulated contributions of the member at the time of death over all payments made to survivors on his or her behalf under this chapter: PROVIDED, That payments under this subsection to children shall be prorated equally among the children, if more than one. If the member has created a trust for the benefit of the child or children, the payment shall be made to the trust.

(4) In the event that there is no surviving spouse eligible to receive benefits under this section, and that there be no child or children eligible to receive benefits under this section, then the accumulated contributions shall be paid to the estate of said member.

(5) If a surviving spouse receiving benefits under this section remarries after June 13, 2002, the surviving spouse shall continue to receive the benefits under this section.

(6) If a surviving spouse receiving benefits under the provisions of this section thereafter dies and there are children as defined in

RCW 41.26.030((~~(7)~~)) (6), payment to the spouse shall cease and the child or children shall receive the benefits as provided in subsection (3) of this section.

(7) The payment provided by this section shall become due the day following the date of death and payments shall be retroactive to that date.

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