The Select Committee on Pension Policy

2008 Interim Issues

Full Report

Office of the State Actuary

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Acknowledgments

This report was prepared by staff of the Office of the State Actuary. The Office of the State Actuary provides staff support to the Select Committee on Pension Policy.

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About This Report

Description of Report

The 2008 Interim Issues Report is a guide to issues considered by the Select Committee on Pension Policy (SCPP) during 2008. This report includes key materials for issues that received substantial policy consideration by the full SCPP.

This report contains both summary and detailed information. Summaries are provided for the recommendations made by the SCPP to the 2009 Legislature, the fiscal impact of those recommendations, and the work of the Committee on specific issues. Policy papers, draft legislation, and draft fiscal notes are included (where available) for those seeking more detail on a specific issue. The summary information in this report is also available in a separately published Executive Summary which may be accessed at http://www.leg.wa.gov/SCPP/Publications/issues_index.htm.

The materials in this report have been updated to reflect the most recent Committee activity. They do not necessarily match the materials provided at the SCPP meetings. A complete record of materials provided at the SCPP meetings is available on the SCPP web site at www.leg.wa.gov/scpp.

Staff Contacts

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About The SCPP

The Select Committee on Pension Policy (SCPP) studies issues and policies affecting the state's public employee retirement systems and makes recommendations to the Legislature regarding changes. Its statutory authority is contained in RCW 41.04.281.

The SCPP meets once a month during the legislative interim (the time when the Legislature is not in session). Its specific areas of interest include benefits design, retirement eligibility requirements, and pension funding methods. The SCPP also:

- Receives the results of actuarial audits administered by the Pension Funding Council.
- Reviews and makes recommendations to the Pension Funding Council regarding changes to actuarial assumptions or contributions rates.

Visit the SCPP website at www.leg.wa.gov/SCPP to learn more about the SCPP.

Members of the 2008 SCPP

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Elaine Banks, *TRS Retirees**

Senator Craig Pridemore

**Executive Committee Member*

2009 SCPP Legislative Proposals

The SCPP has recommended the following proposals for the 2009 Legislative Session:

1. **$150,000 Death Benefit**
   Increase the amount of the death benefit from $150,000 to $175,000. Recommended December 16, 2008.

2. **Change Membership Default for PERS 2/3**
   Change the default retirement plan for new members of the Public Employees' Retirement System (PERS) who do not select a plan upon hire from Plan 3 to Plan 2. Recommended December 16, 2008.

3. **Disability Benefits Study**
   Direct the Washington State Institute for Public Policy, with the assistance of the Office of the State Actuary, to study options for addressing the needs of PERS Plan 2/3, Teachers' Retirement System (TRS) Plan 2/3, and School Employees' Retirement System (SERS) Plan 2/3 members for adequate disability benefit coverage. Recommended December 16, 2008.

4. **DRS Technical Corrections**
   Repeal two obsolete sections of the TRS 1 statute. Recommended November 18, 2008.

5. **Fish & Wildlife Service Credit Transfer**
   Allow enforcement officers for the Department of Fish & Wildlife to convert prior PERS Plan 2 or PERS Plan 3 service to LEOFF Plan 2. Recommended December 16, 2008.

6. **HECB Proposal**
   Allow the Higher Education Coordinating Board to offer Higher Education Retirement Plans to employees not already retired from a state-administered retirement system. Recommended May 13, 2008.

7. **Interruptive Military Service**
   Allow members of the open plans to receive up to five years of free service credit for interruptive military service during a period of war as defined in RCW 41.04.005, with refunds to members who have already made payments for such service. Recommended December 16, 2008.

8. **Lower the General Salary Increase Assumption**
   Lower the statutory general salary increase assumption from 4.50 percent to 4.25 percent for all plans except LEOFF Plan 2—consistent with the actions of the Pension Funding Council. Recommended September 16, 2008.

9. **Military Death Benefits**
   Provide an unreduced joint and survivor annuity to the survivor of a member who dies in war while serving in the National Guard or Military Reserves. Recommended July 15, 2008.

10. **OSA Request Legislation**
    Clarify how the State Actuary studies salary growth, and codify current practices relating to recommendations of the State Actuary following an actuarial experience study. Recommended November 18, 2008.

11. **PERS to SERS Auto-Transfer**
    End the conditional automatic transfer of membership from PERS to SERS and allow certain auto-transferred members to reverse the transfer. Recommended May 13, 2008.

12. **Pre-LEOFF Survivor Benefits**
    Provide a new, member-paid survivor benefit option for spouses who are ineligible to receive a survivor benefit from the plan, and continue paying survivor benefits when a surviving spouse remarries. Recommended December 16, 2008.

13. **Past Part-Time Service Credit**
    Grant half-time service credit to certain Plan 2/3 members who worked at least half-time for an educational employer prior to 1987. Recommended November 18, 2008.

14. **Survivors of PERS 1 Inactives**
    Provide the same pre-retirement survivor annuity for inactive members as for active members in PERS Plan 1. Recommended May 13, 2008.

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Fiscal Impact Summary

2009 SCPP Legislative Proposals

2009-2011 Biennium			
	(Dollars in Millions)		
	2009-11	2009-11	2009-11
Proposals Recommended to the 2009 Legislature	GF-S	Local	Total ER
$150,000 Death Benefit	$0.0	$0.0	$0.0
Change Membership Default for PERS 2/3	$0.0	$0.0	$0.1
Disability Benefits Study	No Fiscal Impact		
DRS Technical Corrections	No Fiscal Impact		
Fish & Wildlife Service Credit Transfer	$0.0	$0.0	$0.0
HECB Proposal	$0.0	$0.0	$0.0
Interruptive Military Service	$0.0	$0.0	$0.0
Lower the General Salary Increase Assumption	No Fiscal Impact		
Military Death Benefits	$0.0	$0.0	$0.0
OSA Request Legislation	No Fiscal Impact		
PERS to SERS Auto-Transfer*	$0.0	$0.0	$0.0
Pre-LEOFF Survivor Benefits	Indeterminate Fiscal Cost		
Past Part-Time Service Credit	$0.0	$0.0	$0.0
Survivors of PERS 1 Inactives	$0.0	$0.0	$0.0
Total - SCPP Legislative Proposals For 2009	**$0.0**	**$0.0**	**$0.1**

Note: Totals may not agree due to rounding.
**No Fiscal Impact. Asset / Liability Transfer only.*

2011-2013 Biennium			
	(Dollars in Millions)		
	2011-13	2011-13	2011-13
Proposals Recommended to the 2009 Legislature	**GF-S**	**Local**	**Total ER**
$150,000 Death Benefit	**$0.1**	**$0.2**	**$0.4**
Change Membership Default for PERS 2/3	**$0.0**	**$0.1**	**$0.2**
Disability Benefits Study	No Fiscal Impact		
DRS Technical Corrections	No Fiscal Impact		
Fish & Wildlife Service Credit Transfer	**$0.0**	**$0.0**	**($0.1)**
HECB Proposal	**$0.0**	**$0.0**	**$0.0**
Interruptive Military Service	**$0.1**	**$0.1**	**$0.2**
Lower the General Salary Increase Assumption	No Fiscal Impact		
Military Death Benefits	**$0.0**	**$0.0**	**$0.1**
OSA Request Legislation	No Fiscal Impact		
PERS to SERS Auto-Transfer*	**$0.0**	**$0.0**	**$0.0**
Pre-LEOFF Survivor Benefits	Indeterminate Fiscal Cost		
Past Part-Time Service Credit	**$0.0**	**$0.0**	**$0.0**
Survivors of PERS 1 Inactives	**$0.0**	**$0.1**	**$0.1**
Total - SCPP Legislative Proposals For 2009	**$0.2**	**$0.5**	**$0.9**

Note: Totals may not agree due to rounding.
**No Fiscal Impact. Asset / Liability Transfer only.*

2009-2034 (25 Year)			
	(Dollars in Millions)		
	2009-34	2009-34	2009-34
Proposals Recommended to the 2009 Legislature	**GF-S**	**Local**	**Total ER**
$150,000 Death Benefit	**$3.5**	**$6.5**	**$11.1**
Change Membership Default for PERS 2/3	**$2.6**	**$6.7**	**$12.9**
Disability Benefits Study	No Fiscal Impact		
DRS Technical Corrections	No Fiscal Impact		
Fish & Wildlife Service Credit Transfer	**($0.1)**	**($0.3)**	**($0.4)**
HECB Proposal	**$0.0**	**$0.0**	**$0.0**
Interruptive Military Service	**$1.1**	**$2.4**	**$4.0**
Lower the General Salary Increase Assumption	No Fiscal Impact		
Military Death Benefits	**$0.6**	**$0.9**	**$1.8**
OSA Request Legislation	No Fiscal Impact		
PERS to SERS Auto-Transfer*	**$0.0**	**$0.0**	**$0.0**
Pre-LEOFF Survivor Benefits	Indeterminate Fiscal Cost		
Past Part-Time Service Credit	**$0.1**	**$0.2**	**$0.4**
Survivors of PERS 1 Inactives	**$0.2**	**$0.7**	**$1.1**
Total - SCPP Legislative Proposals For 2009	**$8.0**	**$17.0**	**$30.9**

Note: Totals may not agree due to rounding.
**No Fiscal Impact. Asset / Liability Transfer only.*

Issues Considered With Recommendation To Legislature

Office of the State Actuary

"Securing tomorrow's pensions today."

$150,000 Death Benefit

Description Of Issue

The retirement systems provide a $150,000 death benefit for public employees who die as a result of a duty-related injury or illness. The benefit amount has not changed since the benefit was first established in 1996. Stakeholders are asking the SCPP to revisit adjusting the amount for inflation.

Actuaries expect fewer than 13 duty-deaths each year from a group of over 290,000 public employees.

This issue raises two basic policy questions. Is the current amount of the death benefit sufficient, or should it be increased for past inflation? Should the death benefit be protected against future inflation?

Policy Highlights

- The relative value of the death benefit has declined 27 percent due to past inflation.
- Cost of Living Adjustments (COLAs) for lump sums provide equity across generations—not inflation protection for an individual's income.
- Some policy makers may prefer an insurance approach rather than a COLA approach.
- Automatic and ad-hoc COLAs can be equally effective in maintaining the value of benefits—with different implications for legislative control.
- The Legislature has previously rejected automatic COLAs for the death benefit.
- The SCPP recommended legislation on this issue in 2007 and 2008.

Policy Options For Adjusting The Duty-Death Benefit

Policy makers who feel the current death benefit should be adjusted for inflation may consider the following options:

- **Option 1: Provide A One-Time Adjustment For Past Inflation.**

- Restores the relative value of the benefit to its original level.
- Doesn't prevent future loss in value due to inflation.

❖ **Option 2: Provide An Automatic CPI-Based COLA.**

- Doesn't recover value already lost due to inflation.
- Generally prevents further loss of value due to inflation.
- Requires policy makers to give up some legislative control over the benefit, but may reduce need to revisit in future.

❖ **Option 3: One-Time Adjustment Plus Automatic COLA.**

- Recovers past value and generally prevents future loss of value.
- Requires policy makers to give up some legislative control over the benefit, but may reduce need to revisit in future.

❖ **Option 4: Increase To $175,000.**

- Recovers some value lost due to past inflation.
- Doesn't prevent future loss in value due to inflation.

Committee Activity

Staff briefed the Committee on this issue in October and November. The Committee held public hearings in November and December, and took executive action in December recommending Option 4 to the Legislature.

Recommendation To 2009 Legislature

Increase the amount of the death benefit from $150,000 to $175,000.

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$150,000 Death Benefit

In Brief

ISSUE

The retirement systems provide a $150,000 death benefit for public employees who die as a result of a duty-related injury or illness. The benefit amount has not changed since 1996.

The LEOFF 2 Board asked the SCPP to consider adjusting the amount of this benefit for past inflation and adding an automatic COLA to address future inflation.

The SCPP twice recommended legislation that would have applied an automatic COLA to the death benefit. The COLA provisions did not pass the Legislature.

MEMBER IMPACT

*Actuaries expect fewer than 13 duty-deaths each year from a group of over 290,000 public employees.**

**As of June 30, 2007.*

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Current Situation

The retirement systems provide a $150,000 lump sum (or one-time) death benefit for public employees who die as a result of a duty-related injury or illness. The benefit amount is set in statute and has not changed since the benefit was first established in 1996. The benefit is not subject to federal income tax.

The benefit is available to members of all state retirement systems*. Determination of eligibility is made by the Department of Labor and Industries (L&I).

The Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board asked the SCPP to consider adjusting the amount of this benefit for past inflation and adding an automatic Cost-Of-Living-Adjustment (COLA) to address future inflation.

**Also state, school district, and higher education employees who are not members of a state retirement system; paid from the state general fund.*

History

History Of The $150,000 Death Benefit

The $150,000 death benefit was first established in the LEOFF and the Washington State Patrol Retirement System (WSPRS) in 1996. The benefit was subsequently extended to various other groups of public employees over a period of several years. See **Appendix A** for a legislative history of the benefit.

Fifty-four $150,000 death benefits have been paid out since the benefit was first established—the majority being paid for LEOFF members (see **Figure 1**).

Figure 1

Number of $150,000 Death Benefits Paid*	
System	**Benefits Paid**
LEOFF	32
PERS	14
VFF	2
TRS	1
SERS	1
WSPRS	1
Unknown (paid from general fund)	3
Total	**54**

**As of 9/25/2008. Length of reporting period varies among systems.*

SCPP Has Recommended Death Benefit Bills

The SCPP studied this issue in coordination with the LEOFF 2 Board in 2006 and 2007. The Committee recommended legislation in the 2007 and 2008 Sessions that would have applied an automatic COLA to the death benefit. The COLA provisions did not pass the Legislature. See below for more details concerning the SCPP legislation.

The Legislature Has Rejected Death Benefit COLAs

Bills with provisions that would have automatically increased the amount of the $150,000 death benefit for inflation were introduced in the past three legislative sessions. None of the bills passed the Legislature with the COLA provisions intact.

Bills that would have automatically increased the amount of the $150,000 death benefit for inflation were introduced in the past three legislative sessions.

2006 Session

HB 2933/SB 6724 dealt with the death benefit for LEOFF Plan 2. The bill expanded eligibility and provided an automatic COLA on the benefit amount. The proposed COLA would have annually increased the amount of the death benefit based on cumulative changes in the Consumer Price Index for Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB), up to a

maximum of 3 percent per year. This is the same increase provided for pensions in the Plans 2/3 retirement systems. The COLA was removed before the bill passed the Legislature.

2007 Session

HB 1266/SB 5177, an SCPP bill, made similar changes to the death benefit as the 2006 bill except it applied to all plans. The COLA was removed from the House bill in the Appropriations Committee, but was retained in the Senate version of the bill that passed Ways and Means. The House version of the bill, without the COLA, ultimately passed the Legislature.

2008 Session

HB 3026/SB 6664, another SCPP bill, contained the same COLA provisions as introduced in the earlier legislation. The bill was heard in the Senate Ways and Means Committee and received no hearing in the House.

Comparisons

Other Death Benefits Provided

The $150,000 death benefit is one of many death benefits that are provided for members*. Others include:

Many death benefits are provided for members.

- Survivor and death benefits from the retirement plan.
- L&I death benefits.
- Social Security survivor benefits.
- Federal public safety officer's death benefits.
- Reimbursement of premiums paid to the Health Care Authority.

A detailed list of the various death benefits provided is contained in **Appendix B**. Among these, the most significant other lump sum death benefit provided is the federal Public Safety Officers' Benefits Death Benefit. This benefit ($315,746 in 2008) is payable to survivors of law enforcement officers, fire fighters, and other public safety

personnel who die in the line of duty. The benefit is annually adjusted for inflation.

**Employer provided life insurance is beyond the scope of this paper and is not considered among the death benefits provided.*

Death Benefits In Comparative Systems

Most of Washington's comparative systems provide survivor annuities similar to those in Washington's retirement systems. The annuities are generally based on the member's earned benefit or some percentage of the member's salary.

Five of Washington's comparative systems also provide some type of lump sum death benefit (see **Figure 2**). The three systems (California, Idaho, and Iowa) that provide fixed-dollar lump sum benefits similar to Washington do not automatically increase the benefit amount for inflation. Three systems (Colorado, Idaho, and Wisconsin) provide a lump sum based on the member's contributions. Since contributions are based on salaries, and salaries grow with inflation, contribution-based lump sums effectively have built-in inflation adjustments. One system (California) provides a lump sum that is "periodically adjusted." Idaho and Iowa provide an enhanced return of contributions and a special duty-related lump sum death benefit for public safety employees.

Figure 2

Lump Sum Death Benefits in Comparative Systems*		
System	**Benefit Amount**	**COLA**
California CALSTRS	$24,652	Periodically adjusted.
Colorado PERA	200% Return Of Contributions plus interest (ROC).	None.
Idaho PERSI	200% ROC. Also $100,000 for police and firefighters killed in line of duty.	None.
Iowa IPERS	100% ROC plus additional amount based on salary and service. Also $100,000 for public safety officer killed in line of duty.	None.
Wisconsin WRS	200% ROC.	None.

**Source: Member handbooks published on system administrator's web sites as of 10/08/2008.*

Policy Analysis

This Issue Raises Two Basic Policy Questions

The issue of whether or not to adjust the $150,000 death benefit for inflation raises two basic policy questions:

- Is the current amount of the death benefit sufficient, or should it be increased for past inflation?
- Should the death benefit be protected against future inflation?

The way policy makers respond will likely depend upon three key factors.

The way policy makers respond to these questions will likely depend upon three key factors:

- How they choose to apply policy on inflation protection to the death benefit.
- How they view the purpose of the death benefit.
- How much control they wish to keep over the death benefit.

The rest of this paper will explore these and other factors that policy makers may consider in addressing this issue.

Inflation Erodes The Relative Value Of The Death Benefit

The value of the death benefit has declined 27 percent since 1996.

Inflation erodes the relative value of a fixed dollar amount over time. The $150,000 death benefit was first established in 1996. The cumulative effect of inflation since then has eroded 27 percent* of the relative value of the benefit. Put another way, the amount of the death benefit would need to be increased to $205,000 to provide the same level of purchasing power that it did in1996. Absent any adjustment, inflation will continue to erode the value of the death benefit in the future.

**Based on the Consumer Price Index for Urban Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB), all Items.*

The State's Policy On Inflation Protection For Pensions

State policy on protecting retirement benefits from inflation can be found in existing policy statements and further inferred from plan design. The SCPP has adopted as a stated goal ". . . to increase and maintain the purchasing

power of retiree benefits in the Plans 1 of PERS and TRS. . . ." The Plans 2/3 of the state's retirement systems, the most recently created tiers, provide an annual COLA on retirement pensions. The Plans 2/3 COLA is based on inflation as measured by changes in a Consumer Price Index (CPI). The inclusion of this COLA in the Plans 2/3 design indicates a clear desire to protect retirement pensions from the effects of inflation.

Policies on inflation protection were not necessarily designed for lump sum benefits.

These policies around inflation protection were designed to apply to ongoing *pension* benefits and not necessarily one-time *lump sum* benefits. Policy makers may wish to consider to what extent, if any, inflation protection policies apply to non-pension benefits like the $150,000 death benefit.

COLAs For Pensions And Lump Sums Have Different Policy Implications

Why would the nature of the benefit matter when considering inflation protection policies? COLAs for ongoing pensions have different policy implications than COLAs for one-time lump sum benefits. One provides inflation protection, while the other provides equity across generations.

Providing a COLA for a pension or other annuity-type benefit provides inflation protection for an *individual's* income. The COLA helps maintain the relative value of the pension payments over time by offsetting the effects of inflation.

COLAs for lump sums maintain value among generations.

In contrast, providing a COLA for a lump sum benefit maintains the value of the benefit among successive *generations* of recipients. It ensures that later recipients are able to purchase the same amount of goods and services with the benefit that earlier recipients could. It does not provide inflation protection for an individual's income. Why not? A lump sum payment is only received once. It doesn't become part of the recipient's ongoing income stream and consequently doesn't lose its value (from the recipient's perspective) over time.

Lump Sum Death Benefits Are Less Likely To Have COLAs

Given the different policy implications of COLAs for annuities and lump sums, policy makers may wish to consider current practice in this area. **Figure 3** shows that death benefits for retirement system members paid in the form of a monthly annuity are more likely to have inflation protection than benefits paid in a lump sum. A detailed list of the various death benefits provided is contained in **Appendix B**.

Figure 3

Death Benefits Provided*			
Type	**Total**	**COLA**	**%COLA**
Annuity	9	7	78%
Lump Sum	7	3	43%

**Similar benefits in state retirement systems are considered a single type.*

In the preceding figure, the "Total" column shows the total number of benefits of each type (annuity or lump sum); the "COLA" column shows how many include an automatic COLA; and the "%COLA" column shows the percentage of annuity and lump sum benefits with an automatic COLA.

The Death Benefit Is Designed To Provide Temporary Assistance

A key policy consideration is the intended purpose of the benefit.

Policy makers may consider the purpose of the $150,000 death benefit in determining how to apply policy on inflation protection. Is the benefit intended to replace income and support an ongoing standard of living? Or, is the benefit intended to provide one-time relief for specific situations? The answers to these questions have implications for policy decisions.

The death benefit is a one-time payment that is not related to a member's salary. Recipients may do with the payment whatever they wish—including spending the entire amount at once. Given this design, it is unlikely that the benefit was intended to replace income and support an ongoing standard of living. Rather, it is more likely that the death benefit was primarily intended to provide temporary financial assistance following the death of a member.

The purpose of the benefit may affect how policy makers view this issue. From the perspective of policy makers, there may be less need to adjust for inflation a benefit that is transitional and does not serve to replace income or maintain an ongoing standard of living.

Policy Makers May Take An Insurance-Based Approach

The death benefit more closely resembles an insurance benefit than a pension.

The design and purpose of the $150,000 death benefit more closely resembles an insurance benefit than a traditional pension benefit. It is a one-time payment of a fixed-dollar amount that provides temporary financial assistance—much like term life insurance. Policy makers who view this as an insurance-type benefit may be inclined to take more of an insurance-based approach to this issue. An insurance approach would involve periodically reviewing the "policy" and adjusting the coverage amount based on the risks and needs at that time. Under this approach, the policy focus shifts away from COLAs and more towards the adequacy of the benefit provided.

Assessing The Adequacy Of The Death Benefit May Be Challenging

Policy makers may find it challenging to assess the adequacy of a benefit (like the $150,000 death benefit) that is not dedicated to a specific purpose. Since the value of the benefit can't easily be measured against a specific outcome, assessments of adequacy will likely be highly subjective. Such assessments may involve considering how the $150,000 death benefit fits in with all the other death benefits provided—many of which are pension benefits that do have inflation protection. This could be a complex task given the number and variety of different death benefits provided, and the fact that survivors may qualify for multiple death benefits (see **Appendix B**).

Policy makers may assume the amount was adequate when the benefit was first enacted.

For the sake of simplicity, some policy makers may assume the amount was adequate when the benefit was first enacted in 1996. Under this assumption, all that is needed to ensure the adequacy of the benefit today is to adjust the amount of the benefit for past inflation.

Duty-Related Death Benefits May Impact Recruitment

When contemplating adjustments to the $150,000 death benefit, policy makers may also consider the purpose and adequacy of the benefit from an employer perspective. Duty-related death benefits may impact the ability of employers to recruit for high-risk occupations. The availability and generosity of such benefits may serve as an added inducement for employees considering such occupations. This would likely have the greatest impact for public safety employers. The fact that the $150,000 death benefit was first established for police and fire fighters (see **History**) may be indicative of a greater interest in duty-related death benefits by public safety groups.

Automatic And Ad-Hoc COLAs Can Be Equally Effective In Maintaining The Value Of Benefits

Policy makers who feel the $150,000 death benefit should be adjusted for inflation will likely consider how to adjust it. Most likely, this will involve some form of a COLA—since COLAs are a common and effective way to adjust benefits for inflation. There are two basic approaches to COLAs that policy makers may wish to consider: ad-hoc and automatic. The approach chosen has implications for how much control policy makers retain over the benefit.

Policy makers who want the most control will likely prefer an ad-hoc approach.

Ad-hoc COLAs are one-time increases. Ad-hoc COLAs are generally more backward-looking. They can be very effective at making up for past inflation, but usually do little to address future inflation. Ad-hoc COLAs can give policy makers the most flexibility in reacting to specific situations and in controlling costs. Policy makers who want to maintain the most control in adjusting benefits will likely prefer an ad-hoc approach.

Policy makers who want less involvement will likely prefer an automatic approach.

In contrast, automatic COLAs are ongoing increases and tend to be more forward-looking. Automatic COLAs can be very effective at protecting benefits against future inflation, but may do little to address lost purchasing power due to past inflation. Automatic COLAs may be preferred from the member viewpoint since they are ongoing and don't require continual action by policy makers. However, for the same reasons, it may be more difficult to fine-tune an automatic COLA for a specific situation. Policy makers

who want less involvement in the process of adjusting benefits will likely prefer an automatic approach.

A common way of implementing automatic COLAs is to base the COLA on a measure of inflation such as the CPI. This process of linking a benefit to an underlying measure of inflation is known as *indexing*. Indexing is a direct and effective way to protect benefits against inflation. This is the method chosen by the SCPP in prior years when the Committee recommended applying an automatic COLA to the death benefit (see **History**). **Appendix C** contains a more complete discussion on the various ways to index a benefit.

Periodically granting ad-hoc COLAs can have much the same effect as an automatic COLA.

Ad-hoc COLAs can be as effective in maintaining the value of a benefit as automatic COLAs, depending on how they are administered. Periodically granting ad-hoc COLAs to make up for past inflation can have much the same effect as providing an automatic COLA. The main difference is that ad-hoc COLAs may occur less frequently than every year. When this happens, the benefit loses more value in the years between ad-hoc COLAs than it would lose under an automatic COLA. Given that both approaches can be equally effective in maintaining value, the approach taken will likely depend on how much control and involvement policy makers want in the process of adjusting benefits.

Conclusion

The issue of adjusting the $150,000 death benefit for inflation raises two basic policy questions. Is the current amount sufficient or should it be increased for past inflation? Should it be protected against future inflation?

How policy makers respond to these questions will likely depend upon three key factors:

- How they choose to apply policy on inflation protection to the death benefit.
- How they view the purpose of the death benefit.
- How much control they wish to keep over the death benefit.

Some policy makers may prefer to take an insurance-based approach to this issue rather than the COLA-based approach taken in the past.

Possible Options

Policy makers who feel the current amount of the death benefit is sufficient for its intended purpose will likely be inclined to take no further action at this time. Policy makers who feel the current death benefit should be adjusted for inflation may consider one of the options below.

Preliminary pricing for each of the policy options was provided at the November meeting.

Option 1: Provide A One-Time Adjustment For Past Inflation

This option restores the relative value to its original level.

This option would grant an ad-hoc COLA on the amount of the death benefit to make up for past inflation. The amount of the death benefit would be increased to $205,000.

This option would restore the relative value of the death benefit to its original level but wouldn't prevent future loss in value due to inflation.

Option 2: Provide An Automatic CPI-Based COLA

This option generally prevents further loss of value.

This option would apply an automatic CPI-based COLA to the death benefit. The COLA would be modeled after the COLA provided for pensions in the Plans 2/3. The amount of the death benefit would annually increase based on cumulative changes in the CPI-W, STB, up to a maximum of 3 percent per year. This is the approach that has been taken by the SCPP in the past and has been rejected by the Legislature (see **History**).

This option would generally not recover value already lost due to past inflation since the annual increases are capped at 3 percent. The 3 percent cap is a cost-control feature originally intended for pension benefits. It may be of limited value for a death benefit that is paid out infrequently. This option would generally prevent further

loss of value due to inflation—while long-term inflation averages 3 percent or less. This approach requires policy makers to give up some control over the benefit amount, but may reduce the need to revisit this in the future.

Option 3: One-Time Adjustment And Automatic CPI-Based COLA

This option recovers lost value and generally prevents further loss.

This option combines the previous two options. It would increase the amount of the death benefit to $205,000 and apply an automatic CPI-based COLA on the new amount.

This option would recover all value lost to past inflation as well as generally prevent further loss of value due to inflation—while long-term inflation averages 3 percent or less. This option has the same policy implications regarding the cap on the automatic COLA as discussed under Option 2. This approach also requires policy makers to give up some control over the benefit amount, but may reduce the need to revisit this in the future.

Option 4: Increase To $175,000

This option recovers some lost value.

This option would increase the amount of the death benefit to $175,000. This option would recover some of the value of the benefit lost to past inflation, but would not fully restore the benefit to its original level. This option would not prevent further loss in value due to future inflation.

Committee Activity

During their September meeting, the Executive Committee of the SCPP directed staff to develop policy options and bring those options back to the full SCPP with pricing.

Staff briefed the Committee on the first three options at the October meeting. Following the meeting, the Chair requested staff to prepare draft legislation and pricing for an additional option of increasing the benefit to $175,000.

At the November meeting, staff briefed the Committee on Option 4 and a public hearing was held. The Committee moved this issue to December for another public hearing.

The Committee held a second public hearing in December and took executive action recommending Option 4 to the Legislature.

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

Increase the amount of the death benefit from $150,000 to $175,000. Recommended December 16, 2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0399.1/09).

Draft Fiscal Note

Attached.

Stakeholder Input

Correspondence attached from:

Kelly Fox, Chair, LEOFF 2 Board, 5/12/2008, and 6/30/2008.

Correspondence on file from:

John Kvamme, WASA & AWSP consultant, 5/15/2008.

Appendix A: History Of Legislative Changes To The $150,000 Death Benefit*

History of Legislative Changes to the $150,000 Death Benefit		
Year	**Bill**	**Effect**
1996	E2SSB 5322	$150,000 death benefit established for LEOFF and WSP.
1998	SB 5217 ESB 6305	$150,000 death benefit established in VFF. $150,000 death benefit is established for survivors of PERS 1 port and university police officers.
1999	ESSB 5180 (Budget)	$150,000 death benefit provided to teachers and paid as sundry claim from general fund. Expired 6/30/2001.
2000	EHB 2487 (Budget)	$150,000 death benefit provided to school district employees and paid as sundry claim from general fund. Expired 6/30/2001.
2001	ESSB 6153 (Budget)	$150,000 death benefit provided to state, school district, and higher education employees and paid as sundry claim from general fund. Expired 6/30/2003.
2003	HB 1207	$150,000 death benefit established in PERS, TRS, and SERS. Benefit also provided as a sundry claim to the general fund for state, school district, and higher education employees who are not eligible to receive the benefit from a state retirement system.
2006	SHB 2933	Eligibility for the $150,000 death benefit expanded to include death from duty-related illness for LEOFF 2.
2007	SHB PL 1266	Eligibility for the $150,000 death benefit expanded to include death from duty-related illness for all plans.

See **Appendix D for a description of the plan acronyms used.*

Appendix B: Death Benefit Provided For Public Employees*

Death Benefits Provided for Public Employees[1]				
Benefit	**Normal Form**	**Eligible Deaths**	**Amount**	**Annual Adjustment[2]**
LEOFF & WSP Plan 1 Survivor Pension	Annuity	Duty & Non-Duty	50%-60% of AFC	Indexed to CPI
PERS & TRS Plan 1 Survivor Benefit	Annuity or Lump Sum	Duty & Non-Duty	Member's earned benefit or return of contributions with interest (ROC)[3]	Uniform COLA on annuity -- indexed by level 3%
Plans 2/3 Survivor Benefit	Annuity or Lump Sum	Duty & Non-Duty	Member's earned benefit or ROC[3,4]	Annuity Indexed to CPI
VFF Survivor Benefit	Annuity	Duty & Non-Duty	Member's earned benefit	None -- Benefits periodically increased by Board
VFF Duty-Death Survivor Pension	Annuity	Duty	$1,589/month +$137/month per child. As of 7/1/2008.	Indexed to CPI
HIED Survivor Benefit	Annuity or Lump Sum	Duty & Non-Duty	Payout of member's account	None
LEOFF Plan 2 Survivor Health Care	Annuity	Duty	Reimbursement of premiums paid to Health Care Authority—up to $839/month for 2008	Indexed to Health Care Authority medical and dental premiums
L&I Death Benefit	Annuity	Duty	60%-70% of gross wages up to 120% of state average wage[5]	Indexed to state average wage[5]
Social Security Survivor Benefit	Annuity	Duty & Non-Duty	75%-100% of employees earned Social Security benefit	Indexed to CPI
$150,000 Death Benefit	Lump Sum	Duty	$150,000 (+$2,000 in VFF)	None
VFF Funeral Benefit	Lump Sum	Duty	$2,000	None
TRS 1 Death Benefit	Lump Sum	Duty & Non-Duty	$400 or $600	None
L&I Death Lump Sum	Lump Sum	Duty	100% state average monthly wage[5]	Indexed to state average wage[5]
L&I Burial Benefit	Lump Sum	Duty	Up to 200% state average monthly wage[5]	Indexed to state average wage[5]
Social Security Burial Benefit	Lump Sum	Duty & Non-Duty	$255	None
Federal Public Safety Officers' Death Benefit	Lump Sum	Duty	$315,746 as of 10/01/2008	Indexed to CPI

1. Eligibility varies by group. Some benefits are not available to all groups and some groups may be eligible for multiple benefits. Excludes employer provided life insurance.

2. Excludes optional COLAs purchased by recipient.

3. Actuarial reduction applied if death is not duty-related.

4. 150% ROC for LEOFF Plan 2; payout of member's DC account for Plans 3.

5. $3,727 as of 7/01/2008.

See **Appendix D for a description of the plan acronyms used.*

Appendix C: Indexing Benefits

A frequently used method of protecting the value of a benefit against inflation is indexing. Indexing involves making annual adjustments to the benefit amount based on changes in an underlying measure of inflation.

One of the most commonly used measures of inflation is the Consumer Price Index (CPI). The CPI records changes in the price of a set "market basket" of goods and services at different points in time. The U.S. Department of Labor publishes numerous indexes that measure inflation based on different market baskets and geographic regions. Each CPI produces a slightly different measure of inflation. The CPI most commonly used in Washington State's retirement systems is the Consumer Price Index for Urban Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB). An individual may experience inflation quite different from that measured by the CPI if the goods and services purchased by the individual do not closely match the market basket used by the CPI.

A key issue in indexing benefits is the amount of inflation protection to provide. The value of a benefit may be:

- Fully protected from inflation (full indexing).
- Protected up to a maximum amount of inflation (partial indexing).
- Protected against a set amount of inflation (level indexing).

A **fully indexed** benefit increases at the same percentage change as inflation each year. This method ensures the full purchasing power of the benefit is always maintained, but can lead to greater than expected costs if actual inflation exceeds the amount assumed for funding the benefit. Examples of fully indexed retirement benefits include Social Security, which is indexed to the CPI-W, All U.S. Cities; and the LEOFF Plan 1 pension, which is indexed to the CPI-W, STB.

A **partially indexed** benefit increases with the percentage change in inflation each year up to a maximum percentage. In years where inflation exceeds the maximum, the benefit will lose some purchasing power.

The index can be designed to allow the benefit to recover lost purchasing power during periods when actual inflation is lower than the maximum. This method can maintain most of the purchasing power of a benefit while controlling costs and promoting stable funding. Examples of partially indexed retirement benefits are Plans 2/3 pensions, which are indexed to the CPI-W, STB, to a maximum of 3 percent.

A **level indexed** benefit increases by a fixed percentage every year. Purchasing power is lost in years when inflation exceeds the fixed percentage and is gained in years when inflation is less than the fixed percentage. This method is simple to administer and can maintain most of the purchasing power of a benefit while controlling costs and promoting stable funding. Under this method, if actual inflation is consistently less than the fixed amount, the purchasing power of the benefit will increase. An example of a level indexed retirement benefit is the PERS and TRS Plan 1 Uniform COLA, which increases by 3 percent each year.

Appendix D: Plan Acronyms

- Public Employees' Retirement System (PERS)
- Teachers' Retirement System (TRS)
- School Employees' Retirement System (SERS)
- Public Safety Employees' Retirement System (PSERS)
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF)
- Washington State Patrol Retirement System (WSPRS)
- Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFF)
- Judicial Retirement System (JRS)
- Higher Education Retirement Plans (HIED)

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0399.1/09

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Increasing the duty-related death benefit for public employees.

AN ACT Relating to increasing the duty-related death benefit for public employees; amending RCW 41.04.017, 41.24.160, 41.26.048, 41.32.053, 41.35.115, 41.37.110, 41.40.0931, and 41.40.0932; reenacting and amending RCW 43.43.285; and declaring an emergency.

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

Sec. 1. RCW 41.04.017 and 2007 c 487 s 1 are each amended to read as follows:

A one hundred ((~~fifty~~)) <u>seventy-five</u> thousand dollar death benefit shall be paid as a sundry claim to the estate of an employee of any state agency, the common school system of the state, or institution of higher education who dies as a result of (1) injuries sustained in the course of employment; or (2) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter, and is not otherwise provided a death benefit through coverage under their enrolled retirement system under chapter 402, Laws of 2003. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the director of the department of general administration by order under RCW 51.52.050.

Sec. 2. RCW 41.24.160 and 2001 c 134 s 2 are each amended to read as follows:

(1)(a) Whenever a participant dies as the result of injuries received, or sickness contracted in consequence or as the result of the performance of his or her duties, the board of trustees shall order and direct the payment from the principal fund of (i) the sum of one hundred ((~~fifty-two~~)) seventy-seven thousand dollars to his widow or her widower, or if there is no widow or widower, then to his or her dependent child or children, or if there is no dependent child or children, then to his or her dependent parents or either of them, or if there are no dependent parents or parent, then the death benefit shall be paid to the member's estate, and (ii)(A) the sum of one thousand two hundred seventy-five dollars per month to his widow or her widower during his or her life together with the additional monthly sum of one hundred ten dollars for each child of the member, unemancipated or under eighteen years of age, dependent upon the member for support at the time of his or her death, (B) to a maximum total of two thousand five hundred fifty dollars per month.

(b) Beginning on July 1, 2001, and each July 1st thereafter, the compensation amount specified in (a)(ii)(B) of this subsection shall be readjusted to reflect the percentage change in the consumer price index, calculated as follows: The index for the calendar year preceding the year in which the July calculation is made, to be known as "calendar year A," is divided by the index for the calendar year preceding calendar year A, and the resulting ratio is multiplied by the compensation amount in effect on June 30th immediately preceding the July 1st on which the respective calculation is made. For the purposes of this subsection, "index" means the same as the definition in RCW 2.12.037(1).

(2) If the widow or widower does not have legal custody of one or more dependent children of the deceased participant or if, after the death of the participant, legal custody of such child or children passes from the widow or widower to another person, any payment on account of such child or children not in the legal custody of the widow or widower shall be made to the person or persons having legal custody of such child or children. Such payments on account of such child or children shall be subtracted from the amount to which such widow or widower would have been entitled had such widow or widower had legal

custody of all the children and the widow or widower shall receive the remainder after such payments on account of such child or children have been subtracted. If there is no widow or widower, or the widow or widower dies while there are children, unemancipated or under eighteen years of age, then the amount of one thousand two hundred seventy-five dollars per month shall be paid for the youngest or only child together with an additional one hundred ten dollars per month for each additional of such children to a maximum of two thousand five hundred fifty dollars per month until they become emancipated or reach the age of eighteen years; and if there are no widow or widower, child, or children entitled thereto, then to his or her parents or either of them the sum of one thousand two hundred seventy-five dollars per month for life, if it is proved to the satisfaction of the board that the parents, or either of them, were dependent on the deceased for their support at the time of his or her death. In any instance in subsections (1) and (2) of this section, if the widow or widower, child or children, or the parents, or either of them, marries while receiving such pension the person so marrying shall thereafter receive no further pension from the fund.

(3) In the case provided for in this section, the monthly payment provided may be converted in whole or in part into a lump sum payment, not in any case to exceed twelve thousand dollars, equal or proportionate, as the case may be, to the actuarial equivalent of the monthly payment in which event the monthly payments shall cease in whole or in part accordingly or proportionately. Such conversion may be made either upon written application to the state board and shall rest in the discretion of the state board; or the state board is authorized to make, and authority is given it to make, on its own motion, lump sum payments, equal or proportionate, as the case may be, to the value of the annuity then remaining in full satisfaction of claims due to dependents. Within the rule under this subsection the amount and value of the lump sum payment may be agreed upon between the applicant and the state board.

Sec. 3. RCW 41.26.048 and 2007 c 487 s 2 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) <u>seventy-five</u> thousand dollar death benefit shall be paid to the member's estate, or such person or

persons, trust or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's death benefit shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) The benefit under this section shall be paid only when death occurs: (a) As a result of injuries sustained in the course of employment; or (b) as a result of an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 4. RCW 41.32.053 and 2007 c 487 s 3 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member has nominated by written designation duly executed and filed with the department. If no such designated person or persons are still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 5. RCW 41.35.115 and 2007 c 487 s 4 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member has nominated by written designation duly executed and filed with the department. If no such designated person or persons are still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 6. RCW 41.37.110 and 2007 c 487 s 5 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or the person or persons, trust, or organization the member has nominated by written designation duly executed and filed with the department. If the designated person or persons are not still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 7. RCW 41.40.0931 and 2007 c 487 s 6 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit for members who had the opportunity to transfer to the law enforcement officers' and firefighters' retirement system pursuant to chapter 502, Laws of 1993, but elected to remain in the public employees' retirement system, shall be paid to the member's estate, or such person or persons, trust, or organization as the member has nominated by written designation duly executed and filed with the department. If there is no designated person or persons still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) Subject to subsection (3) of this section, the benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment as a general authority police officer; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

(3) The benefit under this section shall not be paid in the event the member was in the act of committing a felony when the fatal injuries were suffered.

Sec. 8. RCW 41.40.0932 and 2007 c 487 s 7 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member has nominated by written designation duly executed and filed with the department. If no such designated person or persons are still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 9. RCW 43.43.285 and 2007 c 488 s 1 and 2007 c 487 s 9 are each reenacted and amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's death benefit shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2)(a) The benefit under this section shall be paid only where death occurs as a result of (i) injuries sustained in the course of employment; or (ii) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

(b) The retirement allowance paid to the spouse and dependent children of a member who is killed in the course of employment, as set forth in RCW 41.05.011(14), shall include reimbursement for any payments of premium rates to the Washington state health care authority under RCW 41.05.080.

NEW SECTION. **Sec. 10.** This act is necessary for the immediate preservation of the public peace, health, or safety, or support of the

state government and its existing public institutions, and takes effect immediately.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/08**	**Z-0399.1 / Z-0400.1**

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 and the Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board throughout the 2008 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 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 increases the amount of the duty-related death benefit from $150,000 to $175,000. Current law provides the duty-related death benefit to members of all state retirement systems and other public employees who die from duty-related illnesses or injuries.

Impact on Pension Liability

(Dollars in Millions)	Current	Increase	Total
Today's Value of All Future Pensions	$67,081	$2.6	$67,083
Earned Pensions Not Covered by Today's Assets	$4,957	$0.1	$4,957

Impact on Contribution Rates: (Effective 9/1/2009)

2009-2011 State Budget	PERS	TRS	SERS	PSERS	LEOFF	WSPRS
Employee (Plan 2)	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Employer:						
Current Annual Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Total	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
State					0.00%	

Budget Impacts

(Dollars in Millions)	2009-2011	2011-2013	25-Year
General Fund-State	$0.0	$0.1	$3.5
Total Employer	$0.0	$0.4	$11.1

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 following retirement systems and public employees:

- Public Employees' Retirement System (PERS).
- Teachers' Retirement System (TRS).
- School Employees' Retirement System (SERS).
- Public Safety Employees' Retirement System (PSERS).
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF).
- Washington State Patrol Retirement System (WSPRS).
- Volunteer Firefighters' Relief and Pension Fund (VFF).
- Members of the Judicial Retirement System (JRS).
- Members of the Higher Education Retirement Plans (HIED).
- State, school district, and higher education employees who aren't members of a state retirement system.

This proposal increases the amount of the duty-related death benefit from $150,000 to $175,000.

Assumed Effective Date: Immediately upon passage

What Is The Current Situation?

The retirement systems and, in some cases, the state general fund pay a lump-sum death benefit for public employees who die as a result of a duty-related injury or illness. The amount of the benefit is currently $150,000. This benefit is provided for all members of PERS, TRS, SERS, PSERS, LEOFF, WSPRS, VFF, JRS, and HIED; and to state, school district and higher education employees who aren't members of a state retirement system. The lump-sum death benefit in VFF includes an additional $2,000.

Who Is Impacted And How?

This proposal could affect all 308,267 active members of the systems listed above through improved benefits. In addition, this proposal could affect 577 inactive fire fighters of LEOFF who are eligible for the benefit up to five years after separation of service. However, we only expect this benefit to be paid to about one member out of 24,500 members per year.

This proposal will increase the lump-sum death benefit by $25,000 for any member that dies as a result of a duty-related injury or illness.

Although this proposal does not produce supplemental contribution rate increases in the current biennium, this proposal impacts all 165,035 Plan 2 members of these systems through increased contribution rates in future biennia. With the exception of WSPRS members, this proposal will not affect member contribution rates in Plan 1 since they are

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fixed in statute. Additionally, this proposal will not affect member contribution rates in Plan 3 since Plan 3 members do not contribute to their employer-provided defined benefit.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This proposal increases the amount of the lump-sum death benefit by $25,000. This increases the present value of future benefits of the affected systems. This proposal will not result in more lump-sum death benefits being paid, but when the benefits are paid, the amount will be larger.

Who Will Pay For These Costs?

Each system will subsidize the increase in liability that results from this proposal in their normal funding method:

- LEOFF 2: 50 percent member, 30 percent employer, and 20 percent State
- Plan 1: 100 percent employer
- Plan 2: 50 percent member and 50 percent employer
- Plan 3: 100 percent employer

HOW WE VALUED THESE COSTS

We changed the lump-sum duty death benefit to provide a $175,000 benefit in place of the current $150,000 benefit. We assumed no members of JRS will die from a duty-related illness or injury and have excluded these members from this pricing.

Otherwise, we developed these costs using the same assumptions, methods, assets, and data as disclosed in the June 30, 2007 Actuarial Valuation Report (AVR).

We used the Entry Age Normal actuarial funding method to determine the fiscal budget changes for future new entrants. We used the Aggregate actuarial funding method to determine the fiscal budget changes for current plan members.

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ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of the plans by increasing the present value of future benefits payable under the plans as shown in the following table.

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)*			
PERS 1	$14,061	$0.0	$14,061
PERS 2/3	20,634	0.7	20,635
PERS Total	**34,695**	**0.7**	**34,696**
TRS 1	11,021	0.0	11,021
TRS 2/3	7,078	0.1	7,078
TRS Total	**18,099**	**0.1**	**18,099**
SERS 2/3	**2,698**	**0.2**	**2,698**
PSERS 2	**225**	**0.0**	**225**
LEOFF 1	4,358	0.1	4,358
LEOFF 2	6,149	1.5	6,151
LEOFF Total	**10,507**	**1.6**	**10,509**
WSPRS 1/2	**$856**	**$0.0**	**$856**
Unfunded Actuarial Accrued Liability *(The Portion of the Plan 1 Liability that is Amortized to 2024)*			
PERS 1	**$3,609**	**$0.0**	**$3,609**
TRS 1	**2,288**	**0.0**	**2,288**
LEOFF 1	**($939)**	**$0.1**	**($939)**
Unfunded PUC Liability *(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)*			
PERS 1	$3,990	$0.0	$3,990
PERS 2/3	(2,470)	0.7	(2,469)
PERS Total	**1,520**	**0.7**	**1,521**
TRS 1	2,552	0.0	2,552
TRS 2/3	(1,229)	0.1	(1,229)
TRS Total	**1,323**	**0.1**	**1,323**
SERS 2/3	**(443)**	**0.2**	**(443)**
PSERS 2	**(2)**	**0.0**	**(2)**
LEOFF 1	(975)	0.1	(975)
LEOFF 2	(974)	1.5	(972)
LEOFF Total	**(1,949)**	**1.6**	**(1,947)**
WSPRS 1/2	**($121)**	**$0.0**	**($121)**

Note: Totals may not agree due to rounding.

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In addition, this proposal increases the pension liability of the VFF pension plan by $128,000.

We did not value the impact of this proposal on the following members since we do not currently value them in any of our actuarial valuations:

- 2,854 Volunteer Fire Fighters that are not members of the pension plan;
- Members of HIED; and
- State, school district, and higher education employees who aren't members of the Washington State Retirement Systems.

How Contribution Rates Changed

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01%, therefore the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate increase to measure the fiscal budget changes in future biennia.

Impact on Contribution Rates: (Effective 9/1/2009)

System/Plan	PERS	TRS	SERS	PSERS	LEOFF	WSPRS
Current Members						
Employee (Plan 2)	0.001%	0.000%	0.001%	0.000%	0.005%	0.003%
Employer:						
Normal Cost	0.001%	0.000%	0.001%	0.000%	0.003%	0.003%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.001%	0.000%	0.002%	0.000%	0.003%	0.003%
State					0.002%	
New Entrants*						
Employee (Plan 2)	0.001%	0.000%	0.002%	0.001%	0.008%	0.005%
Employer:						
Normal Cost	0.001%	0.000%	0.002%	0.001%	0.005%	0.005%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.001%	0.000%	0.002%	0.001%	0.005%	0.005%
State					0.003%	

**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.*

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How This Impacts Budgets And Employees

	Budget Impacts						
(Dollars in Millions)	**PERS**	**TRS**	**SERS**	**PSERS**	**LEOFF**	**WSPRS**	**Total**
2009-2011							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2011-2013							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.1	$0.0	$0.1
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**0.1**	**0.0**	**0.0**	**0.0**	**0.1**	**0.0**	**0.2**
Local Government	0.1	0.0	0.0	0.0	0.1	0.0	0.2
Total Employer	**0.1**	**0.0**	**0.1**	**0.0**	**0.2**	**0.0**	**0.4**
Total Employee	**$0.1**	**$0.0**	**$0.0**	**$0.0**	**$0.2**	**$0.0**	**$0.3**
2009-2034							
General Fund	$0.6	$0.2	$0.6	$0.0	$2.1	$0.0	$3.5
Non-General Fund	0.9	0.0	0.0	0.0	0.0	0.2	1.1
Total State	**1.5**	**0.2**	**0.6**	**0.0**	**2.1**	**0.2**	**4.6**
Local Government	2.3	0.1	0.9	0.0	3.1	0.0	6.5
Total Employer	**3.9**	**0.4**	**1.5**	**0.0**	**5.1**	**0.2**	**11.1**
Total Employee	**$2.6**	**$0.2**	**$0.9**	**$0.0**	**$5.1**	**$0.2**	**$9.1**

Note: Totals may not agree due to rounding.

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

As with the costs developed in the actuarial valuation, the emerging costs of the systems 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 used in this pricing, we varied the duty-related death assumption for LEOFF 2. We chose LEOFF 2 for our sensitivity testing for two reasons:

1. We developed our current duty-related death assumptions for LEOFF 2 in 2006 and 2007 in response to new laws for duty-related injuries and illnesses. We have not had sufficient experience in the plan to determine if these assumptions are accurate in the long-term. As a result, there is a higher risk for this pricing with LEOFF 2.

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2. If we experience any catastrophic events impacting duty-related injuries or illnesses that result in death, we expect this will affect our law enforcement officers and fire fighters. A single catastrophic event, while short-term, could add a significant cost to the plan, particularly with lump-sum benefits.

We changed the duty-related death assumption by doubling the rate of deaths that we expect will result from a duty-related injury or illness. We did not increase our mortality assumptions, only the number of deaths that are duty-related. The next table shows our current assumptions ("Base Assumptions") and increased assumptions ("Sensitivity Assumptions").

	Base Assumptions	**Sensitivity Assumptions**
Duty Death Rate	0.0376%	0.0752%
Occupational Disease Death Rate (Fire Fighters only)		
Age 20-49	14.742%	29.484%
Age 50+	27.393%	54.786%

The result of increasing the rate of deaths from a duty-related injury or illness is detailed in the following table. We compare the assumptions used in this proposal ("Best Estimate Pricing") with the increased assumptions ("Sensitivity Pricing") to show the sensitivity of this pricing proposal on the duty-related death assumptions.

(Dollars in Millions)	**Best Estimate Pricing**	**Sensitivity Pricing**
Liability Increase	$1.5	$2.4
Contribution Rate Increase		
Employee	0.005%	0.008%
Employer	0.003%	0.005%
State	0.002%	0.003%
Budget Impacts		
2009-2011		
General Fund - State	$0.0	$0.0
Total Employer	$0.0	$0.3

There is also a possibility that fewer duty-related deaths will occur than we assume for LEOFF 2 in the future. If we tested lower rates, we would expect lower costs than our pricing of this proposal shows.

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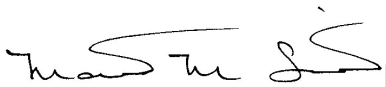
ACTUARY'S CERTIFICATION

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. This draft fiscal note has been prepared for the Select Committee on Pension Policy and Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board.
6. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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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.

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Office of
The State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

May 12, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

On behalf of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board (Board), I would like to thank you for the cooperative working relationship we have shared in the past and look forward to a similar partnership in the future.

I would like to bring several topics back to your attention as you begin preparation for the 2008 interim. It is our hope that the Select Committee on Pension Policy (SCPP) and the Board can work cooperatively on these issues to once again develop legislation. I have provided a brief summary of each topic for your reference:

Interruptive Military Service Credit
Working cooperatively last interim, the Board and the SCPP jointly endorsed a bill that would have eliminated a member's obligation to pay for interruptive military service credit if the member served during a period of war. The Board is once again interested in working cooperatively with the SCPP on the issue and feels the following additional question will need to be further explored:

- Should the benefit apply to all periods of interruptive military service which have not yet been recovered?

Inflationary Adjustment for $150,000 Death Benefit
The Board is interested in once again working with the SCPP to further study the effect of adding an inflationary adjustment to all the state retirement plans that provide the $150,000 death benefit. In addition to last year's study the Board feels following issues will need to be explored further:

- Should an adjustment in the lump sum amount be made to account for inflation since the creation of the benefit?

- Should both the lump sum adjustment and the addition of the inflationary adjustment be included in the bill?

Military Service Death Benefit

The Board and the SCPP jointly recommended legislation to the 2008 Legislature, which would have provided an unreduced annuity to qualifying survivors of members of all plans, who leave employment due to service in the National Guard or Reserves and die while in military service, during a period of war. The Board would like to continue our joint work to eliminate the "early retirement" actuarial reduction applied to the pensions of members who die while honorably serving our country.

Fish and Wildlife Enforcement Officer Service Credit Transfer

The Board and the SCPP also jointly recommended legislation last session that would have permitted Department of Fish and Wildlife Enforcement Officers to transfer service credit earned in the Public Employees' Retirement System (PERS) Plan 2 as enforcement officers into the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2. The Board feels the following issue may need to be further explored as well:

- Should PERS 3 members be included in the transfer group?

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

We would be happy to meet with you to discuss these topics at an upcoming SCPP or LEOFF Plan 2 Retirement Board meeting. Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly Fox, Chair

cc: Matt Smith, State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
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P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

June 30, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

At the recent meeting of the Select Committee on Pension Policy (SCPP) the chairman requested that the Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board (LEOFF 2 Board) provide a prioritized list of the suggested joint topics that the LEOFF 2 Board would like to work on cooperatively with the SCPP.

During the course of the most recent LEOFF 2 Board meeting we prioritized the suggested topics for cooperation in the following order:

1. **Fish and Wildlife Enforcement Officer Service Credit Transfer**
   Allow FWEO members to transfer their PERS Plan 2 service as enforcement officers to LEOFF Plan 2.

2. **Inflationary Adjustment for $150,000 Death Benefit**
   The $150,000 lump-sum death benefit paid to survivors of public employees who die in the line of duty is not adjusted for inflation.

3. **Interruptive Military Service Credit**
   Members whose public employment is interrupted by military service are required to pay member contributions in order to purchase service credit.

4. **Military Service Death Benefit**
   Beneficiaries of members who die while serving on active duty with the United States Military do not qualify for duty related death benefits.

5. **Purchase of Annuity**
   Members are limited in the amount of money they can convert to a defined benefit by the amount required to purchase 5 years of service.

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly Fox, Chair

cc: Matt Smith, State Actuary

Change Membership Default For Plans 2/3

Description Of Issue

The SCPP considered the plan choice default in the Plans 2/3 of the Public Employees' Retirement System (PERS), Teachers' Retirement System (TRS), and the School Employees' Retirement System (SERS). A member requested that new employees who failed to choose between Plan 2 or Plan 3 to become permanent members of Plan 2 by default. The current default plan is Plan 3.

This request raises two immediate policy questions:

- Should the plan default be changed, particularly at this time?
- If so, how should the default be determined?

Policy Highlights

- Have the values changed that made the Plan 3 design the policy preference for the default plan?
- There may be issues with changing the default at this time.
  - Legal considerations.
  - Financial market conditions.
- If policy makers don't have a policy preference for continuing the Plan 3 default, how should they decide which plan should be the default?
  - Look at historical data of plan choice preference?
  - Determine which plan best serves the needs of new employees?

Policy Options For Changing Membership Default

Policy makers who wish to change the membership default may consider the following options:

- **Option 1: Change The Default Plan To Plan 2 For PERS, TRS And SERS.**
  - Maintains consistency between the plans.
  - Ensures members are not defaulted into plan with more investment risk.
  - Doesn't address possible legal or market-driven policy concerns.
- **Option 2: Change The Default Plan To Plan 2 For PERS Only.**
  - Eliminates legal concerns related to optional membership for TRS and SERS new employees.
  - Ensures members are not defaulted into plan with more investment risk.
  - Doesn't address possible concern over decision being market-driven.

Committee Activity

Staff briefed the Committee on this issue in November. The Committee held a public hearing and took executive action in December. The Committee moved to recommend Option 2 to the Legislature.

Recommendation To 2009 Legislature

Change the default retirement plan from Plan 3 to Plan 2 for new members of PERS who do not select a plan upon hire.

Staff Contact

Dave Nelsen, Senior Policy Analyst
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nelsen.dave@leg.wa.gov

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Change Membership Default for Plans 2/3

In Brief

ISSUE

New employees hired into PERS, TRS, or SERS eligible positions must choose to be a member of Plan 2 or Plan 3. Members who don't choose are "defaulted" into membership in Plan 3. Stakeholders have suggested that members who don't choose should be defaulted into Plan 2.

MEMBER IMPACT

This change would impact all new hires into PERS, TRS, and SERS eligible positions. Since the inception of optional membership, beginning for PERS in March 2002, over 95,000 new employees have been faced with the Plan 2 or Plan 3 choice. Of these, nearly 18,000 have been defaulted into Plan 3. See Appendix A for more information.

Dave Nelsen
Senior Policy Analyst
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Introduction

The SCPP is being asked to change the optional plan choice default provisions in the Plans 2/3 of the Public Employees' Retirement System (PERS), the Teachers' Retirement System (TRS), and the School Employees' Retirement System (SERS). The requested change would require new employees who failed to choose Plan 2 or Plan 3 to become permanent members of Plan 2 by default. Currently, new employees who fail to choose a plan are permanently defaulted into membership in Plan 3. This request raises two immediate policy questions:

- Should the plan default be changed, particularly at this time?
- If so, how should the default be determined?

Current Situation

New employees hired into eligible positions in PERS, TRS, and SERS have ninety days from their first day of employment to choose whether to become members of Plan 2 or Plan 3. New employees who do not decide within the ninety-day window become members of Plan 3 by default. Whether members choose or are defaulted into a plan, their plan designation cannot change; the decision or designation is irrevocable.

History

TRS Plan 3, implemented in 1995, was the first Plan 3 in Washington State. At the time, all new teachers were required to be members of Plan 3. This was also true for SERS Plan 3, implemented in 2000. Classified employees hired after 2000 were also required to become members of SERS Plan 3.

The choice of Plan 3 as the default plan began with the implementation of PERS Plan 3 in March 2002. When PERS Plan 3 was created, the Legislature gave new public

Using Plan 3 as the default plan started with PERS in 2002 and was later expanded to TRS and SERS in 2007.

employees the irrevocable choice upon hiring to become a member of Plan 2 or Plan 3. If a new employee failed to make a choice, they were defaulted into PERS Plan 3.

In 2007, the Legislature continued to use Plan 3 as the default plan when they implemented optional membership in TRS and SERS. These benefits, and others, were passed in HB 2391, which also repealed the provisions of gain-sharing. Some of the provisions of this bill are currently being litigated.

Comparing Plan 2 And Plan 3

Plan 2 and Plan 3 provide different designs to accrue a retirement benefit. Understanding the differences in the design of the two plans may help policy makers understand the potential impact of changing the default plan to future new employees.

Below is a description of the benefit design provided by each plan.

Plan 2 is a defined benefit plan that provides a monthly payment for life based upon a formula.

Plan 2 is a **defined benefit retirement plan** that provides a monthly payment for life based upon a formula. The benefit is defined because the formula is known. The Plan 2 benefit formula is: 2% X years of service X salary average. The Plan 2 benefit is funded by equal employee and employer contributions, which may vary over time depending upon the funding needs of the plan. The full benefit is guaranteed by the state of Washington, so employees do not carry the investment risk for their benefits, the state does.

Some Benefits Of Plan 2

Plan 2 offers a cost effective method to provide replacement income at retirement.

For a new employee who will remain a member until retirement, DB plans, like the Plans 2, are generally a very cost effective method to provide lifetime retirement income*.

First, because they "pool" all members into a common fund, defined benefit plans only have to collect enough contributions and earnings to fund the "average" lifetime of the member. Members who fund their own retirement would have to contribute and earn more in order to ensure they wouldn't outlive their savings if they lived longer than the average.

Second, because large defined benefit plans invest over a very long time horizon, they can afford to take on more investment risk, which should lead to higher returns. Individual members are often advised to change their investment allocations to less risky products as they near and enter retirement, which leads to lower lifetime investment returns.

Finally, defined benefit plans generally achieve higher investment returns than individual investors. Defined benefit plans use investment professionals, have access to investment asset classes that individuals typically don't, and can use their size to negotiate lower investment fees. Over a long career, a small increase in investment returns can provide a significantly higher benefit.

* Beth Almeida and William Fornia, "A Better Bang for the Buck," *National Institute on Retirement Security,* <http://www.nirsonline.org/index.php>, August 2008, <http://www.nirsonline.org/storage/nirs/documents/ky_dc_working_group.pdf>, accessed August 2008.

Plan 2 offers members a lower risk retirement plan that requires little involvement in managing the benefit.

Plan 2 is also of value to members who don't want to assume the primary responsibility and risk for their own retirement funding. In a defined benefit plan, the plan sponsor assumes the responsibility and the risk to invest and provide a retirement benefit for the employees. This provides the member with a secure, known benefit that is guaranteed. For members who lack the investment confidence, the desire to more directly manage their retirement income, or the time to accrue substantial earnings, this option can be desirable. However, members do still bear the responsibility to determine if the amount provided by the plan is sufficient for their own retirement needs, and make additional plans if it is not.

Plan 3 is a **hybrid retirement plan**, because it contains two separate components:

- A defined contribution account.
- A defined benefit account.

The *defined contribution* account is funded by the member's own contributions. The plan gives members the choice of how much they want to contribute to their own retirement, and options to manage investing those contributions over time. Currently, Plan 3 members have six contribution rate options, beginning at 5 percent, and over nine separate investment funds from which to choose.

New employees, who become members of Plan 3 by default, are also defaulted into a contribution rate of 5 percent and into an investment option that provides the same mix of investments and rate of return as the retirement trust funds managed by the Washington State Investment Board (WSIB).

Plan 3 has both a defined contribution and defined benefit component.

This is called a "defined contribution" account because the benefit received by members from the account is not defined, only the amount of contributions into the account is defined. The benefit received from the account is based upon how much members contribute and the associated investment earnings. There is no guaranteed return on the contributions, so members carry the full investment risk. This type of retirement option is very similar to the "401K" retirement plans commonly offered by private employers.

The *defined benefit* account in Plan 3 is paid by the employer contributions. The defined benefit provided is similar to the Plan 2 defined benefit, a lifetime monthly payment based upon a formula, guaranteed by the state. However, because member contributions are not funding the defined benefit in Plan 3 like they are in Plan 2, the value is half that of the Plan 2 benefit. The Plan 3 defined benefit formula is: 1% X years of service X salary average.

Some Benefits Of Plan 3

Plan 3 offers members more value if leaving the workforce before retiring.

Many new employees will never draw a lifetime monthly payment from their retirement plan. It is estimated that less than half of all new PERS employees will remain employed for the five years necessary to earn a guaranteed benefit at age 65*. Also, some new employees may work long enough to earn a benefit, but will leave public employment prior to age 65. The Plans 3 were designed in recognition of this new, more mobile workforce. The policy statement in the legislation that created TRS Plan 3 stated "...public employees need the ability to make transitions to other private or public sector careers, and ... the retirement system should not be a barrier...."

To accommodate this recognition of greater mobility, Plan 3 provides more opportunity to receive value for both member and employer contributions should employees leave employment prior to retirement. In Plan 2, members who leave employment can withdraw the contributions

made to the plan and any interest that has been credited to their account. However, if they do so, they forfeit all right to a future defined benefit from the system. This means Plan 2 members who withdraw never receive any benefit from all the contributions made by the employer.

In Plan 3, the benefit is split into the defined contribution and the defined benefit accounts. Plan 3 members who leave prior to retirement can withdraw their contributions from the defined contribution account, and it does not impact their eligibility for an employer-funded defined benefit payment in the future. If Plan 3 members earn a guaranteed future payment, they retain the value from the employer contributions.

* Office of the State Actuary, *2007 Actuarial Valuation Report*, September 2008.

Plan 3 gives members greater flexibility and control within their retirement plan.

Plan 3 also offers members more control over their retirement planning. With the increased awareness of the stock market in the late 1980s and early 1990s, many employees wanted flexibility and control over their retirement contributions. Plan 3 provides flexibility in the amount of contributions and control over how they are invested. Plan 2 does not provide these benefits. Even if the new employees do not choose Plan 3 initially, this flexibility and control may be desired later in their career.

However, with this increased flexibility and control comes increased risk. Members in Plan 3 are assuming more risk for their future retirement benefit than Plan 2 members. Part of the benefit from Plan 3 comes from the members own contributions and earnings, on which there is no guaranteed return. Therefore, depending upon the amount invested and the earnings, members may or may not have as much income replacement at retirement as Plan 2 members may have.

Plan 3 shifts some risk of providing a retirement benefit to members, but provides features to help mitigate that risk.

Some policy makers may question whether a plan designed for active management that shifts some retirement risk to members is appropriate for new employees who cannot choose a retirement plan in ninety days. While there is more risk to members in this plan, there are several design options within Plan 3 that attempt to mitigate some of that risk.

First, as stated earlier, members who are defaulted into Plan 3 are also defaulted into the WSIB investment option. This provides them with access to a professionally

managed, low-fee, and diverse investment portfolio, the same portfolio that funds the defined benefit plans in Washington. This option mitigates some of the risk for individual investors.

Second, the Plans 3 provide an option for members to purchase a lifetime monthly annuity with their contributions at the time of retirement, paid out of the state retirement funds. Because this annuity is purchased from the state, it provides more benefit for less cost than what could typically be purchased in the private sector, and removes some of the risk of members outliving the value of their investments.

Finally, members still receive a defined benefit payment funded from the employer contributions. This ensures there is some level of secure monthly income being earned.

Policy Analysis

The request to change the plan membership default in the Plans 2/3 raises two immediate policy questions:

- Should the default be changed, particularly at this time?
- If so, how should the default be determined?

Should The Plan Default Be Changed?

As discussed earlier in this paper, Plan 3 was the original choice as the default plan for PERS, and has remained the default choice as optional membership was expanded to TRS and SERS. As shown in **Appendix A**, nearly 18,000 members have been defaulted into Plan 3 since the creation of optional membership. This amounts to approximately 19 percent of all new employees.

The question for policy makers is: Have the values changed that made the Plan 3 design the policy preference for the default plan?

The Plan 3 design offers value for the mobility and flexible retirement planning needs of many new employees. For employers, it offers a retirement plan that helps recruit from the private sector, which primarily offers defined

Have the values changed that made the Plan 3 design the policy preference for the default plan?

contribution retirement plans for employees. For the state of Washington, as the plan sponsor, the Plan 3 design shifts some of the investment risk for providing a benefit to members, and lowers the long-term cost of the plan that the state guarantees. As explained earlier, the Plan 3 members carry the investment risk for their own contributions, and the state guarantees the value of the defined benefits paid by employer contributions. Since the Plan 3 defined benefit is half the value of the Plan 2 defined benefit, the state accrues less liability with Plan 3. Shifting the investment risk and lowering the long-term liability were key benefits to the state of implementing Plan 3 and designating Plan 3 as the default plan.

Have the values in the Plan 3 design changed? Do policy makers no longer consider lowering the long-term liability for the state a goal? If the values discussed above have not changed, then some reason must override the design values in significance to consider changing the current plan default. Otherwise, retaining Plan 3 as the default plan would be the consistent approach.

Should The Default Be Changed At This Time?

Changing the plan default at this time may raise legal concerns.

In addition to the question of whether the Plan 3 default should be changed at all, there are also two concerns raised by the timing of this request. First, as mentioned earlier, the Legislature continued the use of Plan 3 as the default plan when they implemented plan choice for TRS and SERS in HB 2391. Some of the benefit provisions in this bill are in current litigation, and the provisions of plan choice may be impacted by the outcome of this litigation. As a result, the committee may want to consult with their Assistant Attorney General before making a decision on this proposal.

Policy makers may want to consider whether the desire to change the default from Plan 3 may be linked to current market conditions.

Second, policy makers may want to consider whether the desire to change Plan 3 as the default may be linked to current market conditions. As discussed earlier, in Plan 3 members invest their contributions. When the financial markets are in a downturn, as they are now, the reaction to this financial climate may be that this exposure to investment risk is too great for members to accommodate. Therefore, some feel Plan 2 should be the default plan because the benefit is guaranteed and the state, as plan sponsor, should carry the investment risk, not members. This

reaction may not fully consider the cyclical nature of the financial markets. The markets have had periods of tremendous gain, as well as loss. Volatility is part of their nature. When the financial markets are earning significant returns, will there be another request to change the default back to Plan 3 so members can participate in the gains?

How Should The Plan Default Be Determined?

If policy makers no longer feel Plan 3 should be the default plan for new employees from a broad-based policy perspective, then how should they choose which plan should be the default? Two possible approaches are:

- Use historical plan choice data to set the default.
- Determine which plan best serves the needs of new employees.

Using Historical Data To Set Plan Default

Appendix A provides detail of new employee choice in the Plans 2/3. PERS has had optional membership since March of 2002, so there is more historical data available. In PERS, over 64 percent of new employees choose Plan 2. An additional 17 percent choose Plan 2, and the remaining 19 percent are defaulted into Plan 3. This data indicates a strong preference in PERS for Plan 2.

Historical data shows a strong preference for Plan 2 among PERS employees, but the data is somewhat less clear for school employees and

SERS data also indicates a preference for Plan 2 of 48 percent to 32 percent choosing Plan 3. The remaining 20 percent are defaulted into Plan 3. TRS new members have a slight preference for Plan 3 of 46 to 40 percent choosing Plan 2. The remaining 14 percent of new teachers are defaulted to Plan 3.

While this data does show a strong preference for Plan 2 among PERS employees, the data is somewhat less clear for school employees and teachers. Also, since optional membership for SERS and TRS was implemented only 16 months ago, there is far less data in those plans from which to base a decision. If taking the approach to use historical data to determine the plan default choice, policy makers may want to consider whether enough data is available in SERS and TRS to make an informed choice.

Which Plan Best Serves The New Employees?

Policy makers may also set the plan default based upon a judgment of which plan best serves the new employees. This determination is complicated; however, as Plan 2 and Plan 3 were each designed to best serve the needs of different members. As discussed earlier in this paper when comparing the benefits in the two plans, Plan 2 may provide more value to the new employees who stay and retire from the system, or who don't want the primary responsibility or the risk of managing their own retirement. Plan 3 may be preferable for the new employees who will likely leave public employment prior to retirement, or those who may remain, but want more flexibility and options than a typical defined benefit plan provides.

Policy makers would need to determine which group of new members they would like to best serve. Those new employees who will stay to retirement age may be benefited by a Plan 2 default, and those who leave prior to retiring may be benefited by a Plan 3 default.

Should There Be Different Defaults For Different Members?

Instead of one default for all retirement systems, other approaches could include defaults based upon each system's demographics, or plan default based upon groupings of new employees.

Applying one default plan for all the Plans 2/3 would necessarily mean some members are defaulted into a plan that may not be best suited for their needs. A different approach may be to fit the default to the demographics of new employees in the retirement system. For example, PERS and SERS new employees are far more likely to leave the workforce prior to the normal age of retirement than new TRS employees. Would a Plan 3 default suit these employees better since it may provide more value to a departing worker? If new employees in TRS are more likely to work to the normal age of retirement, should they be given a Plan 2 default since Plan 2 is a cost effective means of providing retirement income? This approach could result in different default plans among the three retirement systems.

Another approach would be to fit the default to groupings of new employees specifically. For example, Plan 3 may be more valuable to younger employees who have time to invest and manage their contributions through market volatility. Plan 3 may be a logical choice as the default for these new employees. But what of new employees that

enter the workforce at later ages? They may not have time to earn significant investment gains in Plan 3. New employees past a certain age may benefit from being defaulted into Plan 2. This approach could result in different plan defaults within each retirement system.

Other States

Among the comparative states, only two systems offer new employees a choice between a defined benefit plan and some form of defined contribution or hybrid plan, Ohio PERS and the Florida Retirement System.

Only two comparative systems offer similar plan choice to new employees, and both systems default members into the defined benefit option.

Ohio PERS gives new employees a choice between a traditional defined benefit plan like Plan 2, a hybrid retirement plan like Plan 3, and a defined contribution plan. If members do not choose a plan, they are defaulted into the traditional defined benefit plan.

The Florida Retirement System gives new members the option to participate in a defined benefit plan and a defined contribution plan. Like Ohio PERS, if members fail to make a timely choice, they are defaulted into the defined benefit plan.

Conclusion

There is a request to the SCPP to change the plan choice default in the Plans 2/3. Plan 3 has been the policy choice as the plan default since the inception of optional membership in 2002, and remained the default choice when optional membership was expanded in 2007. Have the plan design values that drove that default policy changed?

Is now the right time to change the plan default? There are also timing considerations concerning changing the plan default. These include possible legal concerns and the impact of the current financial markets on the desire for change.

If policy makers don't have a policy preference for continuing the use of Plan 3 as the default, how should they determine which plan should be the default?

- Look at historical data of plan choice preference?

- Make a determination of which plan best serves the needs of new employees?

A look at similar situations in comparative state systems shows that only two systems offer new employees a similar plan choice as Washington. In both of those systems, members who fail to choose within their allotted time period are defaulted into a defined benefit plan.

Committee Activity

Staff briefed the Committee on this issue in November. The Committee held a public hearing and took executive action in December. The Committee moved to recommend to the Legislature a change to the default for PERS only.

Executive Committee Recommendation

Change the default retirement plan from Plan 3 to Plan 2 for new members of PERS, TRS and SERS who do not select a plan upon hire. Recommended November 18, 2008.

Recommendation To 2009 Legislature

Change the default retirement plan from Plan 3 to Plan 2 for new members of PERS who do not select a plan upon hire. Recommended December 16, 2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0395.1/09).

Draft Fiscal Note

Attached.

Appendix A

PERS Choice Data – March 2002 through October 2008		
New Members	85,106	
New Members Opting Into Plan 2	54,067	64%
New Members Opting Into Plan 3	14,882	17%
New Members Defaulting Into Plan 3	16,157	19%

TRS Choice Data – July 2007 through October 2008		
New Members	5,189	
New Members Opting Into Plan 2	2,072	40%
New Members Opting Into Plan 3	2,387	46%
New Members Defaulting Into Plan 3	730	14%

SERS Choice Data – July 2007 through October 2008		
New Members	5,094	
New Members Opting Into Plan 2	2,443	48%
New Members Opting Into Plan 3	1,616	32%
New Members Defaulting Into Plan 3	1,035	20%

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0395.1/09

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Addressing plan membership default provisions in the public employees' retirement system.

AN ACT Relating to plan membership default provisions in the public employees' retirement system; and amending RCW 41.40.785.

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

Sec. 1. RCW 41.40.785 and 2000 c 247 s 302 are each amended to read as follows:

(1) All employees who first become employed by an employer in an eligible position on or after March 1, 2002, for state agencies or institutes of higher education, or September 1, 2002, for other employers, shall have a period of ninety days to make an irrevocable choice to become a member of plan 2 or plan 3. At the end of ninety days, if the member has not made a choice to become a member of plan 2, he or she becomes a member of plan 2 or plan 3 as follows:

(a) He or she becomes a member of plan 3 if first employed by an employer in an eligible position on or after March 1, 2002, but prior to July 1, 2009, for state agencies or institutes of higher education, or on or after September 1, 2002, but prior to July 1, 2009, for other employers; or

(b) He or she becomes a member of plan 2 if first employed by an employer in an eligible position on or after July 1, 2009.

(2) For administrative efficiency, until a member elects to become a member of plan 3, or becomes a member of plan 3 by default pursuant to subsection (1) of this section, the member shall be reported to the department in plan 2, with member and employer contributions. Upon becoming a member of plan 3 by election or by default, all service credit shall be transferred to the member's plan 3 defined benefit, and all employee accumulated contributions shall be transferred to the member's plan 3 defined contribution account.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**1/05/09**	**Z-0395.1 / Z-0396.1**

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 throughout the 2008 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 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 changes the Plan 2/3 membership plan default in the Public Employees' Retirement System (PERS) from Plan 3 to Plan 2. This proposal doesn't increase the benefits or liabilities of the current PERS Plans 2/3 members, but would change future contribution levels due to assumed changes in plan membership.

Budget Impacts

(Dollars in Millions)	**2009-2011**	**2011-2013**	**25-Year**
General Fund-State	$0.0	$0.0	$2.6
Total Employer	$0.1	$0.2	$12.9

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

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WHAT IS THE PROPOSED CHANGE?

Summary Of Change

This proposal impacts the Plans 2 and 3 of PERS. This proposal would change the current plan membership default from Plan 3 to Plan 2. New employees who first become employed by an employer in eligible positions after July 1, 2009, would have 90 days to choose membership in Plan 2 or Plan 3. If the new employee does not make a choice within 90 days, they become a member of Plan 2.

For administrative ease employers report all new employees in Plan 2 until they choose membership in Plan 3. At that point the Department of Retirement Systems (DRS) transfers the member's service credit to their Plan 3 defined benefit accounts and the member's Plan 2 contributions to their Plan 3 defined contribution accounts.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

New employees who first become employed by an employer in PERS eligible positions have 90 days to choose membership in Plan 2 or Plan 3. If the new employee does not make a choice within 90 days, they become a member of Plan 3, contribute at the minimum contribution rate (5 percent), and the Washington State Investment Board invests their contributions.

For administrative ease employers report all new employees in Plan 2 until they <u>choose to join or default into</u> Plan 3. At that point DRS transfers the member's service credit to their Plan 3 defined benefit accounts and the member's Plan 2 contributions to their Plan 3 defined contribution accounts.

Who Is Impacted And How?

This proposal will impact all future members of PERS who don't choose a pension plan. This proposal does not impact the benefits of the current members of these systems.

This proposal potentially impacts all current Plan 2 members of these systems through increased contribution rates. Additionally, this bill will not affect member contribution rates in Plan 3 since Plan 3 members do not contribute to their employer-provided defined benefit.

See the Special Data Needed section of this draft fiscal note for more details.

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WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This proposal will likely increase the percentage of new entrants that go into Plan 2. Because Plan 3 is the current plan default and some members don't select a retirement plan within the 90 day window, a portion of the population enters Plan 3 by default. Instead if Plan 2 became the default, that portion of new entrants would enter Plan 2. If the cost of Plan 2 equals the cost of Plan 3 this change would not have a cost. But the costs of the plans are not necessarily equal.

The employer costs for Plan 2 and Plan 3 are basically equal. The two areas where differences in contribution rates exist include differences in plan benefit structure and differences in the people in the plans. Another area of difference between the plans that causes this proposal to change expected future budget dollars is the salaries that contributions get collected on.

We can focus on the contribution rate differences caused by plan design by comparing the cost of the same group of members valued in Plan 2 and Plan 3 separately. The employer contribution rates we calculated for PERS rounded to the same rate for both Plan 2 and Plan 3. The rates were not identical, but they were very close. The main benefit structure differences in Plan 3 include:

- Ten-year vesting. The stricter vesting requirement leads to lower retirement costs.
- Early retirement eligibility at age fifty-five with only ten years of service. A less strict early retirement standard tends to provide incentive to retire earlier. This could either increase or decrease the cost for a specific member, but the actuarial equivalence of the early retirement reduction factors tends to average the cost changes out to zero.
- Pre-retirement AFC increases for terminated members with more than twenty years of service. Increasing a member's Average Final Compensation (AFC) after they quit working in an eligible position increases costs.

The members in the plans also affect the cost of the plans. Some demographic factors impacting the cost of a plan include – average:

- Age. Older members closer to retirement generally cost more.
- Service. Higher service members tend to leave service less frequently and generally cost more.
- Salary. Higher salary members tend to receive higher pension benefits and tend to cost more.

PERS 2 members are older, have more service, and higher average salaries than PERS 3 members.

If new entrants into PERS tend to reflect similar demographic characteristics as the current active population we can expect the cost of PERS 2 to increase slightly as a result of this proposal. In PERS different demographics tend to cause the cost difference, not the benefit structure of the plans.

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The change in salaries from Plan 3 to Plan 2 causes most of the budget dollar changes we observed. Higher Plan 2 salaries cause all the budget dollar changes we see in the first biennium. They also tend to make any change in budget dollars, due to contribution rate changes in later biennia, larger.

Who Will Pay For These Costs?

To the extent the combined cost of PERS changes because of this proposal, the employers and Plan 2 members will fund those changes using the same funding method as the other costs of the plan. Employers will pay the defined benefit costs for Plan 3 members and half the cost for Plan 2 members. Plan 2 members pay for the other half of their costs.

HOW WE VALUED THESE COSTS

Assumptions We Made

We assumed the portion of new entrants going into Plan 2 would increase for PERS from two-thirds to three-quarters. We also assumed future new-entrants would have the same demographic characteristics as the new-entrants in the 2007 valuation data.

To value the impact of this proposal on member contributions – Plan 2 member defined benefit contributions and Plan 3 member defined contribution contributions – we assumed Plan 3 members contribute at an average of 6.50 percent. We also assumed the average Plan 3 member contribution rate would remain constant in the future.

For more detail please see Appendix A.

How We Applied These Assumptions

We used our liability projection system to project the current group of active members into the future. Using the new-entrant assumptions described above in combination with each system's membership growth assumption (1.25 percent in PERS), we replaced the current active members of the systems as they left active service, and allowed the active populations to increase each year. We compared the results of this new projection to our existing projections to isolate future contribution rate differences.

Special Data Needed

DRS provided us with new-entrant data for PERS. Data for PERS included new entrants from March 2002 through October 2008. The data included – the:

- Total number of new entrants into the system.
- Number of members opting into Plan 2.
- Number of members opting into Plan 3.
- Number of members defaulting into Plan 3.

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Otherwise, we developed these costs using the same assets and data as disclosed in the 2007 Actuarial Valuation Report (AVR).

For more detail please see Appendix B.

ACTUARIAL RESULTS

How The Liabilities Changed

This proposal does not impact the liabilities for the current active members of PERS.

How Contribution Rates Changed

This proposal does not impact the contribution rates for the current active members of PERS in the 2009-11 Biennium. But this proposal does change contribution rates for PERS 2/3 in future biennia. We used these rate changes to measure the budget changes in future biennia.

How This Impacts Budgets And Employees

Since contribution rates generally increase we expect higher employer contributions. Since PERS 3 members' elected contribution rates average 6.50% and we don't project PERS 2 contribution rates to ever exceed that level, the more members we expect to enter Plan 2 the lower the total member contributions we expect will be paid.

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Budget Impacts	
(Dollars in Millions)	**PERS**
2009-2011	
General Fund	$0.0
Non-General Fund	0.0
Total State	**$0.0**
Local Government	0.0
Total Employer	**$0.1**
Total Employee	**($5.3)**
2011-2013	
General Fund	$0.0
Non-General Fund	0.1
Total State	**$0.1**
Local Government	0.1
Total Employer	**$0.2**
Total Employee	**($9.0)**
2009-2034	
General Fund	$2.6
Non-General Fund	3.7
Total State	**$6.2**
Local Government	6.7
Total Employer	**$12.9**
Total Employee	**($166.0)**

Note: Totals may not agree due to rounding.

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

As with the costs developed in the actuarial valuation the emerging costs of the systems will vary from those we 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 selected for this pricing we varied the following assumptions:

- The proportion of new-entrants becoming Plan 2 members by default. We looked at the budget impacts of assuming the following percentages of new entrants becoming Plan 2 members:
  - 70 percent.
  - 80 percent.
  - 78 percent.

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Since the PERS 2 member contribution rate does not reach 6.50 percent, the average PERS 3 contribution rate, the higher the portion of new entrants who become PERS 2 members, the lower the total member contributions we expect. The table below shows the sensitivity of the budget impacts to the various new entrant splits.

	Budget Impacts			
PERS 2 / PERS 3 New Entrant Split	**75/25**	**70/30**	**80/20**	**78/22**
(Dollars in Millions)	**PERS**	**PERS**	**PERS**	**PERS**
2009-2011				
General Fund	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.1	0.1
Total State	**$0.0**	**$0.0**	**$0.1**	**$0.1**
Local Government	0.0	0.0	0.1	0.1
Total Employer	**$0.1**	**$0.0**	**$0.2**	**$0.2**
Total Employee	**($5.3)**	**($2.1)**	**($8.4)**	**($7.1)**
2011-2013				
General Fund	$0.0	$0.0	$0.1	$0.1
Non-General Fund	0.1	0.0	0.1	0.1
Total State	**$0.1**	**$0.0**	**$0.2**	**$0.2**
Local Government	0.1	0.0	0.2	0.2
Total Employer	**$0.2**	**$0.0**	**$0.5**	**$0.4**
Total Employee	**($9.0)**	**($3.7)**	**($14.3)**	**($12.2)**
2009-2034				
General Fund	$2.6	$1.5	$7.3	$5.3
Non-General Fund	3.7	2.1	10.4	7.6
Total State	**$6.2**	**$3.5**	**$17.7**	**$13.0**
Local Government	6.7	3.8	18.9	13.9
Total Employer	**$12.9**	**$7.3**	**$36.5**	**$26.8**
Total Employee	**($166.0)**	**($64.7)**	**($253.8)**	**($218.9)**

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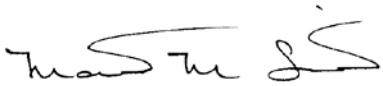
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost 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, assumptions, and data 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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APPENDIX A – ASSUMPTIONS WE MADE

In general we assume that two-thirds of all future entrants into PERS will choose to join Plan 2, and that the remaining one-third will enter Plan 3. The data provided by DRS, shown in Appendix B, shows the portion of new entrants who defaulted into Plan 3. We converted the proportions shown into values corresponding to our one-third/two-thirds assumption in the following manner for each system. The example below shows the calculations for PERS:

(1) Portion of new entrants we assume enters Plan 3 = 33 percent.
(2) Portion of new entrants who actually entered Plan 3 = 36 percent.
(3) Portion of new entrants who actually entered Plan 3 by default = 19 percent.
(4) Portion of (1) we assumed entered Plan 3 by default = (1) * (3) / (2) = 17 percent.
(5) Portion of members who defaulted into Plan 3 who we assumed did not specifically want to be in Plan 3 = 67 percent.
(6) Portion of (4) we assume would default into Plan 2 under this proposal = (4) * (5) = 12 percent.
(7) Portion of new entrants we assume enters Plan 3 under this proposal = (1) – (6) = 22 percent.

The above process led to 22 percent of new entrants becoming PERS 3 members. We assumed 75 percent of new entrants would enter Plan 2 and 25 percent would enter Plan 3.

To accurately value the impact on member contributions we had to determine what Plan 3 members currently contribute to their defined contribution accounts. DRS provided data on the current portion of Plan 3 members who selected each contribution option. The data, shown in Appendix B, provided enough information for us to determine the average PERS 3 contribution rate as of November 25, 2008. We determined that average rate to be 6.48 percent. We assumed 6.50 percent. We applied this rate to our projected PERS 3 salary streams to determine the change in member contributions caused by this proposal.

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

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APPENDIX B – SPECIAL DATA NEEDED

DRS provided the following data:

Department of Retirement Systems - Plan 3 Choice Data
October 29, 2008

PERS Choice Data – March 2002 through October 2008		
New Members	85,106	
New Members Opting Into Plan 2	54,067	64%
New Members Opting Into Plan 3	14,882	17%
New Members Defaulting Into Plan 3	16,157	19%

TRS Choice Data – July 2007 through October 2008		
New Members	5,189	
New Members Opting Into Plan 2	2,072	40%
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SERS Choice Data – July 2007 through October 2008		
New Members	5,094	
New Members Opting Into Plan 2	2,443	48%
New Members Opting Into Plan 3	1,616	32%
New Members Defaulting Into Plan 3	1,035	20%

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PERS Plan 3 Contribution Rate Data:

PERS Plan 3 membership by contribution rate option through November 25, 2008:
(Actively Contributing Members Only)

AGE	OPTION A	OPTION B	OPTION C	OPTION D	OPTION E	OPTION F	***NO OPTION	TOTAL BY AGE
	(5%)	(*)	(**)	(7%)	(10%)	(15%)		
0-34	$5,610	$1,312	$867	$350	$391	$198		8,728
35-44	3,576	1045	760	336	555	299		6,571
45-54	4,827	510	507	850	938	747		8,379
55-65	1,769	90	106	355	438	440		3,198
66-99	111	1	8	6	28	21		175
Total	**$15,893**	**$2,958**	**$2,248**	**$1,897**	**$2,350**	**$1,705**	**$63**	**$27,114**
%	59%	11%	8%	7%	9%	6%	0%	100%

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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.

DRAFT

Disability Benefits

Description Of Issue

The SCPP considered the disability benefits provided in the Plans 2/3 of the Public Employees' Retirement System (PERS), the Teachers' Retirement System (TRS), and the School Employees' Retirement System (SERS). Stakeholders submitted a proposal to the SCPP on this issue.

This issue raises two immediate policy questions:

- Should the state assume more responsibility to provide disability protection? If yes,
- Should the improvements be provided to members through pension enhancements, through insurance products, or both?

Policy Highlights

- In the design of the Plans 2/3, members have the primary responsibility to provide income replacement if disabled.
- The Plans 2/3 provide access to the value of the benefit earned to date when members become disabled.
- Not all employers offer access to disability insurance products.
- There are many ways to design a disability benefit within the retirement plans or through insurance products.
- Changing certain aspects of a disability benefit without fully studying the impacts may create additional issues to consider.

Options For Changing Plan 2/3 Disability Benefits

Policy makers who wish to address the disability benefits for members of the Plans 2/3 may consider the following options:

- **Option 1: The Original Stakeholder Proposal.**
    - Provide increased disability pension benefits to Plans 2/3 members based upon years of service and age and using the current standard for disability.

- Also requires the Washington State Institute for Public Policy (WSIPP) to study options for providing access to disability insurance to all members of the Plans 2/3.

- **Option 2: Revised Stakeholder Proposal.**
  - The same as the original stakeholder proposal except that in order to qualify for the increased pension benefits, members must meet the standard of disability used by the Social Security Administration.
- **Option 3: Insurance Study Only.**
  - This option would implement the study portion only of Option 1 and Option 2.

Committee Activity

Staff briefed the Committee on this issue in October and December. The Committee held a public hearing and took executive action in December. The Committee recommended a revised version of Option 3 to the Legislature. The revised Option 3 expands the study to include pension benefits.

Recommendation To 2009 Legislature

Direct the Washington State Institute for Public Policy, with the assistance of the Office of The State Actuary, to study options for addressing the needs of PERS Plan 2/3, TRS Plan 2/3, and SERS Plan 2/3 members for adequate disability benefit coverage.

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Disability Benefits

In Brief

ISSUE

If disability benefits should be improved, should the improvements come through modifying the pension-provided benefits, through insurance products, or both? Stakeholders have made a recommendation to improve the pension-provided benefits in the PERS, TRS, and SERS Plans 2/3 and to study supplemental insurance options.

MEMBER IMPACT

This issue impacts all members of PERS, TRS, and SERS Plans 2/3 who meet the disability standard. See Table 1 for data on current disability retirees in these systems or plans.

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Introduction

The Select Committee on Pension Policy (SCPP) is being asked to improve the disability benefits provided in the Public Employees' Retirement System (PERS), the Teachers' Retirement System (TRS), and the School Employees' Retirement System (SERS) Plans 2/3. This issue raises two immediate policy questions:

- Should the state assume more responsibility to provide disability protection for these members? If yes,
- Should the improvements be provided to members through pension enhancements, through insurance products, or both?

The SCPP has undertaken comprehensive study of disability benefits in the 2005 and 2007 Interims. This paper will not seek to reproduce all that same information, but instead will focus on the two primary questions above as it relates to PERS, TRS, and SERS Plans 2/3, the plans addressed in the stakeholder proposal. However, if the Committee chooses to move forward on this issue, additional policy considerations could be developed in a future issue paper.

See Appendix A for new information and analysis specifically related to changing the disability standard in the Plans 2/3.

Table 1

Plan 2/3 Disability Retirements
Source: 2007 Actuarial Valuation Report

	PERS		TRS		SERS	
	Plan 2	Plan 3	Plan 2	Plan 3	Plan 2	Plan 3
Count	1,549	48	87	44	156	57
Avg. Current Age	63.7	57.5	62.7	58	61.3	60.5
Avg. Yrs Retired	6.9	2.1	6.3	4.4	3.6	3.3
Avg. Benefit Received	$374	$229	$544	$210	$289	$191

Current Situation In The Plans 2/3

Currently, members have several potential sources that may provide some level of disability benefit. They are:

- Pension provided benefits.
- Insurance provided benefits.
- Other programs.

These three areas of potential disability coverage are explained in greater detail below.

Pension Benefits

A Plans 2/3 member is eligible for a disability benefit from their retirement plan when they are "totally incapacitated for continued employment by an employer." To *qualify* for the benefit, it doesn't matter how you became disabled, your age when you became disabled, or your years of service when you became disabled. An eighteen-year-old employee in their first month of employment can qualify for a disability retirement (although the value of the benefit would be quite small).

Once the Department of Retirement Systems (DRS) approves the disability, members are provided an *earned disability benefit.* This benefit type is calculated using the member's age, salary average, and years of service, and simply provides access to the benefit earned up to the point where the member left employment due to the disability. Since this typically occurs before a member was eligible to begin drawing their retirement benefit, the monthly benefit value is adjusted to reflect the longer time it will be paid out.

This monthly amount can seem small when spread over a long lifetime. It is likely that some disabled members, when shown the small monthly value of their benefit, choose instead to withdraw their contributions and interest.

The earned disability benefit for a Plans 2/3 member retiring at age 50 is actuarially reduced to 24 percent of its base amount.

Table 2 on the next page provides an example of how this type of benefit is calculated.

A PERS, TRS, or SERS Plan 2 member who becomes disabled and retires at age 50 would receive a benefit reduced to 24 percent of its base amount.

Table 2

PERS, TRS, or SERS Plan 2 Earned Disability Retirement Benefit Source: OSA	
Age	50
Average Final Compensation (AFC)	$4,000
Years of Service	20
Base Percent	40%
Base Benefit (monthly)	$1,600
Actuarial Adjustment Factor (15 yrs early)	24%
Adjusted Benefit (monthly)	$384

Note: A Plan 3 member of the same age and AFC would have a defined benefit based on a 1 percent formula; the base percent, base benefit, and adjusted benefit would be half the amounts in the above table. The Plan 3 member would also have access to the accumulations in their defined contribution account.

Insurance Benefits

In addition to the earned disability benefit within the Plans 2/3, some members may also purchase disability insurance through their employer, though not all employers provide access to insurance for their employees. The state offers benefits to all employees of state agencies and the Legislature through the Public Employees' Benefits Board (PEBB). Local government employers and school districts choose their own benefit packages for employees, of which the benefits offered by PEBB are one option.

Members may also purchase insurance benefits through their employer, though not all employers provide access and not all members with access purchase the coverage.

One example of a disability insurance program is the insurance program offered to all eligible state employees. For state employees, a small insurance benefit is provided, paid for by the state, and the member can purchase additional coverage. However, not all members choose this additional coverage. The Health Care Authority (HCA) statistics show that only 40 percent of eligible state employees actually purchase this benefit.

There is a wide variety of disability insurance benefits programs that public employers can offer. Each program can vary the qualification requirements, the amounts paid,

and the time-period over which they are paid. Typically, insurance benefits pay a percentage of the member's salary at the time of injury or illness. The percentage of salary replaced is often a choice of the holder, up to a plan maximum percentage. The policy holder can sometimes pick the period of payments, and many offer lifetime payout options. Insurance companies also offer products to address short-term disabilities and, in many cases, the short-term and long-term benefits are in the same policy. This issue paper will focus on the long-term products, as they are most comparable to pension-provided disability retirement benefits.

Other Disability Benefit Programs

Plans 2/3 members may also receive disability benefits from other state or federal programs. Members disabled because of an on-the-job injury may receive benefits from the Workers' Compensation program through the Department of Labor and Industries (L&I) or a similar "self-insured" workers' compensation program operated by their employer. Also, disability benefits are available for any member covered under the Federal Social Security program. In Washington State, most PERS, TRS, or SERS Plans 2/3 employees are covered by Social Security.

Background

This section of the issue paper provides some history of the disability provisions within the Plans 2/3, as well as some background about other methods of providing disability benefits within pension systems. Disability benefits in other plans differ from the earned disability benefit provided in the Plans 2/3. Examples of the disability benefits offered in the other retirement systems in Washington will illustrate these differences.

History

With the creation of the Plans 2 in 1977, there was a definitive shift in benefit policy. The Plans 1 in each system tended to provide additional benefits to members other than pure retirement benefits. These benefits included such items as free military service credit, medical benefits,

additional survivor payments, and enhanced benefits for disabled members. In the design of the Plans 2, many of those "non-retirement" benefits were eliminated, which reduced the long-term cost of the plans. That policy design regarding additional benefits carried into the design of the Pans 3 in the middle and late 1990s.

Legislative improvements in disability benefits have occurred over the past several years. In 2004, the SCPP sponsored legislation that created PSERS. The disability provision in the PSERS plan allows members with ten years of service credit to retire with a benefit actuarially reduced from age sixty; five years earlier than in PERS, TRS, or SERS.

The most recent improvements in disability benefits have focused on LEOFF 2 and have moved the plan away from the earned benefit design for work related disabilities.

The other legislative improvements have focused on Law Enforcement Officers' and Fire Fighters' (LEOFF) Retirement System Plan 2 disability benefits, and have moved the plan away from the earned disability benefit design used in the Plans 2/3. Changes passed in the 2004, 2005, and 2006 legislative sessions provided additional disability benefits to members who suffer a work or duty-related injury or illness.

In the 2005 and 2007 interims, the SCPP studied comprehensive disability benefits policies. However, no proposals were submitted to the Legislature based upon either study.

Other Methods Of Providing Disability Benefits Within Pension Systems

There are two other primary methods of providing disability benefits within pensions, other than the earned disability benefit method provided by the Plans 2/3. They are:

- Enhanced earned disability benefit.
- Guaranteed disability benefit.

These two methods are explained in greater detail below.

The Enhanced Earned Disability Benefit

The enhanced earned disability benefit is not fully reduced for early retirement.

This method provides members with a benefit calculated like the earned disability benefit in the Plans 2/3, but the benefit is either not fully reduced or not reduced at all for early retirement. Because the benefit is not fully reduced, the member will receive additional value over their lifetime. PERS 1 non-duty disability and TRS 1 disability are

examples of enhanced earned disability benefits. Table 3 below shows how the benefits are calculated in these plans.

Table3

TRS and PERS Plan 1 Enhanced Earned Disability Retirement Benefit Source: OSA		
Plan	**TRS 1**	**PERS 1**
Age	50	50
Average Final Compensation (AFC)	$4,000	$4,000
Years of Service	20	20
Base Percent	40%	40%
Base Benefit (monthly)	$1,600	$1,600
Adjustment Factor (per year early)	0%	2%
Adjusted Benefit (monthly)	$1,600	$1,440

This table shows the increased monthly benefit provided to disabled members in an enhanced earned benefit plan, as compared to the earned disability benefits provided to members of the Plans 2/3 (shown in Table 2), given the same age, salary average, and years of service. Again, the enhanced earned disability benefits provide additional lifetime value to the member.

The Guaranteed Disability Benefit

This type of benefit provides disability retirees with a percentage of their salary at the time they were disabled, regardless of their age and years of service. This type of benefit also typically provides more lifetime benefit than an earned disability benefit.

Table 4 on the following page provides an example of how LEOFF Plan 1 calculates its guaranteed disability benefit.

Table 4

LEOFF Plan 1 Guaranteed Disability Retirement Benefit Source: OSA	
Age	40
Final Average Salary (FAS)	$4,000
Years of Service	20
Base Percent	Always 50%
Benefit (monthly)	$2,000

A guaranteed disability benefit provides a percentage of salary, regardless of age or years of service.

As this example shows, the benefit provided is not based upon age, nor is it based upon years of service. In this guaranteed disability plan, the disabled member will always receive half of his or her salary average, even if the disability occurred in the first month of employment.

Funding The Three Methods Of Providing Disability Benefits In Pension Systems

The primary difference between these methods is how they are funded.

As explained earlier in the paper, earned disability benefits, such as in the Plans 2/3, only provide access to the benefit value already earned when the member became disabled. The value of that benefit is spread over a lifetime, resulting in the reduced monthly payment. The benefits received are funded by the individual member and employer contributions, plus interest.

Enhanced disability benefits provide greater lifetime value than the member had earned when they became disabled.

The enhanced earned disability benefit and the guaranteed disability benefit provide **greater** lifetime value to a member than what they had earned when they became disabled. This greater value is funded by additional member and employer contributions paid by *all* plan members. Essentially, the increased value of an enhanced disability benefit is subsidized by all the rest of the plan members and employers. Providing greater benefits for the few based on contributions by all can create additional policy considerations. This is what the stakeholders are proposing, and the considerations of this will be discussed later in the policy section of the issue paper.

Recap

To summarize, the three methods of providing disability benefits in the pensions are:

Earned disability benefit: Reduced benefit to spread value over a lifetime (Plans 2/3).

Enhanced earned disability benefit: Additional value added by eliminating or reducing early retirement adjustments. Additional value funded through additional contributions by all members.

Guaranteed disability benefit: Additional value added by paying a percentage of salary regardless of age or years of service when disabled. Additional value funded through additional contributions by all members.

Stakeholder Proposal

The Public Employees for Pension Reform (PEPR) coalition provided a proposal to the SCPP that increases the Plans 2/3 disability benefits.

The PEPR Coalition provided the committee with a proposal to increase the disability benefits in the Plans 2/3 and to examine options to provide standard disability insurance access to all Plan 2/3 members.

This proposal calls for an enhanced disability benefit within the Plans 2/3. This benefit would be funded by additional contributions by all members and employers. The proposal does not differentiate between duty and non-duty causes of disability (both receive the same level of benefit) nor does it call for the benefits provided to be off-set if receiving benefits from other sources, such as L&I or Social Security. The type of benefit provided is an enhanced earned disability benefit, and the standards to qualify for the benefit would remain unchanged.

The proposal also calls for expanded access to disability insurance products. This would ensure all Plans 2/3 members would have the option to purchase disability insurance, regardless of whether their employer offers the benefit.

The details of their proposal are as follows:

- **Provide an enhanced earned disability benefit to PERS, TRS, and SERS Plans 2/3 members with more than ten years of service, based on 30-year Early Retirement Reduction Factors (ERRFs)**.

- No change in current rules governing disability eligibility (duty and non-duty).
- Eligible Plans 2/3 members with 20 or more years of service could retire using an ERFF that is a reduction of 3 percent for each year of age less than 62.
- Eligible Plans 2/3 members with ten or more years of service, but less than 20 could retire using a reduction equal to 3 percent for each year of age under age 65.

❖ **Supplemental Option**: **Opt-In Disability Retirement Insurance provided through either DRS or HCA.**
The SCPP would ask the Washington State Institute for Public Policy (WSIPP) or other appropriate body to study, develop proposals, and report back on insurance product options:

- For members who do not qualify (due to less than ten years of service) for the above disability retirement provisions.
- For additional replacement income for members that do qualify for the disability retirement proposal (above), but need additional income to compensate for the reduced retirement benefit.
- Available to all Plans 2/3 members, regardless of whether their employer offers the benefit.

Policy Analysis

The two primary policy questions regarding disability benefits in the Plans 2/3 are:

1. Should the state assume more responsibility to provide disability protection? If yes,
2. Should the improvements be provided to members through pension enhancements, through insurance products, or both?

The design of the Plans 2/3 placed the responsibility to provide replacement income when disabled primarily on the member.

Should The State Assume More Responsibility?

What role should government play in the lives of its employees? As mentioned earlier, the Plans 2/3 design generally only provides traditional retirement benefits. Consequently, the disability benefit offered within the plans is only the value of the accrued service to the time of disability. This value can seem small on a monthly basis when spread over a long lifetime. However, it was never the intent in the Plans 2/3 design to have the pension system be the primary provider of income should the member become disabled. The design only ensures the member has access to his or her accrued retirement value. In contrast, benefits provided by the other plans are more generous, and provide a more substantial replacement of income when disabled.

If the plan design does not provide the primary source of replacement income, then the burden to provide that income falls to the member. Notwithstanding other forms of mandatory disability coverage, such as Social Security benefits or workers' compensation programs, this can be accomplished through employer-provided or individually obtained insurance policies. To decide to assume more responsibility for the state, therefore, would imply a judgment by policy-makers that individual responsibility in this area is not resulting in adequate coverage.

Finally, most employees will one day retire (from some employment, if not necessarily public employment), and most will also have need of medical attention at some point, but the majority of workers will not suffer a career ending disability. Are mandates for all employees appropriate when not all will ever use the benefit? Or, conversely, is the impact of the event when it does happen significant enough from a societal standpoint to ensure all are protected?

Is Individual Responsibility Working?

Many members aren't choosing to purchase insurance coverage. As previously provided, only 40 percent of state employees purchase additional disability insurance. One reason could be lack of information. Perhaps members aren't aware of the benefit, or aren't aware of the value of ensuring adequate replacement income. Another factor

could be cost. Paying premiums for a statistically unlikely occurrence may not be a high priority, particularly for new, lower-paid employees entering the workforce.

Other members can't purchase insurance coverage. Not all employers offer this benefit to their employees. Members who don't have access through their employer would have to purchase private insurance. While this is possible for some, this usually requires meeting insurability standards based upon health, age, occupation, and personal practices. These standards can be difficult to meet. Employer-provided insurance usually doesn't require meeting insurability standards if members join within a short time after becoming employed.

Is Individual Responsibility The Standard For Other Benefits?

Should the state assume what is best for the employee and mandate an "acceptable" amount of disability coverage? There are examples of this approach with regard to other government employee benefits.

For some employee benefits, such as retirement, the state assumes more responsibility and requires employee participation.

One example of mandating coverage is the mandatory membership for the retirement plans. Members generally do not have the choice to belong to one of the state-administered retirement plans. If they meet certain eligibility standards, they are *required* to belong and to contribute. It is a condition of their employment. The state also requires medical coverage for its eligible state employees. An eligible employee can only waive participation in the medical programs offered if they are covered by some other medical insurance program, such as through a spouse or other employment.

Conversely, the state does not mandate additional life or disability insurance coverage for its employees. The state pays for minimal life and disability coverage through insurance products, but does not require additional coverage beyond the minimum. While the state offers options for both, participation is voluntary and the employee pays the full cost of additional coverage. This is also true with additional savings programs, such as the deferred compensation program administered by DRS, and the health savings account administered by HCA. Both of these programs are optional to state employees, not required.

Are There Other Options Besides Expanding The Role Of The State?

If members aren't purchasing or can't provide their own adequate disability coverage, are there other options besides expanding the role of the state through pension enhancements or insurance products? One other possible approach would be through enhanced education. Perhaps enhanced member education could increase participation in the plans offered if members are choosing not to purchase adequate coverage. If members cannot participate in plans because employers do not offer disability protection as a benefit, perhaps employer education or encouragement to offer the benefits could expand access to members.

Should Disability Improvements Be Provided To Members Through The Pension System?

Disability benefits provided by the pension systems are typically lower-cost to members.

If the desire is to assume more responsibility to protect members in the event of a disability, then the next question is how to provide that protection. This can be done through changes to the benefits provided by the retirement systems or through insurance policies. Each of these methods has advantages and disadvantages.

In general, there are several positive aspects to providing enhanced benefits through the retirement systems. First, this method can provide cost advantages. The pension systems provide benefits to all members, regardless of the likelihood of becoming disabled. This means members with low risk of becoming disabled and members with a higher risk of becoming disabled are all in the same "risk pool." Insurance policies are typically purchased by members who may feel they are more likely to need the policy, due to riskier occupation or hobbies, poor health, etc. Therefore, insurance risk pools generally have a higher frequency of claims, which raises costs to the member. Also, unlike an insurance provider, there is no profit margin with pension-provided benefits.

Second, this method would also ensure a standard eligibility criteria and level of coverage for all plan members. Whether members weren't choosing coverage previously, or couldn't, this approach would ensure an enhanced level of protection for all.

Finally, by providing the benefits within the retirement systems, members would have more assurance that their disability coverage would be available throughout their career. State pension law would have to be amended to change the benefits once they are granted.

Disadvantages To Pension-Provided Enhancements

Providing enhanced benefits through the pensions does have some potential disadvantages. In the current situation, employers have the choice to subsidize disability insurance protection for employees. However, the funding policy in the Plans 2/3 would require employers to contribute to this benefit. This is a potential cost increase for employers that currently don't subsidize employee disability coverage.

Also, while providing enhanced benefits may increase the overall replacement income of a disabled member, this coverage may still be insufficient for some members. If they do not have access to additional insurance products, or choose not to purchase additional insurance coverage, there still could be gaps in their level of protection.

Disability benefits provided by the pension systems may still leave gaps in some members' coverage.

Finally, by enhancing the benefits through the pension system, benefits for some are subsidized through contributions by all. As explained earlier in this paper, an enhanced disability beneficiary receives more benefit than they individually have earned or paid for. This invites a higher level of public interest in ensuring only truly eligible members are approved for the benefits, and that additional care is made to validate that they continue to be disabled as time progresses. This level of public protection from fraud can be administratively expensive to provide, and opens the system to public criticism if errors are made. This also requires extensive administrative support to ensure members who are denied benefits have due process.

Should Enhanced Benefits Be Provided Through Insurance Products?

Providing enhanced benefits through insurance products allows great flexibility in developing proposals. As stated earlier in the paper, not all Plans 2/3 members have access

to employer provided disability insurance. If policy makers wish to focus improvements on these members, one approach would be to explore having a state agency offer insurance that would be available to all plan members regardless of who employs them. This would ensure access to coverage without mandating participation. This approach is part of the stakeholder proposal.

With an insurance program, employers also have the flexibility to choose whether or not to subsidize some of the employee cost, and employees may be able to choose a variety of coverage options to match their need. This maintains the flexibility employers and members currently have.

Finally, policy makers could have the flexibility to design coverage that is mandatory for all plan members, like the pension-provided benefits, or offer other designs that are less prescriptive, such as an "opt-out" provision. This option would initially enroll members into a designated level of insurance coverage, but members would have the option to end or modify their coverage if they desire. Opt-out provisions typically result in higher rates of participation while still providing member choice.

Disadvantages To Insurance-Provided Enhancements

There are other considerations to providing enhanced coverage through insurance products. As discussed earlier, disability insurance benefits are generally purchased by individuals more likely to become disabled, which increases individual cost. Insurance companies are in business to make a profit, so cost to the members for similar benefits is typically higher.

Providing enhanced benefits through insurance products is typically more expensive for the member for a given coverage level.

The use of an insurance provider to administer benefits can be a challenging administrative requirement. While the administrator of the contract would not have to develop the infrastructure to satisfy the public interest in ensuring against fraud or providing due process, it does require extensive selection processes and contract oversight. This is particularly true for benefits as sensitive as disability benefits.

Finally, disability coverage through an insurance provider may not be as stable as through the pension system. Each

new contract can result in differences in cost and coverage levels, which may present challenges to protecting the long-term affordability of the benefits. The desire of policy makers to provide the benefit to members could also change over time. It may be easier to discontinue insurance benefits than to remove a pension benefit in statute.

Summary Of Pros And Cons

Table 5 below provides a summary of the pros and cons from various views for providing enhanced benefits through the retirement system or through expanded access to insurance products.

Table 5

Views on Disability Benefit Policies		
View	**Retirement System Provided**	**Insurance Provided**
Fiscal (State)	Costly to the plans, so state carries responsibility	Cost shifts to individuals and employer
Employee	Potential gaps in coverage; less member cost; availability of coverage more secure	More flexibility to vary the timing and amount of coverage; member costs typically higher; less assurance of continued coverage
Employer	Required payments due to plan funding policy	Employer choice to subsidize member cost
Retirement System	Expanded infrastructure to address public expectations for accountability	Expanded contract process and oversight responsibilities
Political	Open to requests from those desiring more coverage.	Broader access to insurance coverage may lead to less criticism of existing pension policy
Public	Greater interest in ensuring against fraud	Greater interest in contract oversight accountability

Other Questions If Expanding Pension-Provided Benefits

There are a number of additional questions that arise, each with policy implications, if the committee decides to provide enhanced disability pension benefits to members.

- Should benefits be enhanced for duty-related injuries or illnesses only, for non-duty related, or both?
- Should the additional benefits be off-set by other sources, such as Workers' Compensation or Social Security?
- Should benefits be enhanced earned or guaranteed benefits?
- Should the standard for disability be changed or remain as is, and should it differ between PERS, TRS, and SERS?

These questions were raised in 2005 and 2007, and if the decision is to expand the disability retirement provisions, these policy questions can be explored again in a future issue paper.

Disability Benefit Policies In Comparative State Systems

The one provision that is commonplace in the comparative systems is the absence of an early retirement reduction in calculating a duty or non-duty disability benefit.

Among the comparative systems there is similar variability in disability retirement benefit policies as in Washington's systems. Some systems use the enhanced earned benefit policy, while others use the guaranteed benefit policy. The one provision that tends to be commonplace is the absence of any reduction for early retirement in calculating either a duty or non-duty disability benefit. Each of the comparative states provides enhanced benefits within their retirement plan.

Most of the comparative systems use the enhanced earned benefit approach to disability benefits. Iowa and Minnesota provide an enhanced earned benefit without a reduction for early retirement. Florida, Seattle, and Ohio PERS provide the same, but also set minimum benefit percentages (Ohio PERS also has a maximum percentage). Idaho, Oregon, Colorado, and Wisconsin provide disability benefits based on combining what the member has earned plus what the member would have earned up to an assumed "normal" retirement age.

A few other systems use the guaranteed approach to disability benefits. CalSTRS, Ohio TRS, and Missouri all guarantee specific percentages of a member's salary at the time of disability.

Summary Of Analysis

The original design in the Plans 2/3 placed more responsibility on the member to ensure their own adequate disability coverage. For some benefits, like retirement and medical, the state assumes more responsibility to ensure the member has adequate coverage. If the choice is to assume more responsibility for the member, then there are pros and cons to enhancing pension-provided benefits or expanding the use of insurance policies.

Pension benefits generally cost less to the member for a given level of coverage than insurance, but may still leave gaps in coverage. Insurance benefits offer more flexibility to fit your coverage to your personal situation, but there is less assurance of stable coverage over the long-term. Expanding the pension-provided benefits raises additional policy questions that can be fully developed if the committee wishes to proceed in that direction.

The Plans 2/3 are the only Washington-administered plans that do not provide enhanced value to the disability benefits provided. An analysis of comparative states shows each system provides some form of enhanced disability benefit within their retirement plan, and none of the systems require any reduction for early retirement.

Possible Options

Option 1: Maintain Current Policy.

The first possible option for the committee is to maintain the current policy in the Plans 2/3 and assume no additional responsibility for the disability benefits of the members. The committee could encourage system employers to:

- Provide disability coverage, if they don't already.
- Increase the member education of the benefits of disability protection.

This would add no additional costs to the system and maintain the original plan design.

Option 2: Expand Insurance Coverage.

The second possible option is to look into expanding insurance coverage to all members of the Plans 2/3, since some employers do not provide disability insurance access as a benefit to their employees. These insurance benefits would be available to members regardless of their employer.

This would require study by an organization knowledgeable in the insurance industry to ensure adequate options are explored. Some of these options could include mandatory membership, or opt-out provisions for employees. Additionally, this could potentially expand the administrative cost and role of a state agency. DRS currently doesn't administer insurance benefits, and the HCA doesn't provide benefits to all public employees in the state.

Option 3: Enhance the Benefits Provided by the Plans 2/3.

A third option is to enhance the disability benefits provided within the Plans 2/3. This would add cost to the system, involve several additional policy decisions, and have administrative impacts.

Option 4: Combination of Previous Options.

A fourth option could be to combine elements of the insurance and pension-provided enhancement approaches. The stakeholder proposal does this. Their proposal is a combination of Option 2 and Option 3. The proposal calls for a study of disability insurance options that could be provided to all Plans 2/3 members regardless of their employer, and for the Plans 2/3 to provide an enhanced earned disability benefit from the pension system.

Revised Proposal

At their October meeting, the Executive Committee instructed staff to draft bill language to implement the stakeholder proposal, and bring the bill draft to the Executive Committee in November. The stakeholder proposal called for enhanced pension benefits based upon years of service combined with studying options for broader access to disability insurance for all members.

At their November meeting, the Executive Committee voiced concern with two aspects of the stakeholder proposal:

- The cost.
- Whether the current disability standard in the Plans 2/3 was narrow enough to prevent future employment while receiving the enhanced benefits.

The Executive Committee directed staff to draft a new bill for a work session, public testimony, and possible executive action in December. The new proposal would provide the same benefits and insurance study, but the new benefits would be paid only if the members meet the standard of disability used by the Social Security Administration (SSA), which is a total disability standard. ***See Appendix A for information and analysis of the newly proposed disability standard.*** The Chair also requested staff to prepare a bill draft for the December meeting providing for a study of insurance options only.

Options Considered At December Meeting

1. Implement the original stakeholder proposal.
2. Implement the revised proposal from the Executive Committee which uses the SSA standard for disability.
3. Implement only a study of insurance options by the WSIPP.
4. The Committee may also choose to take no further action on this issue.

Committee Activity

Staff briefed the Committee on this issue in October and December. The Committee held a public hearing and took executive action in December. The Committee recommended to the Legislature a revised version of Option #3 from the December meeting (with the study expanded to include pension benefits).

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

Direct the Washington State Institute for Public Policy, with the assistance of the Office of The State Actuary, to study options for addressing the needs of PERS Plan 2/3, TRS Plan 2/3, and SERS Plan 2/3 members for adequate disability benefit coverage. Recommended December 16, 2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0397.1/09).

Draft Fiscal Note

Attached.

Stakeholder Input

Correspondence attached from:

Public Employees for Pension Reform (PEPR), 9/4/2008 .

Correspondence on file from:

John McGuire, 5/9/2008.

John Kvamme, WASA & AWSP consultant, 5/15/2008.

Matt Zuvich, Chair, PEPR, 9/10/2008.

Appendix A

Changing The Disability Standard In The Plans 2/3

At their November meeting, the Executive Committee voiced concern with two aspects of the stakeholder proposal:

- The cost.
- Whether the current disability standard in the Plans 2/3 was narrow enough to prevent future employment while receiving the enhanced benefits.

The Executive Committee directed staff to draft a new bill. The new proposal would provide the same benefits and insurance study, but the new benefits would be paid only if the members meet the standard of disability used by the Social Security Administration, which is a total disability standard.

This appendix will provide information about the current disability standard in the Plans 2/3 and the proposed new standard. It will also attempt to answer the following questions:

1. Will changing the standard address the concerns with the original stakeholder proposal?
2. Does changing the standard impact other aspects of the disability program?

Current Disability Standard In The Plans 2/3

The current "occupational" disability standard in the Plans 2/3 provides benefits to members when they can no longer perform work for a public employer.

Currently, members are eligible to receive their benefit due to disability when they are "totally incapacitated for continued employment by an employer." Administrative code further defines this as "totally incapacitated to perform your job or any other position for an employer for which you are qualified by training or experience." This type of standard is generally referred to as an "occupational" disability standard.

The occupational standard provides benefits to members when they can no longer perform work for a public

employer due to a permanent injury or illness. This benefit is not for disabilities that are likely to improve over time.

Proposed New Standard - The Social Security Standard*

The current proposal to change the eligibility standard in the Plans 2/3 would mirror the standard used by the Social Security Administration for their disability benefit determinations. The general standard for Social Security is based upon an inability to work. Essentially, applicants are approved for a benefit if:

- They cannot do the work they did before.
- SSA decides they cannot adjust to other work because of their medical conditions.
- Their disability has lasted or is expected to last for at least one year or to result in death.

The Social Security Standard is a "total" disability standard, and to qualify members must be unable to perform any substantially gainful employment for any employer, public or private.

This standard is generally considered a "total" disability standard. However, the SSA standard is not necessarily a permanent standard. While most disabilities that are total are also likely to be permanent, some may be total and long-lasting, but not necessarily permanent. Recovery from multiple surgeries related to a serious accident may be an example. Individuals in this situation may have a total disability for a year or more, but they could be reasonably expected to recover and return to work at a later date.

Total disability generally implies the member is no longer able to work in any "substantially gainful" way for any employer, public or private. This determination requires an assessment of whether employees are currently able, or could become able for other employment, based upon their experience, age and education. SSA defines substantially gainful employment as earning at least $980 per month in 2009. This earnings limit is adjusted annually.

* Social Security Administration Website, www.ssa.gov/pgm/links_disability.htm

Analysis

Changing the standard for disability was proposed in response to two voiced concerns with the stakeholder proposal:

- The cost.
- Whether the current disability standard in the Plans 2/3 was narrow enough to prevent future employment while receiving the enhanced benefits.

Attempting to address the concerns by changing the disability standards in the Plans 2/3 raises the following questions:

1. Will changing the standard address the concerns with the original stakeholder proposal?
2. Does changing the standard impact other aspects of the disability program?

Does The Proposed Disability Standard Address The Concerns With The Stakeholder's Proposal?

Cost

The first concern with the original stakeholder proposal was cost. Will changing the standard lower the cost of the proposal? Actuarial pricing for the Executive Committee's revised proposal may be available at the December meeting, but was not available at the time of writing.

Ability To Work While Still Receiving A Disability Benefit

Another concern with the original stakeholder proposal was that the current disability standard in the Plans 2/3 was not strict enough to prevent a recipient from becoming employed elsewhere while still receiving a disability allowance. Is this a likely possibility in the Plans 2/3?

For general government and educational employees there is likely little difference in who qualifies for disability under either an occupational or total disability standard.

The current occupational standard provides benefits to members with permanent disabilities that prevent them from performing *any* work for a public employer for which they are qualified by education/training or experience. It would be rare for public employees and school employees to qualify under this standard and still be able to work elsewhere. Most public and school employers offer some positions that require very little specialized skill or training, such as many entry-level positions. If members' disabilities would allow them to work elsewhere, they would also likely be able to work one of these positions, which would disqualify them under the occupational standard.

There may be more possibility for a teacher with a qualifying disability to work elsewhere. A teacher who meets the occupational standard must be unable to teach. For example, it is possible some medical conditions may prevent teachers from teaching in front of dozens of students, such as anxiety disorders triggered by public speaking, but wouldn't prevent them from other employment without a public speaking requirement.

Does Changing The Standard Impact Other Aspects Of The Disability Program?

Designing a disability program is a combination of complex policy decisions, many of which are often interdependent. Changing certain aspects of that program without fully studying the possible impacts may create additional issues to consider. The following sections address some of the possible impacts of changing the disability standard in this proposal.

Does The Proposed New Standard Match The Design For Providing The Increased Benefit?

The original stakeholder proposal maintained all structures in the current disability program design, but provides more benefit to those who qualify within that design. Implementing a presumably narrower standard for providing increased disability benefits changes one of the structures in the design.

The current benefit structure provides a higher monthly benefit to those members with a disability who are closest to the normal age of retirement. The structure is based partially on age. The design of providing increased benefits to members in the stakeholder proposal mirrors that structure. Younger or middle aged employees who qualify for the benefits will still have a large reduction in their monthly allowance, but they will likely receive that allowance longer than an older employee. Older employees may see a higher monthly amount, but they will likely receive it for less time.

If members receive more benefit when they have a more severe disability, should age be a factor in how much additional benefit they receive?

Linking a narrower standard to increased benefits implies that those most severely disabled, those most in need, should receive additional benefit. The criterion for providing benefits has now changed. Now, the new value introduced into the design of the program is that severity

or need of the members impacts who receives more benefit. If severity or need determines eligibility to receive additional benefit, should age be a factor in determining the amount of the benefit provided? Does the younger employee with a total disability need less than an older employee, given the same years of service? The current structure may no longer be appropriate if there is a new value introduced into the design of how members qualify for benefits.

Coordination With Other Benefits Received

Should the enhanced benefits be off-set with other benefits the member may receive, such as Workers Compensation benefits?

Making the disability standard more restrictive may increase the likelihood that members qualifying for disability may also qualify for other benefits, such as workers compensation benefits for line of duty injuries or illnesses, or social security benefits. When providing enhanced disability benefits in these situations, there may be increased expectation from the public or others that benefits be coordinated to ensure members aren't receiving significantly more income while disabled than while working.

Administrative Impacts

Applying the SSA standard to increased benefits for Plans 2/3 members adds additional complexity to a labor intensive process. Changing the standard creates two tiers of disability benefits; an occupational benefit where the member receives the earned retirement allowance, and a total disability benefit with an enhanced earned retirement allowance. This second tier involves assessing the ability to work within the comprehensive employment market, a specialized area of expertise not currently required of the DRS.

Changing the disability standard creates two tiers of disability benefits, and may increase the complexity and infrastructure needs of the Department.

Additionally, because the SSA standard only requires the disability to last for one year, this may require more frequent follow-up with recipients than is currently required. As discussed earlier, some members may qualify for disability under the SSA standard even if there is a reasonable expectation of recovery from the disabling condition after a year or more. Under the current occupational standard, the disability must be permanent in order to qualify, so the likelihood of members recovering from their disability is less.

Other Systems

With one exception, the other systems and plans within Washington State use an occupational standard for disability.

With the other systems in Washington State, the standard for disability is an occupational standard, with one exception. Generally, the other systems provide a disability benefit if the member no longer can perform duties for an employer in their system. The lone exception is the benefit provided to LEOFF Plan 2 members who are totally disabled in the line of duty. The standard for qualifying for this benefit is the SSA standard. If members qualify, they are provided 70 percent of their final average salary, which is off-set by Workers' Compensation and Social Security benefits such that they can receive a total amount from all sources no greater than 100 percent of final average salary.

Other States

Eight of twelve of our comparative systems use an occupational disability standard for general government or educational employees. The remaining four use a total disability standard.

When evaluating the disability benefits provided to general government or educational employees in twelve of the systems within our comparative states, four states use a total disability standard similar or exactly the same as the SSA standard. Of these four systems, Iowa, Minnesota, Wisconsin, and Idaho, three off-set the benefits provided with workers' compensation benefits if the members were receiving both.

The remaining eight systems provided benefits based upon an occupational disability standard. Of these eight, only Oregon and Missouri off-set the benefits with workers compensation benefits.

None of the twelve systems had different medical standards for disability based upon duty or non-duty distinctions. Four had years of service requirements for non-duty eligibility and none had a service requirement for duty disability. Only one state provided different benefit amounts based upon duty or non-duty distinctions. Florida provides an unreduced earned benefit for both duty and non-duty disabilities, but the minimum benefit provided is 25 percent for non-duty and 42 percent for duty disabilities.

Conclusion

Designing a disability program is a combination of complex policy decisions, many of which are often interdependent. Changing certain aspects of that program without fully studying the possible impacts may create additional issues to consider.

The proposal to narrow the disability standard to that used by the SSA for increased disability benefits in the Plans 2/3 attempted to accomplish two goals; lowering the cost of the proposal and restricting the eligibility for additional benefits to only those that cannot work anymore. Pricing of the new proposal will likely address whether the first goal is met. Analysis of how the occupational standard is applied to general government and educational employees shows there is likely little difference between either standard in who qualifies for disability.

Additionally, other issues are raised when changing the standard. If members receive more benefit when they are more severely disabled, is age an appropriate criteria in determining how much they receive? Since the narrower disability standard may increase the likelihood of members receiving other benefits, should the increased benefits be off-set? Will there be additional pressure from the public to ensure members don't receive duplicative coverage? Finally, do policy makers want to consider the additional administrative complexity and infrastructure for DRS that changing the standard could create?

Research shows that the standards for disability benefits in the other systems and plans within Washington State are occupational standards, with one exception. The systems within our comparative states tend to use occupational standards, but some do use total disability standards.

Possible Options

Option 1: Use SSA standard and proposed method for increasing benefits.

The first option is to maintain the current revised proposal. This would increase disability benefits only for members who qualify under the Social Security standard for

disability. This option would also retain the insurance study requirement of the WSIPP.

Option 2: Use SSA standard but modify method for increasing benefits.

This option would allow policy makers to match the method for increasing benefits with the presumably narrower standard for qualifying. One approach could be to provide increased benefits, but remove age as a determining factor in how the benefits are calculated. Possible methods of achieving this would be to remove the percentage reduction from the normal retirement age, or to provide a flat percentage of salary regardless of age. Provisions to off-set benefits could also be included. This option would also retain the insurance study requirement of the Washington State Institute for Public Policy.

Option 3: Maintain the current standard of disability and proposed method for increasing benefits.

This is the option originally proposed by the stakeholders. It would maintain the current occupational disability standards used in the Plans 2/3. This option would also retain the insurance study requirement of the. WSIPP

Option 4: Move forward with an insurance study only.

The committee could move forward only with requiring the WSIPP to study insurance options for Plans 2/3 members.

Option 5: Continue to study the issue in the next interim.

This option would allow the committee to continue studying the complex issues with increasing disability benefits in the upcoming interim.

Option 6: Take no action.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0397.1/09

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Studying disability benefit options for members of the public employees' retirement system plan 2 and plan 3, the teachers' retirement system plan 2 and plan 3, and the school employees' retirement system plan 2 and plan 3.

AN ACT Relating to a study of disability benefit options for members of the public employees' retirement system plan 2 and plan 3, the teachers' retirement system plan 2 and plan 3, and the school employees' retirement system plan 2 and plan 3; and creating a new section.

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

NEW SECTION. **Sec. 1.** During the 2009 legislative interim, the Washington state institute for public policy, with the assistance and support of the office of the state actuary, shall study the options available to the legislature for addressing the needs of members of the public employees' retirement system plan 2 and plan 3, the teachers' retirement system plan 2 and plan 3, and the school employees' retirement system plan 2 and plan 3, to have adequate disability benefit coverage through disability benefits under the public pension systems, through access to long-term disability insurance coverage, or a combination of both. Options could include but are not limited to recommended statutory changes to the public pension systems, an insurance product available to all members administered by a state agency, expansion of eligibility for the current long-term disability

benefits offered by the public employees' benefits board, or other options as developed by the institute. The institute shall report the findings and recommendations of its study to the select committee on pension policy no later than November 1, 2009.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/2008**	**Z-0397.1 / Z-0398.1**

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, throughout the 2008 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 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

There is no fiscal impact resulting from this proposal.

This bill directs the Washington State Institute for Public Policy, with the assistance of the Office of The State Actuary, to study options for addressing the needs of Plans 2/3 members for adequate disability benefit coverage.

WHAT IS THE PROPOSED CHANGE?

Summary Of Change

This proposal impacts the following systems:

- Public Employees' Retirement System (PERS) Plans 2/3
- Teachers' Retirement System (TRS) Plans 2/3
- School Employees' Retirement System (SERS) Plans 2/3

The proposal calls for a study by the Washington State Institute for Public Policy, with the assistance of the Office of The State Actuary, to study options for addressing the needs of PERS Plans 2/3, TRS Plans 2/3, and SERS Plans 2/3 members for adequate disability benefit coverage.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

Members of the Plans 2/3 gain access to their earned retirement benefit upon qualification for disability. This benefit is actuarially reduced from the normal age of retirement to account for earlier access. Qualification for a disability retirement is based upon a member's inability to perform his / her current job or any other job by an employer for which he / she is qualified based upon skills, experience, or training, due to a permanent disabling condition. There is no service qualifier, no distinction between duty and non-duty disablement, and no off-sets with other benefit sources. Additionally, members may have the option to purchase long-term disability insurance through their employer if coverage is part of the benefits package offered to employees.

Who Is Impacted And How?

This proposal does not directly impact any members of the affected systems, as it only provides for a study of benefits.

WHY THIS PROPOSAL DOES NOT HAVE A COST

This proposal does not have a cost because it does not change benefit provisions.

DRAFT

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
2. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

DRAFT

Public Employees for Pension Reform

A coalition of Washington State Public Employee Unions and Retiree Associations serving active and retired state and public employees

Disability Benefits

September 4, 2008

Proposal: **Provide an Earned Disability Benefit to those w/ more than 10 yrs of service, based on 30 yr. ERRF's[1].**

- No change in current rules governing disability eligibility (duty and non-duty)
- Permanently Disabled Individuals with 20 or more years of service could retire using an ERFF that is a reduction of 3% for each year of age less than 62.
- Permanently Disabled Individuals with 10 or more years of service, but less than 20 could retire using a reduction equal to 3% for each year of age under age 65. This would be consistent with the Alternate Early Retirement reduction factors provided in C 247 L 2000. [RCW 41.32.765 (3)(a); 41.35.420 (3)(a); 41.40.630 (3)(a)]

Supplemental Option: **Opt-In Disability Retirement Insurance provided through either DRS or HCA.**

- Insure against the loss of pension benefits for both Duty and non-Duty related catastrophic events to be offered through the Department of Retirement Systems for participation by all system employers.
- The Select Committee on Pension Policy would ask the Washington State Institute for Public Policy (WSIPP) or other appropriate body (Insurance Commissioners office?) to study and develop proposals:
  - For individuals who do not qualify (due to less than 10 years of service) for the above Disability Retirement provisions.
  - For replacement income for individuals that do qualify for the Disability Retirement proposal (above) but need additional income to compensate for the reduced retirement benefit.
- The WSIPP or other appropriate body would report back any results to the SCPP for formulation of any legislative proposals.

[1] ERRF is an Early Retirement Reduction Factor

DRS Technical Corrections

Description Of Issue

The Department of Retirement Systems (DRS) has identified certain technical corrections to pension statutes. The proposed corrections would repeal two obsolete sections of Plan 1 of the Teachers' Retirement System:

- The disability reserve fund in RCW 41.32.360.
- The death benefit fund in RCW 41.32.366.

These funds are no longer used by DRS—the Department has paid death and disability benefits from the pension reserve fund since 1992. The proposed changes have no policy or fiscal impact.

Policy Highlights

Typically, the SCPP sponsors technical corrections bills in long sessions. There were no policy decisions to make with respect to the proposed corrections.

Committee Activity

Staff briefed the Committee on this issue in November. The Committee held a public hearing in November and took executive action to recommend the proposed technical corrections to the Legislature.

Recommendation To 2009 Legislature

Repeal obsolete sections of Plan 1 of the Teachers' Retirement System.

Staff Contact

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0232.4/09 4th draft

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Repealing certain obsolete state retirement system statutes.

AN ACT Relating to repealing certain obsolete state retirement system statutes; and repealing RCW 41.32.360 and 41.32.366.

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

NEW SECTION. **Sec. 1.** The following acts or parts of acts are each repealed:

(1) RCW 41.32.360 (Basis of contributions to disability reserve fund) and 1991 c 35 s 47, 1963 ex.s. c 14 s 8, 1955 c 274 s 17, & 1947 c 80 s 36; and

(2) RCW 41.32.366 (Basis of contributions to death benefit fund) and 1991 c 35 s 48 & 1963 ex.s. c 14 s 10.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/08**	**Z-0232.4 / Z-0407.2**

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 (SCPP) throughout the 2008 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 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.

RESULTS

There is no fiscal impact resulting from this proposal.

This proposal would repeal two obsolete sections of statute concerning Plan 1 of the Teachers' Retirement System: RCW 41.32.360 (Basis of contributions to disability reserve fund) and RCW 41.32.366 (Basis of contributions to death benefit fund). The auxiliary funds referenced in these statutes are no longer used. Since 1992, the Department of Retirement Systems has paid death and disability benefits from the pension reserve fund.

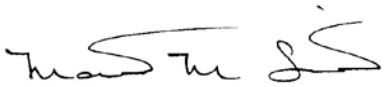
DRAFT

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. This draft fiscal note has been prepared for the SCPP.
2. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

DRAFT

Fish And Wildlife Service Credit Transfer

Description Of Issue

Fish and Wildlife enforcement officers were placed into Plan 2 of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Retirement System beginning July 23, 2003. When this occurred, existing employees were not allowed to transfer their prior Public Employees' Retirement System (PERS) service as enforcement officers into LEOFF Plan 2.

The question for policy makers is: Should these enforcement officers be allowed to transfer their prior PERS service into LEOFF Plan 2?

Policy Highlights

- Fish & Wildlife enforcement officers did not always have general law enforcement authority while in PERS.
- Impacted enforcement officers are currently dual members, with service in both PERS and LEOFF Plan 2.
- Prior examples of groups gaining LEOFF Plan 2 membership allowed the transfer of prior PERS service.
- Prior proposed legislation on this issue did not include enforcement officers with prior service in PERS Plan 3.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 session. The 2008 SCPP bill (HB 3023/SB 6653) allowed the transfer of prior enforcement officer service and required payments by members and the Department of Fish and Wildlife sufficient to keep from increasing the LEOFF Plan 2 contribution rates. The bill did not pass the Legislature, but did pass the Senate.

Staff briefed the Committee on this issue in September, and the Committee held a public hearing on this issue in October. The Committee held a second public hearing in December and took executive action to recommend this proposal to the Legislature.

Recommendation To 2009 Legislature

Allow enforcement officers for the Department of Fish & Wildlife to convert prior PERS Plan 2 or PERS Plan 3 service to LEOFF Plan 2.

Staff Contact

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Fish and Wildlife Service Credit Transfer

In Brief

ISSUE

Should the SCPP once again jointly recommend to the Legislature a proposal to allow Fish and Wildlife enforcement officers to transfer prior PERS Plan 2 service into LEOFF Plan 2?

The LEOFF Plan 2 Board has requested the Committee jointly recommend this proposal. Additionally, the Board has requested the Committee study allowing officers with prior service in PERS Plan 3 to also transfer their service into LEOFF Plan 2.

MEMBER IMPACT

This proposal would impact an estimated 81 active members of LEOFF Plan 2 serving as Fish and Wildlife enforcement officers with prior PERS Plan 2 or Plan 3 service. 72 officers have prior Plan 2 service, and nine have prior Plan 3 service.

Dave Nelsen
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Current Situation

Fish and Wildlife enforcement officers who were members of the Public Employees' Retirement System (PERS) Plan 2 or PERS Plan 3 on or before January 1, 2003, and were employed on July 23, 2003, are required by legislation passed in 2003 to be members of the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2. Service as an enforcement officer prior to that date remains in PERS. Enforcement officers that were members of PERS Plan 1 remained in Plan 1.

History

Prior to the passage of HB 1205 in the 2003 Legislative Session, all enforcement officers hired by the Department of Fish and Wildlife were placed into the PERS retirement system. The employees had long sought membership in the LEOFF system, but the responsibilities and authority of these officers were somewhat different than LEOFF-eligible police officers. Generally, the eligibility of a group of employees for membership in LEOFF Plan 2 as law enforcement officers is determined by three things:

- They must be full-time, fully authorized law enforcement officers commissioned and employed to enforce the criminal laws in general.
- Their employer must be a general authority law enforcement agency that has as its primary function the enforcement of the traffic and criminal laws of the state in general.
- They must meet certain qualifications, including the Criminal Justice Training Commission basic law enforcement course.

As summarized by Office of the State Actuary staff in an October 18, 2000, letter to the Joint Committee on Pension Policy, enforcement officers were considered limited authority peace officers prior to 2002, with their primary

responsibility to enforce the laws and regulations related to Fish and Wildlife. However, staff research at the time showed their duties often placed them in cooperative working situations with local law enforcement agencies, assisting with actions clearly outside the enforcement of Fish and Wildlife regulations. These situations were fairly common, particularly in the rural areas of the state.

Legislation in 2002 explicitly authorized Fish and Wildlife enforcement officers to be general authority enforcement officers, and designated the Department of Fish and Wildlife as a general authority enforcement agency. This legislation also kept the enforcement officers from qualifying for LEOFF by excluding the employer from the employer definition section in the LEOFF statute.

The legislation in 2003 established the future eligibility in LEOFF Plan 2 for existing employees and all new hires into these positions, but specifically did not allow the transfer of prior PERS service credit earned as enforcement officers into the LEOFF Plan 2 system. These existing members would be dual members in the PERS and LEOFF systems. Public testimony from both labor and employer representatives at the time agreed that they were asking only for prospective LEOFF eligibility, without a transfer of prior service.

The legislative request in 2003 to allow enforcement officers membership in LEOFF Plan 2 did not include the ability to transfer prior PERS service into LEOFF Plan 2.

Since that time, the LEOFF Plan 2 Board endorsed legislation for the 2006 and 2007 Legislative Sessions that would have allowed for the transfer of prior PERS Plan 2 service into LEOFF Plan 2. Neither effort was passed by the Legislature. The Committee jointly recommended with the LEOFF Plan 2 Board a proposal to the Legislature in 2008 that also allowed the transfer of prior PERS Plan 2 service. This bill passed in the Senate, but did not pass the House.

For the 2009 Legislative Session, the LEOFF Plan 2 Board has again requested the Committee jointly recommend a transfer proposal. They have also recommended the Committee study allowing officers with prior service in PERS Plan 3 to also transfer their PERS service into LEOFF Plan 2.

Examples

The following examples highlight the difference in the total retirement benefit amount between an enforcement officer that retires at the normal age in LEOFF Plan 2 as a

dual member or retires with all prior service transferred into LEOFF Plan 2. Dual members are members who retain service in the retirement system they were members of previously. When they retire, they receive a benefit from each system, calculated under each system's rules.

A Fish and Wildlife enforcement officer had ten years of prior PERS Plan 2 time as an enforcement officer, worked 15 years in LEOFF Plan 2, and now is retiring at age 53, with a Final Average Salary of $50,000 per year.

Members who transfer their prior service to LEOFF Plan 2 will likely receive higher retirement benefits.

Example 1: Retiring As A Dual Member

15 yrs X 2% X $50,000 = LEOFF Plan 2 annual benefit of $15,000

10 yrs X 2% X $50,000 X .31 (reduction factor for 12 year early retirement) = PERS Plan 2 annual benefit of $3,100

Total annual benefit of ***$18,100.***

Example 2: Retiring With All Service In LEOFF

25 yrs X 2% X $50,000 = *Total annual benefit of* ***$25,000***

Policy Analysis

The policy question is whether the current LEOFF Plan 2 Fish and Wildlife enforcement officers should be allowed to transfer prior PERS service as enforcement officers into the LEOFF Plan 2 system.

Dual membership provisions help members retain the value of the retirement benefit they will receive for the time worked in their previous retirement system.

Currently, the policy of dual membership is in place to provide a cost effective way to help retain the value of service credit earned in a prior system under the prior system's rules. Are there compelling reasons why the dual membership status is insufficient in this situation?

Additionally, when service from one system is transferred to a system with a higher level of benefits, a financial liability is created. How that liability is paid for becomes part of the policy deliberations about the transfer. Should the affected members and employers be the only parties that pay for the transfer, and if so, in what proportion for each? Alternatively, should the costs be socialized throughout the

plan so everyone in the plan pays through increased contribution rates, if necessary?

There are two key questions:

1. *Do you keep the policy of dual membership in place and not allow the transfer of prior service?*
2. *If the transfer is allowed, then who pays for the increased cost of moving the PERS service to LEOFF Plan 2?*

To address these questions, we can first look at what has been the historical practice in LEOFF Plan 2 when eligibility has been expanded to include former PERS duties. There have been four prior instances where other PERS members were allowed to become members of LEOFF. In each case, prior PERS service was allowed to be transferred, although the funding models to pay for the increased liabilities varied.

The following chart displays information about these four prior situations, including the year the expansion took place, what members were included in the eligibility change, what payment was required of the affected member to transfer prior service, what corresponding payment was required of the affected member's employer if the member paid their share, and finally, was their additional liability socialized over all members and employers of the plan?

YEAR	Members Affected	Cost to Affected Member	Cost to Affected Employer	Additional liability socialized by plan? (Y/N)
1993 SHB 1744	Port and university police officers	Difference in member contribution rates, plus interest	Difference in PERS employer rate and the LEOFF employer and state contribution rates, plus interest amount sufficient to prevent increased rates	N
1996 SHB 2191	Higher Ed fire fighters	Difference in member contribution rates, plus interest	Difference in PERS employer rate and the LEOFF employer and state contribution rates, plus interest, and an additional amount sufficient to ensure the LEOFF rates would not increase due to the transfer	N
2003 SHB 1202	Prior PERS EMTs whose jobs were relocated to a fire district and they became fire fighters	Difference in member contribution rates, plus interest	None	Y
2005 HB 1936	Current PERS EMTS working for a LEOFF employer	Difference in member contribution rates, plus interest	An amount sufficient to ensure the LEOFF contribution rates will not increase due to the transfer	N

Previous expansions of LEOFF Plan 2 eligibility allowed prior service transfers.

In each of the four above cases, the member's prior time in PERS was allowed to transfer into LEOFF. The only consistency in the funding, however, was the amount required to be paid by the member. The nature of the prior service in the four instances also varied. For example, EMT service alone had long been considered PERS service, until 2005 legislation amended the definition of LEOFF-eligible duty to include EMT time. As discussed earlier, for the Fish and Wildlife enforcement officers, the duties and authority granted them over time grew into more LEOFF-like service, but may not have always been as similar as they were in 2003.

Other Systems

There are also examples within the other retirement systems administered by the State of individuals performing the same job who are moved to a different retirement system.

- In 2000, existing PERS Plan 2 members of school and educational service districts had all their prior service transferred to the School Employees' Retirement System (SERS) Plan 2.
- In 2002, PERS Commercial Vehicle Enforcement Officers (CVEO) became eligible for the WSPRS, and prior service as a CVEO was allowed to be transferred.
- In 2006, PERS Plan 2 and 3 members could transfer to the Public Safety Employees' Retirement System (PSERS), but their prior PERS service remained in PERS.

Other Washington State systems addressed prior service transfers based upon the unique circumstances of the situation.

There doesn't appear to be a consistent application of a prior service transfer policy to each of the above situations. All but PSERS allowed prior service to transfer, and the SERS example mandated the transfer. The SERS example is the only situation where the benefits in the two systems affected were equivalent and where the affected individuals were not moving to a system with a higher benefit level. What the disparity shows, is that each situation was treated uniquely, and may have had other compelling reasons to justify the decisions made regarding the transfer of prior service.

Other States*

Other peer state's systems have expanded eligibility. However, as in Washington, it appears the decision whether to allow the transfer of prior service was made based on the circumstances of each expansion.

A look at similar situations in our comparative states provides a general mix of how this situation has been handled over time, even within the same state. The state of California, for example, is indicative of other states' practice, and has seen significant expansion of their public safety plan. In all cases save one, where the public safety eligibility requirements were expanded to include members previously reported in their general plan, the prior service was also moved into the public safety plan. The only exception to allowing prior service was the latest transfer, in 2005, where some 4,000 employees in various job classes were allowed into the system, but only on a prospective basis. According to staff of the system, the main reason for disallowing the transfer in this case was the cost.

** Research into practices by other states was performed in October of 2007.*

Possible Options

The Committee has two primary options:

Option 1: Maintain the current policy of dual membership for the prior service in PERS.

Option 2: Recommend allowing some form of prior service transfer.

The **first option** allows the enforcement officers to maintain value of their prior service according to the original plan rules through dual membership, and is in keeping with the original requests of the labor and employer representatives who backed the legislation in 2003. While this doesn't appear to be consistent with the past practice in LEOFF Plan 2, the examples from the other systems show in those cases that prior service transfers were addressed based upon their own unique circumstances.

One argument against dual membership in these situations was in the House bill analysis for HB 1202. The argument made was that though the dual membership provisions exist, given the wide difference in the normal retirement ages for PERS Plan 2 and LEOFF Plan 2 (age 65 and age 53), only a greatly reduced PERS 2 benefit would be available to the member at the LEOFF 2 normal retirement

age. This reduction was demonstrated in our earlier example.

The **second option** is consistent with past practice in LEOFF Plan 2, and represents the current wishes of the affected stakeholders. While it doesn't match with the use of dual membership, it recognizes the impact of disparate normal ages of retirement.

Funding The Transfer

If the Committee recommends the option to transfer prior PERS service, several questions arise regarding the funding of the transfer:

1. If a member payment is required, how much should it be and how long should the member have to elect and pay for the transfer of service?
2. If an employer payment is required, how much should it be and how long should the employer have to pay?
3. Should any amount of the liability be socialized over all members and employers in the plan?

With regard to the first question, past practice in LEOFF Plan 2 has required the member to pay the difference in the PERS 2 member contributions and the LEOFF 2 member contributions, plus interest, and provide a window to complete that payment, usually five years. There is no past practice for transferring prior PERS Plan 3 service. However, other payment options exist. For example, the proposal could require the employee to pay the full actuarial cost of the prior service in the LEOFF system. Given the value of the service, the cost could be high, but it would be a compromise between the current dual membership status and the employer paying for the benefit enhancement.

As to the employer payment, the past practice is generally to pay an amount sufficient to keep contribution rates from ever increasing due to the transfer. A payment of this nature makes the question of socialization moot. The one time in LEOFF Plan 2 the employer didn't make this type of payment was the 2003 EMT legislation. In that situation, the remaining liability was socialized throughout the plan.

However, the socialized cost would not have been sufficient to cause an immediate rate increase in the 2003-2005 Biennium.

New Consideration For This Interim

The LEOFF Plan 2 Board has again requested the Committee jointly recommend this transfer proposal. Additionally, the Board has requested the Committee study allowing officers with prior service in PERS Plan 3 to also transfer their service into LEOFF Plan 2.

For the 2009 Legislative Session, the LEOFF Plan 2 Board has again requested the Committee jointly recommend a transfer proposal. The Board also recommended the Committee study allowing officers with prior service in PERS Plan 3 to also transfer their PERS service into LEOFF Plan 2.

The proposal to the Legislature on this issue in 2006 and 2007 from the LEOFF Plan 2 Board, and the jointly recommended proposal of the Committee and the Board in 2008, allowed the transfer of prior PERS Plan 2 service to the LEOFF system. The details of the proposals are as follows:

- Members who elect to transfer their prior service pay the difference in the member contribution rates between PERS 2 and LEOFF 2, plus interest.
- Members would have five years to complete payment, but service credit would not be transferred prior to the end of the five-year waiting period.
- Upon completion of the five-year waiting period, the Department of Fish and Wildlife would have one year to pay a sum sufficient to ensure the LEOFF Plan 2 rates would not increase at any time due to this transfer.

Why Didn't The Proposals Include Members With Prior PERS Plan 3 Service?

Enforcement Officers with prior PERS Plan 3 service were excluded from earlier proposals due to possible IRS concerns. DRS clarified with tax counsel that these concerns do not likely apply to this situation.

At the time of the previous proposals on this issue, concern existed about the Internal Revenue Service (IRS) disallowing an additional transfer choice between a Plan 3 and a Plan 2. The Department of Retirement Systems (DRS) has since consulted with tax counsel and clarified the parameters around that IRS concern. This transfer of service from a Plan 3 to a Plan 2 *would not likely cause IRS concern* for the following reasons:

- The transfer that would occur is between two separate systems, PERS and LEOFF.

- The transfer would not affect future contribution rates within the same defined benefit plan.

Should Prior PERS Plan 3 Service Be Allowed To Transfer?

Given that this would not cause IRS concern, is there another reason to exclude these officers from transferring their prior service? Except for transferring to PERS Plan 3, there are no other distinguishing differences between these members and the PERS Plan 2 members. Both groups of members perform the same duties and have the same varying levels of experience as enforcement officers. There are currently nine enforcement officers mandated into LEOFF Plan 2 whose prior service is in PERS Plan 3. All nine of the Plan 3 members are younger than the normal age of retirement in Plan 3 and could potentially benefit from the prior service transfer. The additional members in the proposal could increase the cost to the Department of Fish and Wildlife to ensure the rates in LEOFF Plan 2 do not ever increase due to the transfer.

Conclusion

In determining whether to allow the transfer of prior service, the historical practice in LEOFF Plan 2 has been to allow the members moving to the new system the option to transfer their prior service. However, a prior service transfer was not part of the original request by the stakeholders in the 2003 legislation that moved the members into LEOFF Plan 2. Other systems administered by the state of Washington have addressed this issue in variety of ways, each situation based upon their own unique circumstances.

When the transfer has been allowed, the funding of the transfer has generally required:

- A member payment of the difference in contributions between the systems, plus interest.
- An employer payment sufficient to keep the LEOFF 2 rates from ever increasing due to the transfer.

Finally, the clarification of the possible IRS issues with transferring prior PERS Plan 3 service to LEOFF Plan 2 removes the primary reason for excluding these members

from past proposals. However, including them in the proposal could result in additional cost to the Department of Fish and Wildlife.

Committee Activity

Staff briefed the Committee on this issue in September, and the Committee held a public hearing on this issue in October. The Committee held a public hearing and took executive action in December to recommend this proposal to the Legislature.

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

Allow enforcement officers for the Department of Fish & Wildlife to convert prior PERS Plan 2 or PERS Plan 3 service to LEOFF Plan 2. Recommended December 16, 2008.

Stakeholder Input

Correspondence attached from:

Kelly Fox, Chair, LEOFF Plan 2 Board, 5/12/2008 and 6/30/2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0217.2/09).

Draft Fiscal Note

Attached.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0217.2/09 2nd draft

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Allowing department of fish and wildlife enforcement officers to transfer service credit.

AN ACT Relating to allowing department of fish and wildlife enforcement officers to transfer service credit; and adding a new section to chapter 41.26 RCW.

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

NEW SECTION. **Sec. 1.** A new section is added to chapter 41.26 RCW to read as follows:

(1) A member of plan 2 who was a member of the public employees' retirement system plan 2 or plan 3 while employed as an enforcement officer for the department of fish and wildlife has the option to make an election no later than December 31, 2009, filed in writing with the department of retirement systems, to transfer all service credit previously earned as an enforcement officer in the public employees' retirement system plan 2 or plan 3 to the law enforcement officers' and firefighters' retirement system plan 2. Service credit that a member elects to transfer from the public employees' retirement system to the law enforcement officers' and firefighters' retirement system under this section shall be transferred no earlier than June 30, 2014, and only after the member completes payment as provided in subsection (2) of this section.

(2)(a) A member who elects to transfer service credit under subsection (1) of this section shall make the payments required by this subsection prior to having service credit earned as an enforcement officer with the department of fish and wildlife under the public employees' retirement system plan 2 or plan 3 transferred to the law enforcement officers' and firefighters' retirement system plan 2.

(b) A member who elects to transfer service credit from the public employees' retirement system plan 2 under this subsection shall pay, for the applicable period of service, the difference between the contributions the employee paid to the public employees' retirement system plan 2 and the contributions that would have been paid by the employee had the employee been a member of the law enforcement officers' and firefighters' retirement system plan 2, plus interest on this difference as determined by the director. This payment must be made no later than June 30, 2014, and must be made prior to retirement.

(c) A member who elects to transfer service credit from the public employees' retirement system plan 3 under this subsection shall transfer to the law enforcement officers' and firefighters' retirement system plan 2, for the applicable period of service, the full balance of the member's defined contribution account within plan 3 as of the effective date of the transfer. At no time will the member pay, for the applicable period of service, a sum less than the contributions that would have been paid by the employee had the employee been a member of the law enforcement officers' and firefighters' retirement system plan 2, plus interest as determined by the director. This transfer and any additional payment, if necessary, must be made no later than June 30, 2014, and must be made prior to retirement.

(d) No later than June 30, 2015, the department of fish and wildlife shall pay an amount sufficient to ensure that the contribution level to the law enforcement officers' and firefighters' retirement system will not increase due to this transfer. Payments made prior to June 30, 2015, are authorized as determined by the department and coordinated with the state actuary.

(e) Upon completion of the payment required in (b) of this subsection, the department shall transfer from the public employees' retirement system to the law enforcement officers' and firefighters' retirement system plan 2: (i) All of the employee's applicable accumulated contributions plus interest and all of the applicable

employer contributions plus interest; and (ii) all applicable months of service, as defined in RCW 41.26.030(14)(b), credited to the employee under this chapter for service as an enforcement officer with the department of fish and wildlife as though that service was rendered as a member of the law enforcement officers' and firefighters' retirement system plan 2.

(f) Upon completion of the payment required in (c) of this subsection, the department shall transfer from the public employees' retirement system to the law enforcement officers' and firefighters' retirement system plan 2: (i) All of the employee's applicable accumulated contributions plus interest and all of the applicable employer contributions plus interest; and (ii) all applicable months of service, as defined in RCW 41.26.030(14)(b), credited to the employee under this chapter for service as an enforcement officer with the department of fish and wildlife as though that service was rendered as a member of the law enforcement officers' and firefighters' retirement system plan 2.

(g) If a member who elected to transfer pursuant to this section dies or retires for disability prior to June 30, 2014, the member's benefit is calculated as follows:

(i) All of the applicable service credit, accumulated contributions, and interest is transferred to the law enforcement officers' and firefighters' retirement system plan 2 and used in the calculation of a benefit.

(ii) If a member's obligation under (b) or (c) of this subsection has not been paid in full at the time of death or disability retirement, the member, or in the case of death the surviving spouse or eligible minor children, have the following options:

(A) Pay the bill in full;

(B) If a continuing monthly benefit is chosen, have the benefit actuarially reduced to reflect the amount of the unpaid obligation under (b) or (c) of this subsection; or

(C) Continue to make payment against the obligation under (b) or (c) of this subsection, provided that payment in full is made no later than June 30, 2014.

(h) Upon transfer of service credit, contributions, and interest under this subsection, the employee is permanently excluded from membership in the public employees' retirement system for all service

related to time served as an enforcement officer with the department of fish and wildlife under the public employees' retirement system plan 2 or plan 3.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/08/08**	**Z-0217.2**

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 and Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board throughout the 2008 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 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 would allow enforcement officers for the Department of Fish & Wildlife (DFW) to convert prior PERS Plan 2 or PERS Plan 3 service to LEOFF Plan 2.

Impact on Pension Liability

(Dollars in Millions)	**Current**	**Increase**	**Total**
Today's Value of All Future Pensions	$26,784	$4.2	$26,788
Earned Pensions Not Covered by Today's Assets	N/A	N/A	N/A

Impact on Contribution Rates: (Effective 09/01/2009)

2009-11 State Budget	**PERS**	**LEOFF**
Employee (Plan 2)	0.00%	0.00%
Employer:		
Current Annual Cost	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%
Total	0.00%	0.00%
State		0.00%

Budget Impacts

(Dollars in Millions)	**2009-2011**	**2011-2013**	**25-Year**
General Fund-State	$0.0	$0.0	($0.1)
Total Employer	$0.0	($0.1)	($0.4)

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 Plan 2 of the Law Enforcement Officers' and Fire Fighters' (LEOFF 2) Retirement System, as well as Plans 2 and 3 of the Public Employees' Retirement System (PERS). This proposal allows LEOFF 2 members to transfer into LEOFF 2 their prior PERS 2 or PERS 3 service credit for periods of employment as enforcement officers for DFW. The proposal specifies Department of Retirement Systems (DRS) may not transfer the service credit prior to June 30, 2014, except for members who become disabled or die during the waiting period. Members have until June 30, 2014, to make their payments. The proposal also specifies the DRS may only transfer service credit after members complete their payments.

Finally, the proposal provides that members who elect to transfer their service credit must transfer all their service as an enforcement officer with DFW under PERS 2 or PERS 3. Furthermore, upon transfer this proposal permanently excludes members from using service related to time served as an enforcement officer with the DFW in PERS 2 or PERS 3.

Effective Date: 90 days after session.

What Is The Current Situation?

Currently, LEOFF 2 members who were members of PERS 2 or PERS 3 while serving as enforcement officers for DFW cannot transfer their prior PERS service to LEOFF 2. They are dual members of PERS 2 or PERS 3 and LEOFF 2 and can retire under portability provisions (Chapter 41.54 RCW).

Who Is Impacted And How?

We estimate this proposal could affect 81 members out of the total 104 active DFW enforcement officers because they have eligible prior service credit in PERS. Furthermore, we expect 61 members will actually receive improved benefits. We expect the remaining members would not elect to transfer service credit because it would not be financially advantageous for them. This proposal would not affect inactive members in LEOFF 2.

We estimate that for a typical member impacted by this proposal, the increase in benefits would be the opportunity for a full retirement at age 53 instead of 65, or a benefit at age 50 with 20 years of service reduced 3 percent for each year under age 53.

This proposal requires Plan 3 members who elect to transfer their eligible service to transfer their entire defined contribution (DC) account balances attributable to the transferred service.

The terms of this proposal include transfer payments made by members and the employer from PERS to LEOFF Plan 2.

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Please see Appendix A for more details.

WHY THIS PROPOSL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This proposal has a cost because service credit in LEOFF 2 is more valuable than service credit in PERS. However, it also provides that there shall be no impact to LEOFF 2 contribution rates. Any costs that result from this proposal will be paid as described below.

This proposal also results in a slight savings in PERS because the reduction in liability from the service credit transfer exceeds the value of assets transferred from PERS to LEOFF Plan 2.

Who Will Pay For These Costs?

Members electing to transfer eligible service pay the difference between the PERS contributions they paid while earning the service credit and the contributions they would have paid as a member of LEOFF 2. Members with past service in PERS 3 must pay the balance in their DC accounts attributable to service credit earned as an enforcement officer in DFW, plus an additional amount, if any, to cover the difference between that balance and the contributions they would have paid in LEOFF 2. These amounts are increased with interest as determined by the director of DRS. DRS will transfer the assets associated with the PERS 2 member and PERS employer contributions with interest from PERS to LEOFF 2.

The proposal provides that no later than June 30, 2015, DFW will pay an additional amount to ensure the LEOFF 2 contribution rates do not change. The proposal also allows for payments prior to 2015 as determined by DRS in consultation with the Office of the State Actuary.

HOW WE VALUED THESE COSTS

Assumptions We Made

We assumed this proposal makes all past PERS service with DFW eligible for transfer to LEOFF 2, and only active DFW enforcement officers may transfer prior service. We assumed members eligible to transfer service credit would elect to transfer that service if the increase in benefits exceeds the additional costs they must pay. See Appendix A for more detail.

We assumed members who transfer service will not receive additional benefits from the transfer until after June 30, 2014. We assumed DRS will perform the calculation of the cost to DFW using annuity factors that use no pre-retirement decrements other than mortality.

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We assumed DRS would charge 8 percent interest when calculating additional contributions due from members electing to transfer their service to LEOFF 2. We also assumed an 8 percent rate of return on DC accounts for Plan 3 members.

Otherwise, we developed these costs using the same assumptions as disclosed in the 2007 Actuarial Valuation Report (AVR).

How We Applied These Assumptions

The proposal gives DFW the responsibility for funding the liability increase to LEOFF 2 not covered by the additional member contributions and assets transferred from PERS.

We calculated the additional contributions for each member with prior eligible PERS 2 service by finding the difference between historical LEOFF 2 and PERS 2 contribution rates and multiplying that difference by their estimated past salaries. We estimated salaries at the time the service was earned. We accumulated those contributions with interest to the present. For members with past PERS 3 service, we calculated the contributions they would have paid if they had been in LEOFF 2, accumulated the contributions with interest to the present, and subtracted their DC account balances.

We estimated the assets transferred from PERS 2 to LEOFF 2 as twice the members' contribution account balances. The assets transferred from PERS 3 to LEOFF 2 equal the employer contributions made during the PERS 3 service, with interest.

To estimate the liability in LEOFF 2, we projected members' age, service, and salary to June 30, 2014 or their LEOFF 2 normal retirement age, whichever was later. Then we calculated the members' final average salary at retirement and multiplied it by a deferred annuity factor.

This proposal also affects PERS by decreasing liabilities and assets when members transfer their service to LEOFF. We used a similar method to find the liability savings in PERS, except we found age, service, and salary for these members under PERS rules for retirement.

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

Special Data Needed

We relied in part on information from the LEOFF Plan 2 Retirement Board and DRS to determine members eligible for the improved benefits under this proposal. The PERS 3 DC balances for eligible members came from annual data provided by DRS. Otherwise, we developed these costs using the same assets and data as disclosed in the AVR.

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Please see Appendix A for a detailed description of how we determined who we expect to transfer service under this proposal.

ACTUARIAL RESULTS

How The Liabilities Changed

This proposal would increase the liability in LEOFF 2 by about $7 million. Assets transferred from PERS, additional member contributions, and a payment by DFW will completely offset this cost.

The liability in PERS would decrease by about $2.7 million under this proposal. The estimated transfer of assets from PERS to LEOFF 2, which consists of the member and employer contributions, with interest, would not completely offset this gain to PERS. This results in a small contribution decrease in PERS.

The members eligible to transfer service credit are currently dual members eligible for portability benefits. The transfer could result in additional experience gains for PERS Plans 2 and 3.

The next table shows a summary of costs/(savings) for all parties:

Summary of Costs/(Savings) for All Parties

(Dollars in Millions)	PERS	LEOFF 2	Total
Change in Present Value of Fully Projected Benefits			
(The Value of the Total Commitment to all Current Members)	($2.7)	$7.0	$4.2
Assets Transferred from PERS to LEOFF 2	2.3	(2.3)	0.0
Additional Member Contributions	0.0	(1.8)	(1.8)
Payment from Department of Fish and Wildlife	0.0	(2.9)	(2.9)
Net Change in Present Value of Unfunded Fully Projected Benefits	($0.5)	$0.0	($0.5)

Note: Totals may not agree due to rounding.

We based these costs on the assumption that 61 out of 81 eligible DFW enforcement officers will transfer past PERS service credit to LEOFF 2. The actual cost of this proposal will depend on the number of affected members who elect to transfer past service.

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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)			
PERS 2/3	**$20,634**	**(2.7)**	**$20,632**
LEOFF 2	**$6,149**	**7.0**	**$6,156**
Unfunded Actuarial Accrued Liability			
(The Portion of the Plan 1 Liability that is Amortized to 2024)			
PERS 2/3	**N/A**	**N/A**	**N/A**
LEOFF 2	**N/A**	**N/A**	**N/A**
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not Covered by Current Assets)			
PERS 2/3	**($2,470)**	**(0.5)**	**($2,470)**
LEOFF 2	**($974)**	**0.0**	**($974)**

How Contribution Rates Changed

The decrease in the required actuarial contribution rate does not round down to the minimum supplemental contribution rate of (0.01 percent); therefore, the proposal will not affect contribution rates in the current biennium. However, we will use the unrounded rate decrease to measure the budget changes in future biennia.

Impact on Contribution Rates: (Effective 09/01/2009)		
System/Plan	**PERS**	**LEOFF**
Current Members		
Employee (Plan 2)	0.000%	0.000%
Employer:		
Normal Cost	0.000%	0.000%
Plan 1 UAAL	0.000%	0.000%
Total	0.000%	0.000%
State		0.000%
New Entrants*		
Employee (Plan 2)	0.000%	0.000%
Employer:		
Normal Cost	0.000%	0.000%
Plan 1 UAAL	0.000%	0.000%
Total	0.000%	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.

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How This Impacts Budgets And Employees

We have not included the estimated $3 million payment by DFW in the budget impacts below.

Budget Impacts			
(Dollars in Millions)	**PERS**	**LEOFF**	**Total**
2009-2011			
General Fund	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**
2011-2013			
General Fund	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0
Total Employer	**(0.1)**	**0.0**	**(0.1)**
Total Employee	**$0.0**	**$0.0**	**$0.0**
2009-2034			
General Fund	($0.1)	$0.0	($0.1)
Non-General Fund	(0.1)	0.0	(0.1)
Total State	**(0.2)**	**0.0**	**(0.2)**
Local Government	(0.2)	0.0	(0.3)
Total Employer	**(0.4)**	**0.0**	**(0.4)**
Total Employee	**($0.3)**	**$0.0**	**($0.3)**

Note: Totals may not agree due to rounding.

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

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

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

The estimated cost to DFW under this proposal is sensitive to the number of members we assume will transfer their PERS service to LEOFF 2. For this pricing exercise we assumed the members who benefit financially from making the transfer would do so. For the sensitivity analysis, we assumed that the members who benefit the most would be the members most likely to transfer their service.

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If only the 14 most costly members transfer, the cost to DFW would be $1 million. If between 15 and 33 of the most expensive transfers occur, DFW would be required to contribute about $2 million. If the top 34 or more members transfer, DFW would pay around $3 million. We assumed 61 members would transfer and this generates a $3 million estimated cost for DFW.

Plan 3 members' DC accounts can be impacted by poor stock market performance. We found our estimated Plan 3 transfer count by comparing their DC account balances to the increased value of their benefits if they were to transfer to LEOFF (see Appendix A for more detail). Therefore, given recent economic events, the number of members electing to transfer their past service from PERS to LEOFF could differ from our assumptions.

To model this sensitivity, we decreased the DC account balance for each Plan 3 member by 25 percent and compared the new balances to the increased value of benefits under this proposal. We found an additional four of the nine PERS 3 members would transfer under these conditions. The table below shows that under this scenario, the liability in LEOFF 2, member contributions, asset transfers from PERS to LEOFF, and the charge to DFW would all increase. There would still be a net liability decrease in PERS, but it would be slightly smaller.

Summary of Costs/(Savings) for All Parties if PERS 3 DC Balances were 25% Lower

(Dollars in Millions)	**PERS**	**LEOFF 2**	**Total**
Change in Present Value of Fully Projected Benefits			
(The Value of the Total Commitment to all Current Members)	($2.8)	$8.3	$5.5
Assets Transferred from PERS to LEOFF 2	2.5	(2.5)	0.0
Additional Member Contributions	0.0	(2.4)	(2.4)
Payment from Department of Fish and Wildlife	0.0	(3.4)	(3.4)
Net Change in Present Value of Unfunded Fully Projected Benefits	($0.3)	$0.0	($0.3)

Note: Totals may not agree due to rounding.

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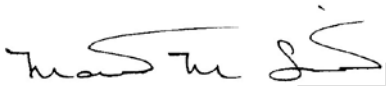
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost 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, assumptions, and data may also be reasonable, and might produce different results.
5. This draft fiscal note has been prepared for the Select Committee on Pension Policy and Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board.
6. This draft fiscal note has been prepared, and opinions given, in accordance with Washington State law and accepted actuarial standards of practice as of the date shown on page one of this draft fiscal note.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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APPENDIX A – Additional Information About the Data We Used

Of the 104 DFW enforcement officers active as of June 30, 2007, we found 81 who had prior service credit in PERS Plans 2 and 3. Among the DFW active records we found a few members with more than the approximately four years of service they could have earned in their current positions since joining LEOFF 2 in 2003. These members probably have past service with other LEOFF agencies. We also observed some active members with no past service in PERS because they began employment after July 2003. Of the LEOFF members with prior PERS service, we found 61 who would likely transfer that service. To determine which members we expect to transfer prior service, we compared estimated liabilities in LEOFF 2 under this proposal with liabilities under current benefit provisions.

We excluded members who become eligible for normal retirement in PERS by June 30, 2014. These members would get the same benefits under portability as provided in this proposal. We also excluded members who become eligible for alternate early retirement in PERS by June 30, 2014. These members would receive smaller reductions in their benefits for early retirement than members with less than 30 years of service. The reduction in PERS benefits would be less costly than the additional contributions they would pay to transfer their PERS service to LEOFF 2.

We excluded members with prior PERS 3 service whose DC account balances were more valuable than the increased lifetime LEOFF benefits they would get under this proposal. These members received a transfer bonus of about 100 percent when they moved their service to Plan 3. Investment returns for these accounts had also been higher than expected from 2003 through 2007. As a result, we found that only two of nine eligible members with past Plan 3 service would likely transfer that service.

If we consider the current market volatility in our analysis, we realize this estimate could change. Recent losses in the stock market could translate to lower future DC account balances. If so, more Plan 3 members might elect to transfer their past service to LEOFF. Please see the section "How the Results Change When the Assumptions Change" for a more thorough description.

The table on the following page shows a demographic summary of the affected members under our best estimate analysis.

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Demographic Summary of the Affected Members				
	Count	Average Service (Years)	Average Savings Fund*	Average Current Salary**
LEOFF Actives	104	4.42	$19,657	$68,776
LEOFF Actives with PERS Service	61	7.76	$18,691	$71,214
PERS Service Range (Rounded, in years)				
0 - 2	17	1.11	$607	$66,981
3 - 5	14	3.38	2,624	70,273
6 - 10	8	7.82	12,916	71,322
11 - 15	12	13.63	36,009	75,197
16 - 20	9	17.69	54,475	75,779
21+	1	22.00	$67,355	$66,621

**PERS 3 amounts represent DC account balances as of June 30, 2008.*
***We use LEOFF 2 salary, effective June 30, 2007, for all records including PERS inactive records.*

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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.

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Office of
The State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

May 12, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

On behalf of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board (Board), I would like to thank you for the cooperative working relationship we have shared in the past and look forward to a similar partnership in the future.

I would like to bring several topics back to your attention as you begin preparation for the 2008 interim. It is our hope that the Select Committee on Pension Policy (SCPP) and the Board can work cooperatively on these issues to once again develop legislation. I have provided a brief summary of each topic for your reference:

Interruptive Military Service Credit

Working cooperatively last interim, the Board and the SCPP jointly endorsed a bill that would have eliminated a member's obligation to pay for interruptive military service credit if the member served during a period of war. The Board is once again interested in working cooperatively with the SCPP on the issue and feels the following additional question will need to be further explored:

- Should the benefit apply to all periods of interruptive military service which have not yet been recovered?

Inflationary Adjustment for $150,000 Death Benefit

The Board is interested in once again working with the SCPP to further study the effect of adding an inflationary adjustment to all the state retirement plans that provide the $150,000 death benefit. In addition to last year's study the Board feels following issues will need to be explored further:

- Should an adjustment in the lump sum amount be made to account for inflation since the creation of the benefit?

- Should both the lump sum adjustment and the addition of the inflationary adjustment be included in the bill?

Military Service Death Benefit

The Board and the SCPP jointly recommended legislation to the 2008 Legislature, which would have provided an unreduced annuity to qualifying survivors of members of all plans, who leave employment due to service in the National Guard or Reserves and die while in military service, during a period of war. The Board would like to continue our joint work to eliminate the "early retirement" actuarial reduction applied to the pensions of members who die while honorably serving our country.

Fish and Wildlife Enforcement Officer Service Credit Transfer

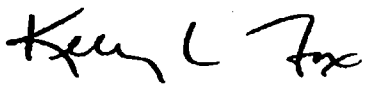
The Board and the SCPP also jointly recommended legislation last session that would have permitted Department of Fish and Wildlife Enforcement Officers to transfer service credit earned in the Public Employees' Retirement System (PERS) Plan 2 as enforcement officers into the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2. The Board feels the following issue may need to be further explored as well:

- Should PERS 3 members be included in the transfer group?

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

We would be happy to meet with you to discuss these topics at an upcoming SCPP or LEOFF Plan 2 Retirement Board meeting. Thank you for your consideration and we look forward to working with you.

Sincerely,



Kelly Fox, Chair

cc: Matt Smith, State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

June 30, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

At the recent meeting of the Select Committee on Pension Policy (SCPP) the chairman requested that the Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board (LEOFF 2 Board) provide a prioritized list of the suggested joint topics that the LEOFF 2 Board would like to work on cooperatively with the SCPP.

During the course of the most recent LEOFF 2 Board meeting we prioritized the suggested topics for cooperation in the following order:

1. **Fish and Wildlife Enforcement Officer Service Credit Transfer**
   Allow FWEO members to transfer their PERS Plan 2 service as enforcement officers to LEOFF Plan 2.

2. **Inflationary Adjustment for $150,000 Death Benefit**
   The $150,000 lump-sum death benefit paid to survivors of public employees who die in the line of duty is not adjusted for inflation.

3. **Interruptive Military Service Credit**
   Members whose public employment is interrupted by military service are required to pay member contributions in order to purchase service credit.

4. **Military Service Death Benefit**
   Beneficiaries of members who die while serving on active duty with the United States Military do not qualify for duty related death benefits.

5. **Purchase of Annuity**
   Members are limited in the amount of money they can convert to a defined benefit by the amount required to purchase 5 years of service.

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly Fox, Chair

cc: Matt Smith, State Actuary

HECB Proposal

Description Of Issue

The Higher Education Coordinating Board (HECB) is seeking statutory authority to offer Higher Education Retirement Plans (HERPs) to some of its employees. The HECB is a Public Employees' Retirement Systems (PERS) employer that actively recruits employees from higher education institutions, which usually offer HERPs.

Granting the HECB authority to offer HERPs to its employees requires changing higher education statutes, not pension statutes. This raises questions around whether the Higher Education Committees of the House and Senate would be more suited to decide this issue, or whether the issue should be coordinated with those committees.

Policy Highlights

- The HECB views this as a recruitment and retention issue.
- HERPs may provide larger benefits than state-administered plans and do not have the same restrictions on post-retirement employment.
- Providing more generous pension benefits to select employees within an agency may impact morale.
- The Washington State Board for Community and Technical Colleges is allowed to offer HERPs to its employees.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 session allowing the HECB to offer HERPs to its employees (HB 3025/SB 6647). The 2008 SCPP bill did not pass the Legislature, but did pass the House and was heard in, but did not pass, the Senate Committee on Ways & Means.

The Committee held a public hearing and took executive action on this issue in May 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 session.

Recommendation To 2009 Legislature

Allow the Higher Education Coordinating Board to offer Higher Education Retirement Plans to employees not already retired from a state-administered retirement system.

Staff Contact

Laura Harper, Policy and Research Services Manager
360.786.6145
harper.laura@leg.wa.gov

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HECB Proposal

In Brief

ISSUE

The Higher Education Coordinating Board (HECB) seeks statutory authority to offer Higher Education Retirement Plans (HERPs) to some of its employees. The HECB is a Public Employees' Retirement System (PERS) employer that actively recruits from higher education institutions, which usually offer HERPs.

MEMBER IMPACT

In 2007 the HECB reported that it had approximately eighty-five employees. Approximately ten of those came from higher education institutions, and about ten more are expected to come from higher education institutions in the near future.

HECB employees who participate in a HERP would no longer accrue service in PERS.

Laura Harper
Policy and Research Services Manager
360.786.6145
harper.laura@leg.wa.gov

Current Situation

The Higher Education Coordinating Board (HECB) is a Public Employees' Retirement System (PERS) employer that proposes to amend the higher education statutes. The HECB seeks authority to offer Higher Education Retirement Plans (HERPs) to its employees. Currently only the following groups have that authority:

- Board of Regents of the State Universities.
- Boards of Trustees of the Regional Universities.
- The Evergreen State College.
- The State Board for Community and Technical Colleges.

These groups define which of their employees are eligible to participate in the higher education retirement plan (HERP) or plans offered. Once the eligible positions are determined, employees in those positions are mandated into the HERP; however, employees who have prior Public Employees' Retirement System (PERS) service are typically offered the choice to remain in PERS.

In contrast, all of the HECB's employees are currently covered by the Public Employees' Retirement System (PERS).

What Is The HECB?

The HECB is a ten-member citizen board that administers the state's student financial aid programs and provides strategic planning, coordination, monitoring, and policy analysis for higher education in Washington. Created by the Legislature in 1985, as successor to the Council for Postsecondary Education, the board is charged by state law with representing the "broad public interest above the interests of the individual colleges and universities." An Advisory Council, which includes K-12 and higher education leaders, advises the board on carrying out its statutory duties.

The HECB employs a staff of approximately eighty-five employees and functions as a state agency. Its employees belong to PERS. Currently, none of these employees are offered the opportunity to join a HERP because the HECB does not have authority to offer such plans to its employees.

What Is The HECB's Interest?

In particular, the HECB has expressed interest in offering participation in the Teachers Insurance and Annuity Association - College Retirement Equities Fund (TIAA – CREF) to some of its employees. This is the most common HERP offered to higher education employees in Washington. The proposal, however, would allow the HECB to offer other higher education retirement benefits.

TIAA-CREF offers a variety of financial products and services to those in the academic, medical, cultural and research fields. The company offers retirement plans with immediate vesting, full portability and member choice of investment options. Members may be allowed to relocate, change future contributions, transfer existing account balances and reallocate funds. Additional member security can be purchased and offered by plan sponsors as a supplemental benefit. For example, after a pre-determined number of years of service, a retirement supplement can be paid to a member if the member's base pension does not provide what has been determined to be an adequate retirement benefit.

The HECB views this as a recruitment and retention issue.

The HECB views the ability to offer this type of plan to its employees as a recruitment and retention issue. According to Don Bennett, HECB Deputy Director, the HECB competes with colleges, universities, and the State Board for Community and Technical Colleges for mid-career staff. It also recruits from colleges and universities throughout the nation as well as from other state higher education executive offices. Mr. Bennett views the inability to offer a HERP as a competitive disadvantage. (See attached letter dated July 16, 2007, and HECB handout.)

The HECB anticipates that its own costs will increase for those employees who would be covered by TIAA-CREF under the expanded authority. To the extent that more

HECB employees seek and obtain TIAA-CREF coverage, those costs could increase over time.

History

The SCPP studied this issue in the 2007 Interim. At that time the SCPP amended the HECB's proposal to limit its application to employees not already retired from a state-administered retirement system. The amendment was designed to prevent HECB employees from simultaneously earning a full salary, drawing a public pension and accruing another retirement benefit in a HERP.

The amended proposal was recommended to the Legislature as HB 3025/SB 6647 (2008). The bill passed the House and was heard in, but did not pass, the Senate Committee on Ways and Means.

Other Higher Education Agencies In Washington State

The Washington State Board for Community and Technical Colleges (SBCTC) is a state agency that is somewhat similar to the HECB. It employs approximately ninety-four people. The State Board provides "general supervision and control over the state system of community and technical colleges." Its responsibilities include preparing a single system operating budget and capital budget request for the Legislature, disbursing capital and operating funds, ensuring statutory compliance, administering criteria for establishing new colleges, establishing operational standards, preparing a comprehensive master plan, and providing research.

SBCTC is specifically authorized by statute to offer higher education retirement plans to its employees. This agency reports that of its ninety-four employees, approximately sixty are reported in PERS and the remaining employees are covered under TIAA-CREF.

The other entities authorized to offer higher education retirement plans in Washington are the higher education institutions themselves.

Other States

Representatives of TIAA-CREF in their Seattle and Denver offices represented to OSA staff during the 2007 Interim that forty-nine government entities in eighteen states offer membership in TIAA-CREF. The types of employees most typically served by TIAA-CREF are in the academic, medical, cultural and research fields.

Questions For Policy Makers

1. What is the impact on PERS? The proposal before the SCPP would leave it to the HECB to determine who is eligible to participate in a HERP. Once a higher education employer determines an employee is eligible for membership in a HERP and the employee decides to participate in the HERP, that employee is exempted from PERS membership. In other words, by participating in a HERP such as TIAA-CREF, HECB employees would no longer be eligible for PERS coverage unless they had prior PERS service and chose to remain in PERS. Thus the proposal, if successful, could lead to a loss of PERS plan members. The number, however, is expected to be small, i.e. no more than the number of employees working for the HECB (currently about eighty-five). It is unclear at this time whether there are other groups who might seek similar treatment in the future. In any event, the proposal is not expected to impact PERS contribution rates.

2. What is the impact on benefits policy? The SCPP may wish to consider the ramifications of a state agency offering different retirement benefits to different individuals within the same agency. For example, if the HECB receives the requested authorization, approximately twenty of its employees would be in TIAA-CREF and sixty-five would be in PERS (at least initially). Since the TIAA-CREF plan is viewed by most people as a more generous plan, this could lead to issues around employee morale and consistent treatment within the plan.

On the other hand, the offering may make the employer more attractive to some employees. As stated by the HECB deputy director, the benefit may enable the HECB to attract highly qualified people from the higher education sector to work at HECB.

There are consequences for members who continue their public employment but change retirement plan participation to a HERP, in that they are removed from coverage by certain programs. (This situation already exists for other retirement system members who are offered HERP participation, such as those employed by the SBCTC.) First, dual membership does not apply to higher education plans. This means that an employee who has been covered in PERS and then becomes covered by TIAA-CREF cannot combine the non-PERS time with the prior PERS time in order to determine benefit eligibility, nor can the salary earned while participating in TIAA-CREF be considered in computing the final retirement benefit from PERS.

Secondly, current retirement system restrictions on post-retirement employment do not apply to those covered by a HERP. This means that a PERS retiree who returns to work in a HERP-covered position can draw the PERS pension, earn a state salary as an employee of the agency, and simultaneously earn a new retirement benefit under TIAA-CREF.

3. How does the proposal impact the higher education institutions? This proposal raises questions about processes that do not typically arise when an issue is brought before the SCPP, primarily because this proposal is to amend the higher education statutes, not the pension statutes.

It is unknown at this time how the higher education institutions currently covered under Title 28B would view this proposal or how they would be impacted. Are they aware of the proposal? Do they support it? Is that important to the SCPP? Is there a desire to formally engage them in the process of crafting legislation that amends the statutes affecting their institutions?

4. Should the Higher Education Committees be involved? The SCPP may also want to think about whether the Higher Education Committees of the House and Senate would be more suited to decide this, or whether the issue should at least be coordinated with those committees. Does the SCPP want to hear what they have to say, or proceed independently?

If the SCPP decides to get involved, the SCPP may want to look at entire proposal and take a position, or alternatively, the SCPP could limit its analysis to the impact of the proposal on the state retirement system.

Possible SCPP Strategies

The Executive Committee did not recommend a strategy.

1. **Sponsor.** Reintroduce the 2008 bill as SCPP-sponsored legislation in 2009.
2. **Endorse.** Move proposal forward as SCPP-endorsed legislation.
3. **Coordinate with the Higher Education Committees.** Provide input limited to describing the impact on PERS, or if sponsoring or endorsing legislation, make such action contingent upon a favorable recommendation from those committees. Another option would be to defer action until the Higher Education Committees have had an opportunity to weigh in on the issue.
4. **Request further study.** Move the issue forward for further study.
5. **Monitor.** Track the progress of the issue, but do not sponsor or endorse.
6. **No action.** Take no action and treat the matter as informational only.

Committee Activity

The SCPP held a public hearing and took executive action on this issue on May 13, 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 session.

Executive Committee Recommendation

None.

Recommendation to 2009 Legislature

Allow the Higher Education Coordinating Board to offer Higher Education Retirement Plans to employees not already retired from a state-administered retirement system. Recommended May 13, 2008.

STAKEHOLDER INPUT

Correspondence attached from:

Don Bennett, Deputy Director of HECB, 7/16/2007.

Bill Draft

A Code Reviser bill draft implementing the Committee's recommendation is attached (Z-0070.1/09).

Draft Fiscal Note

Attached.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0070.1/09

ATTY/TYPIST: LL:ean

BRIEF DESCRIPTION: Authorizing the higher education coordinating board to offer higher education annuities and retirement income plans.

AN ACT Relating to higher education employees' annuities and retirement income plans; and amending RCW 28B.10.400.

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

Sec. 1. RCW 28B.10.400 and 1979 ex.s. c 259 s 1 are each amended to read as follows:

The boards of regents of the state universities, the boards of trustees of the regional universities and of The Evergreen State College, and the state board for community and technical colleges ((~~education~~)) are authorized and empowered:

(1) To assist the faculties and such other employees as any such board may designate in the purchase of old age annuities or retirement income plans under such rules ((~~and regulations~~)) as any such board may prescribe. County agricultural agents, home demonstration agents, 4-H club agents, and assistant county agricultural agents paid jointly by the Washington State University and the several counties shall be deemed to be full time employees of the Washington State University for the purposes hereof;

(2) To provide, under such rules and regulations as any such board may prescribe for the faculty members or other employees under its

supervision, for the retirement of any such faculty member or other employee on account of age or condition of health, retirement on account of age to be not earlier than the sixty-fifth birthday: PROVIDED, That such faculty member or such other employee may elect to retire at the earliest age specified for retirement by federal social security law: PROVIDED FURTHER, That any supplemental payment authorized by subsection (3) of this section and paid as a result of retirement earlier than age sixty-five shall be at an actuarially reduced rate;

(3) To pay to any such retired person or to his or her designated beneficiary(s), each year after his or her retirement, a supplemental amount which, when added to the amount of such annuity or retirement income plan, or retirement income benefit pursuant to RCW 28B.10.415, received by ((~~him or his~~)) the retired person or the retired person's designated beneficiary(s) in such year, will not exceed fifty percent of the average annual salary paid to such retired person for his or her highest two consecutive years of full time service under an annuity or retirement income plan established pursuant to subsection (1) of this section at an institution of higher education: PROVIDED, HOWEVER, That if such retired person prior to ((~~his~~)) retirement elected a supplemental payment survivors option, any such supplemental payments to such retired person or ((~~his~~)) the retired person's designated beneficiary(s) shall be at actuarially reduced rates: PROVIDED FURTHER, That if a faculty member or other employee of an institution of higher education who is a participant in a retirement plan authorized by this section dies, or has died before retirement but after becoming eligible for retirement on account of age, the designated beneficiary(s) shall be entitled to receive the supplemental payment authorized by this subsection ((~~(3) of this section~~)) to which such designated beneficiary(s) would have been entitled had said deceased faculty member or other employee retired on the date of death after electing a supplemental payment survivors option: PROVIDED FURTHER, That for the purpose of this subsection, the designated beneficiary(s) shall be (a) the surviving spouse of the retiree; or, (b) with the written consent of such spouse, if any, such other person or persons as shall have an insurable interest in the retiree's life and shall have been nominated by written designation duly executed and filed with the retiree's institution of higher education;

(4) The higher education coordinating board is also authorized and empowered as described in this section, subject to the following: The board is prohibited from offering or funding a purchased annuity or retirement income plan authorized under this section for the benefit of any retiree who is receiving or accruing a retirement allowance from a public employees' retirement system under Title 41 RCW or chapter 43.43 RCW.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/08**	**Z-0070.1 / Z-0405.1**

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 throughout the 2008 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 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

The proposal is to authorize the Higher Education Coordinating Board (HECB) to offer participation in higher education retirement plans to any or all of its employees, unless the employees are retirees of state-administered plans.

Impact on Pension Liability			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Today's Value of All Future Pensions	$34,695	(2.9)	$34,693
Earned Pensions Not Covered by Today's Assets	$3,609	0.3	$3,609

Impact on Contribution Rates: (Effective 9/1/2009)			
2009-11 State Budget	**PERS**	**SERS**	**PSERS**
Employee (Plan 2)	0.00%	0.00%	0.00%
Employer:			
Current Annual Cost	0.00%	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%	0.00%
Total	0.00%	0.00%	0.00%

Budget Impacts			
(Dollars in Millions)	**2009-2011**	**2011-2013**	**25-Year**
General Fund-State	$0.0	$0.0	$0.0
Total Employer	$0.0	($0.0)	$0.0

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

WHAT IS THE PROPOSED CHANGE?

Summary of Change

This proposal will amend the higher education statutes to include the HECB as one of the entities authorized to offer higher education retirement plans to its employees, unless the employees are retirees of state-administered plans. If passed, the bill wou1d impact potentially all plans of the Public Employees' Retirement System (PERS), but only the members of those plans who are HECB employees in positions chosen by HECB to be covered by a higher education retirement plan (HERP).

Effective Date: 90 days after session

What Is The Current Situation?

Currently employees of the HECB are covered in PERS. The HECB is not currently authorized to offer higher education retirement benefits to its members, as only the following groups have this statutory authority: Board of Regents of the State Universities, Board of Trustees of the Regional Universities, the Evergreen State College, and the State Board for Community and Technical Colleges (SBCTC). Typically, these groups define which of their employees are eligible to participate in the HERP. Once the eligible positions are determined, employees in those positions are mandated into the HERP; however, employees who have prior PERS service are typically offered the choice to remain in PERS. The SBCTC, another higher education agency, currently reports approximately 56 of its 95 employees in PERS and the rest are covered under a HERP known as the Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF).

Who Is Impacted And How?

We estimate this proposal could affect 89 out of the total 158,022 active members of PERS Plans 1, 2 and 3. We assume that 22 of these 89 employees will be designated by their employer as eligible to participate in a HERP.

HERP benefits are not defined under this proposal. As a result, we cannot assess the value of benefits that will be provided by a HERP for the impacted members.

This bill impacts all 120,625 Plan 2 members of PERS 2 through decreased contribution rates. This bill will not affect member contribution rates in Plan 1 since they are fixed in statute. Additionally, this bill will not affect member contribution rates in Plan 3 since Plan 3 members do not contribute to their employer-provided defined benefit.

WHY THIS PROPOSAL HAS A SAVINGS AND WHO BENEFITS FROM IT

Why This Proposal Has A Savings

If this bill is passed, it could result in a loss of PERS members to the extent that HECB employees who are currently covered in PERS plans are offered the choice to either

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remain in PERS or to participate in a higher education retirement plan (HERP). In addition, the plans are impacted to the extent that future employees who would have otherwise been covered in PERS could be covered by a HERP. The HECB would determine the scope of the offering.

If the 22 highest paid HECB employees leave the PERS system, the PERS Plans will see a small loss of pension liabilities since these members will not continue to accrue service under PERS and will not have their future salary increases used in the calculation of their final benefits. This results in a small decrease in the PERS current annual cost.

Additionally, all PERS, SERS, and PSERS employers would experience a small increase in the PERS 1 UAAL (past cost) rate due to the decrease in covered salaries. This increase is offset by the decrease in current annual cost is offset by the increase in PERS 1 past cost for PERS employers.

Who Will Benefit From These Savings?

Members of PERS Plan 2 will pay lower contribution rates in the future, calculated under the standard funding method. PERS employers will pay the same contribution rates in the future. SERS and PSERS employers will pay slightly higher contribution rates in the future due to the increase in the PERS 1 UAAL rate.

HOW WE VALUED THESE COSTS

Assumptions We Made

We assumed the 22 highest paid employees for the HECB would transfer out of PERS and into a HERP.

For more detail please see Appendix A.

How We Applied These Assumptions

We determined the expected future liability for these members. We subtracted the expected future liability from the total liability of the system. Then, we determined the expected future salary for these members. We subtracted the expected future salary from the total salary of the system. Lastly, we calculated the contribution rates for the system using the new liability and salary numbers.

For more detail please see Appendix B.

Special Data Needed

Using the most recent valuation data file, we isolated the 89 HECB active members in the PERS Plans based on their department codes. This allowed us to review the data and select a reasonable group that we expect would be offered a HERP. We selected the 22 highest paid employees and produced a new database with those employees to process through our valuation software.

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Otherwise, we developed these costs using the same assets and data as disclosed in the Actuarial Valuation Report (AVR).

ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of PERS 1, 2, and 3 by decreasing the present value of future benefits payable 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)			
PERS 1	$14,061	($0.1)	$14,061
PERS 2/3	20,634	(2.8)	20,632
PERS Total	**$34,695**	**($2.9)**	**$34,693**
Unfunded Actuarial Accrued Liability			
(The Portion of the Plan 1 Liability that is Amortized to 2024)			
PERS 1	**$3,609**	**$0.3**	**$3,609**
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)			
PERS 1	$3,990	($0.1)	$3,990
PERS 2/3	(2,470)	(0.8)	(2,470)
PERS Total	**$1,520**	**($0.9)**	**$1,519**

Note: Totals may not agree due to rounding.

How The Present Value of Future Salaries (PVFS) Changed

This proposal will impact the actuarial funding of PERS 1, 2, and 3 by decreasing the PVFS of the members as shown below.

Present Value of Future Salaries			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Future Salaries			
(The Value of the Future Salaries Expected to be Paid to Current Members)			
PERS 2/3	$68,137	($15.0)	$68,122
UAAL Present Value of Future Salaries			
(The Value of the Future Salaries Used to Fund the UAAL)			
PERS	$115,651	($23.1)	$115,628

Note: Totals may not agree due to rounding.

How Contribution Rates Changed

The change in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01%, therefore the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate change to measure the fiscal budget changes in future biennia.

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Impact on Contribution Rates: (Effective 9/1/2009)			
System/Plan	**PERS**	**SERS**	**PSERS**
Current Members			
Employee (Plan 2)	-0.001%	0.000%	0.000%
Employer:			
Normal Cost	-0.001%	0.000%	0.000%
Plan 1 UAAL	0.001%	0.001%	0.001%
Total	0.000%	0.001%	0.001%
New Entrants*			
Employee (Plan 2)	0.000%	0.000%	0.000%
Employer:			
Normal Cost	0.000%	0.000%	0.000%
Plan 1 UAAL	0.001%	0.001%	0.001%
Total	0.001%	0.001%	0.001%

**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

We display the projected budget impacts to the affected retirement systems below due to the loss of PERS members. We have not included the budget impacts to the HECB.

	Budget Impacts			
(Dollars in Millions)	**PERS**	**SERS**	**PSERS**	**Total**
2009-2011				
General Fund	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2011-2013				
General Fund	($0.0)	$0.0	$0.0	$0.0
Non-General Fund	(0.0)	0.0	0.0	(0.0)
Total State	**(0.0)**	**0.0**	**0.0**	**(0.0)**
Local Government	(0.0)	0.0	0.0	(0.0)
Total Employer	**(0.0)**	**0.0**	**0.0**	**(0.0)**
Total Employee	**($0.1)**	**$0.0**	**$0.0**	**($0.1)**
2009-2034				
General Fund	($0.0)	$0.1	$0.0	$0.0
Non-General Fund	(0.0)	0.0	0.0	(0.0)
Total State	**(0.0)**	**0.1**	**0.0**	**0.0**
Local Government	(0.1)	0.1	0.0	0.0
Total Employer	**(0.1)**	**0.1**	**0.0**	**0.0**
Total Employee	**($1.1)**	**$0.0**	**$0.0**	**($1.1)**

Note: Totals may not agree due to rounding.

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The analysis of this proposal does not consider any other proposed changes to the system. The combined effect of several changes to the system 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 assumptions and methods:

- The number of members who will leave PERS and join a HERP.

We assumed the 22 highest paid employees would move out of the PERS Plans and into a HERP. The decision to leave PERS and join the HECB HERP will depend on the level of benefits provided under the HERP, which are not defined under this proposal. The decision may also be affected if the employee plans to participate in post-retirement employment. The proposal restricts members from earning any HERP benefits while receiving a retirement allowance from a state-administered retirement plan.

If a smaller number of employees actually leave the PERS Plans, the cost savings would be less than outlined in this draft fiscal note. We excluded 5 members out of the 22 expected to transfer since they are relatively close to retirement and would be less likely to switch. If only 17 members transferred, the resulting liability decrease would be $2.4 million instead of the $2.9 million outlined in the body of this draft fiscal note.

If more HECB employees leave the system than assumed, we would see a higher cost savings to the Plans. If the HECB offered a HERP to all of its employees and all 89 employees left the PERS Plans, the impact would be a decrease in liabilities of $6.8 million versus the $2.9 million under our assumptions.

There is a possibility that the HERP offering would be to a different number of employees or to a different salary range of employees versus what we have assumed. In addition, some employees that are offered the HERP may choose to remain in PERS. However, from a long-term perspective, those positions that are selected by the HECB are likely to transition to non-PERS positions. In any case, we expect that the financial impact to the PERS Plans will be a cost savings with a magnitude that will not impact contribution rates in the next biennium.

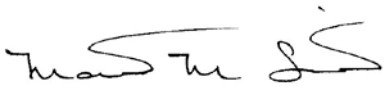
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost 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, assumptions, and data may also be reasonable, and might produce different results.
5. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
6. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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APPENDIX A – ASSUMPTIONS WE MADE

Based on last year's fiscal note, the HECB expects 10 to 20 of their employees will be eligible for a HERP but they have requested authority to offer this to all employees. Since we did not have any data as to which employees will be eligible for the HERP and what level of benefits will be provided under the HERP, we assumed the highest paid 22 employees/positions would leave the PERS Plan and join a HERP. We made this assumption based on the most visible break in salaries outlined below.

We sorted the HECB active employee data by salary and found a reasonable break in salaries at $69,000. This provided us with 22 employees above $69,000 followed by a large group of employees in the $62,000 to $66,000 range.

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

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APPENDIX B – HOW WE APPLIED THESE ASSUMPTIONS

To calculate the cost of this bill, we determined the impact on the PERS Plans if the 22 highest paid current HECB employees terminated their PERS membership to join a HERP. The PERS Plans would be impacted by a loss of liabilities for future service credit and a loss of future contributions associated with these employees.

We calculated the Present Value of Future Benefits (PVFB), the Present Value of Accrued Benefits (PVAB), and the total savings fund (SF) for the 22 highest paid current HECB members. The PVFB is calculated for all 22 employees while the PVAB is calculated for the vested employees and the SF is calculated for the non-vested employees. The difference between these numbers (PVFB - PVAB - SF) represents the decrease in liabilities for future service.

In order to determine the impact due to the loss of future contributions, we calculated the Present Value of Future Salaries (PVFS) for the 22 HECB employees. We reduced the total PERS Plan PVFS by this amount. The resulting PVFS is used, as appropriate by Plan, to determine contributions for the PERS 1 Unfunded Actuarial Accrued Liability (UAAL) and any impact on contribution rates for PERS 2 members and all PERS employers.

Otherwise, we developed these costs using the same methods as disclosed in the June 30, 2007 actuarial valuation report (AVR).

We used the Aggregate actuarial funding method to determine the fiscal budget changes for current plan members.

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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.

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Bill Grinstein
Chair

Ann Daley
Executive Director

STATE OF WASHINGTON
HIGHER EDUCATION COORDINATING BOARD
917 Lakeridge Way • PO Box 43430 • Olympia, WA 98504-3430 • (360) 753-7800 • FAX (360) 753-7808 • www.hecb.wa.gov

July 16, 2007

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, WA 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

The Higher Education Coordinating Board (HECB) is the only higher education agency/institution in Washington state that does not have the authority to offer its employees a purchased annuity and retirement income plan such as the Teachers Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF). We respectfully request that the SCPP support a statutory change allowing the HECB to offer such a plan to its employees.

The HECB competes with colleges, universities, and the State Board for Community and Technical Colleges (SBCTC) for mid-career staff. In addition, the HECB attempts to recruit qualified employees from colleges and universities throughout the nation and from other State Higher Education Executive Offices (SHEEOs). The SBCTC, state universities, and colleges have the statutory authority to assist faculty members and other (generally exempt) employees in the purchase of an annuity or retirement income plan. The HECB is at a competitive disadvantage in attracting and retaining individuals from a higher education background because it cannot offer portability of retirement systems.

RCW 28B.10.400 et seq., relating to annuities and retirement income plans, would need to be amended to include the Higher Education Coordinating Board in the list of employers authorized to offer such a plan. We have enclosed a draft bill amending RCW 28B.10.400 to grant the HECB this authority.

Please feel free to contact me if you have any questions or concerns regarding this request. Thank you for your attention to this matter.

Sincerely,

Don Bennett
Deputy Director

AN ACT Relating to annuities and retirement income plans; amending RCW 28B.10.400; and providing an effective date.

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

The boards of regents of the state universities, the boards of trustees of the regional universities and of The Evergreen State College, ((~~and~~)) the *state board for community ((~~college education~~)) and technical colleges and the higher education coordinating board are authorized and empowered:

(1) To assist the faculties and such other employees as any such board may designate in the purchase of old age annuities or retirement income plans under such rules and regulations as any such board may prescribe. County agricultural agents, home demonstration agents, 4-H club agents, and assistant county agricultural agents paid jointly by the Washington State University and the several counties shall be deemed to be full time employees of the Washington State University for the purposes hereof;

(2) To provide, under such rules and regulations as any such board may prescribe for the faculty members or other employees under its supervision, for the retirement of any such faculty member or other employee on account of age or condition of health, retirement on account of age to be not earlier than the sixty-fifth birthday: PROVIDED, That such faculty member or such other employee may elect to retire at the earliest age specified for retirement by federal social security law: PROVIDED FURTHER, That any supplemental payment authorized by subsection (3) of this section and paid as a result of retirement earlier than age sixty-five shall be at an actuarially reduced rate;

(3) To pay to any such retired person or to his designated beneficiary(s), each year after his retirement, a supplemental amount which, when added to the amount of such annuity or retirement income plan, or retirement income benefit pursuant to RCW 28B.10.415, received by him or his designated beneficiary(s) in such year, will not exceed fifty percent of the average annual salary paid to such retired person for his highest two consecutive years of full time service under an annuity or retirement income plan established pursuant to subsection (1) of this section at an institution of higher education: PROVIDED, HOWEVER, That if such retired person prior to his retirement elected a supplemental payment survivors option, any such supplemental payments to such retired person or his designated beneficiary(s) shall be at actuarially reduced rates: PROVIDED FURTHER, That if a faculty member or other employee of an institution of higher education who is a participant in a retirement plan authorized by this section dies, or has died before retirement but after becoming eligible for retirement on account of age, the designated beneficiary(s) shall be entitled to receive the supplemental payment authorized by this subsection (3) of this section to which such designated beneficiary(s) would have been entitled had said deceased faculty member or other employee retired on the date of death after electing a supplemental payment survivors option: PROVIDED FURTHER, That for the purpose of this subsection, the designated beneficiary(s) shall be (a) the surviving spouse of the retiree; or, (b) with the written consent of such spouse, if any, such other person or persons as

shall have an insurable interest in the retiree's life and shall have been nominated by written designation duly executed and filed with the retiree's institution of higher education.

--- END ---

Interruptive Military Service Credit

Description Of Issue

The SCPP considered whether members should receive up to five years of free service credit for periods of public employment that is interrupted by military service during a period of war as defined in RCW 41.04.005.

Policy Highlights

- The SCPP recommended legislation on this issue in 2008 that did not provide refunds for members who had already paid for interruptive military service during a period of war.
- Stakeholders and policy makers wanted more consistent treatment of members who served during the same period of war.
- A refund policy allows members serving within the same period of war to be treated more consistently.

Policy Options For Applying The Benefit

- **Option 1: Prospective Service Only.**
  - Less generous than the 2008 bill.
  - Results in inconsistent treatment for service in ongoing conflicts.
- **Option 2: All Service, No Refunds.**
  - Same as the SCPP's 2008 bill.
  - Led to complaints of inconsistency.
- **Option 3: All Service, Some Refunds.**
  - Refunds only for service in Operation Iraqi Freedom and Operation Enduring Freedom, including Afghanistan.
  - Provides consistency for participants in ongoing conflicts, but not to those who participated in earlier periods of war.
- **Option 4: All Service, All Refunds.**
  - Refunds for any period in member's career.
  - Provides the most consistent treatment of members.

Committee Activity

Staff briefed the Committee in September and November. The Committee held a public hearing in December and took executive action to recommend Option 4.

Recommendation To 2009 Legislature

Allow members of the open plans to receive up to five years of free service credit for interruptive military service during a period of war as defined in RCW 41.04.005, with refunds to members who have already made payments for such service.

Staff Contact

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Interruptive Military Service

In Brief

ISSUE

Should members receive up to five years of free service credit for periods of public employment that are interrupted by military service during a period of war? If so, should this benefit be applied to past service? Should members who already paid to reinstate past service receive refunds?

MEMBER IMPACT

All active members of the open plans in all systems could potentially be impacted, since all plans provide for interruptive military service credit. OSA estimates that one out of 4,000 members could be impacted by this proposal in a given year.

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Current Situation

"Interruptive military service" includes the following:

- The member leaves public employment to serve in the uniformed services.
- The service is honorable.
- The member returns to public employment upon completion of the service.

Employment practices related to interruptive military service are governed by federal law. At a minimum, public employers must provide their members with the protections specified in the Uniformed Services Employment and Re-employment Rights Act (USERRA). Included in USERRA's re-employment rights is the right to restore retirement plan benefits such as service credit.

Currently, to reinstate service credit for interruptive military service completed on or after October 6, 1994, a member must pay employee contributions (no interest). If the service was completed on or after March 31, 1992, and before October 6, 1994, the member must pay the employee contributions plus interest. For interruptive military service completed on or after October 1, 1977, and before March 31, 1992, the member must pay both the employer and employee contributions plus interest.

A member who cannot return to public employment due to a total disability must also repay contributions to receive interruptive military service credit. In the case of a military death, the member's survivor can pay what would have been the member cost to receive the service credit.

Generally, members must make the required payments within five years of resuming service with their employer, or prior to retirement, whichever comes first. Members who fail to make timely payment have the option of purchasing the service credit by paying the actuarial cost of the resulting increase in their benefits. Survivors must pay the member cost within five years or prior to receiving a benefit.

When the benefit is more generous than what USERRA provides, the Legislature can set parameters for granting the benefit.

The state can be more generous to members than required by USERRA if it so chooses. For example, the Legislature may choose to provide free service credit for members whose public employment is interrupted by military service during a period of war. When the benefit is more generous than what is already provided under federal law, the Legislature can set its own parameters for granting the additional benefit.

Example A

A member voluntarily joins the armed forces during peace time. The member's military service interrupts public employment and the member serves honorably. The member complies with USERRA and repays contributions. The state retirement system must grant interruptive military service credit to the member.

Example B

The Legislature chooses in an upcoming session to improve benefits. The retirement system already complies with USERRA, but the Legislature decides to amend the retirement plan to provide up to five years of free interruptive military service credit for serving honorably during a period of war. [See RCW 41.04.005(2), attached, which defines "period of war."] A plan member can then apply for **free** service credit for those periods of interruptive military service that are defined in **state** law. The parameters for granting free service credit (Example B) are more strict than those for granting standard interruptive military service credit (Example A).

History

The SCPP first studied interruptive military service credit in the 2004 Interim. At that time, the SCPP concluded that USERRA did not adequately address members who were unable to return to public employment due to a death or total disability while serving in the uniformed services. As a result, the SCPP recommended legislation to address this issue. Chapter 64, Laws of 2005 provided that a member with a total disability or a survivor of a deceased member

may purchase service credit for interruptive military service up to the date of death or disability. The law requires repayment of member contributions to reinstate service credit for the period of interruptive military service.

The SCPP also studied interruptive military service in the 2007 Interim. The Committee decided that more should be done for retirement system members whose public employment was interrupted by military service during a period of war.

The SCPP recommended a bill for the 2008 Legislative Session that would have granted up to five years of free service credit for interruptive military service during a period of war.

The SCPP recommended a bill for the 2008 Legislative Session that would have granted up to five years of free service credit for interruptive military service during a period of war. Period of war is defined in RCW 41.04.005(2) (copy attached). The bill was endorsed by the Law Enforcement Officers' and Fire Fighters' Plan 2 Board (LEOFF 2 Board). SSB 6645 (2008) passed Senate Ways and Means and was not heard in the House.

During the current interim, the SCPP received correspondence from the LEOFF 2 Board requesting that the Board and the SCPP work cooperatively to submit a bill in 2009 on this issue. The LEOFF 2 Board seeks to eliminate members' obligation to pay contributions to obtain service credit for interruptive military service during a period of war. The Board identified the issue as priority number three out of five issues for SCPP coordination. The LEOFF 2 Board also requested that the SCPP explore possible retroactive application of the bill.

Policy Analysis

The SCPP Can Give Better Benefits Than Those Required By Federal Law.

USERRA treats employees as if they had been continuously employed during the period of interruptive military service.

Interruptive military service is governed by federal law. At a minimum, public employers must provide the protections specified in USERRA. This law provides for the re-employment of individuals who leave employment to serve in the "uniformed services," a term that is federally defined and includes most types of military service. Included in USERRA's re-employment rights is the right to restoration of retirement plan benefits.

For employers, the fundamental requirement of USERRA as it relates to retirement plan benefits is to provide for

recovery of the benefits that a re-employed participant did not receive due to qualifying military service. The employee must be treated for vesting and benefit accrual purposes as if he or she had been continuously employed. Thus, the member must pay the contributions that would have been paid during the period of service, and can receive service credit as if there had been no interruption in employment.

USERRA pre-empts state retirement policy in that all public employers must meet the minimum requirements of this federal law. However as mentioned above, employers have the discretion to go beyond USERRA and grant benefits for periods of interruptive service that are more generous than those available under the act. Employers who choose to go beyond USERRA may do so by using a variety of methods. They can grant free service credit for periods of interruptive military service. They can reward active duty by paying all or part of the contributions that the member would have paid during the period of active duty. Employers may also provide all or part of the member's salary during such periods. Enhanced benefits can be limited as long as the basic USERRA protections remain intact for all interruptive military service in the uniformed services.

Most of Washington's closed plans provide free interruptive military service credit.

Comparison With Other Washington Plans

Currently, free interruptive military service credit is available to members in most of the closed plans, including Plan 1 of the Public Employees' Retirement System (PERS 1), Plan 1 of the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF 1), and Plan 1 of the Washington State Patrol Retirement System (WSPRS). This benefit is not available in Plan 1 of the Teachers' Retirement System (TRS).

Comparison With Other States*

**This research was conducted for the SCPP in the 2007 Interim.*

California, Idaho, Iowa, and Wisconsin provide free interruptive military service credit. None of these states limit free credit to declared wars or armed conflicts.

Ohio allows members to purchase interruptive military service credit under USERRA, and also grants free service

Washington's peer states are split on the issue.

credit to members under more restrictive conditions, including requirements that members participate in the retirement system on a contributing basis for one year prior to and one year after the interruptive military service.

Florida is a non-contributory state, meaning members do not contribute to their retirement benefits. Thus, there are no member contributions to repay in order to receive interruptive military service credit under USERRA.

Missouri's plans differ. The State Employees' plan is non-contributory like Florida's. The Public School Plan allows members to purchase service under USERRA. The Local Government Plan provides free interruptive service for USERRA-qualified service.

The remaining states – Colorado, Minnesota, and Oregon – require members to repay contributions.

Reasons For And Against Providing Free Service Credit

The following table summarizes some of the policy pros and cons of providing special or increased benefits to members based on military service:

Free military service credit has pros and cons.

No Additional Special Benefits	Additional Special Benefits
Members serve voluntarily; no draft requires them to leave employment	Encourage military service; help avoid need for a draft
Members already receive adequate federal compensation and benefits for military service	Support ability to recruit more military personnel into state service and more state personnel into military service
Other members and employers would not have to absorb extra costs for these members	Support view that all WA citizens benefit, directly or indirectly, from military service rendered by public employees
More favorable service credit treatment is already given to these members via federal law (no interest, 5 years to repay)	Recognize that members who serve in conflicts are at higher risk for injury or death; pension plans typically offer extra support for high risk occupations that serve the public at large
Military service is unrelated to the service rewarded by state pension plans	Supplement federal benefits, which may not be viewed as adequate

The LEOFF 2 Board asked the SCPP to give additional consideration to how the benefit is applied. Four options are outlined here.

How Should The Benefit Be Applied?

In testimony before the SCPP at its July 15, 2008, meeting, the LEOFF 2 Board's Executive Director asked that the SCPP consider possible retroactive application of the bill. There are several options that policy-makers might choose for determining who would be eligible to receive free interruptive military service credit for periods of war. The options range from a prospective application of the benefit to a retroactive application with refunds.

Option 1 – Prospective Service Only

Under this option, only up to five years of interruptive military service after the effective date of the bill would be free and credited to members without repayment of member contributions. This approach is the least generous to members of the four options described but is also the least costly. It is the more common approach to benefit improvements, as it allows for contributions to be adjusted along with the implementation of the benefit improvement. This approach is also consistent with principles of intergenerational equity (meaning that each generation of taxpayers should pay only for the benefits associated with the services rendered to that generation of taxpayers). One possible concern with this approach is that service within the same conflict is treated differently – some is free and some is not.

Option 2 – Past And Prospective Service With No Refunds

Under this option, up to five years of free interruptive military service credit would be available to members who apply for the service credit after the effective date of the bill. Members can apply for interruptive military service credit any time up to their retirement. Thus, active members who have not yet retired could pick up five years of free service credit for any periods of war in their career for which service credit was not already restored by repaying contributions– even those periods that were prior to the effective date of the bill. This option corresponds to last year's SCPP bill.

The SCPP's 2008 bill did not provide for refunds. A concern with this approach has been that persons who already paid for their interruptive military service credit may feel that they are being unfairly treated.

Option 3 – Past And Prospective Service With Refunds For Recent Service

This option seeks to provide the same free service as in Option 2, but would also pay refunds to those who already reinstated service credit for the following periods of war: Operation Iraqi Freedom (Persian Gulf) and/or Operation Enduring Freedom (southern or central Asia, including Afghanistan).

Refunding member contributions creates administrative burdens and increases cost. On the other hand, this approach may provide consistent benefits for all members participating in ongoing periods of war.

Option 4 – Past And Prospective Service With Refunds For All Service

This option would provide the same free service as in Option 2, but would also pay refunds to those who already reinstated service credit for any period of war during their career. Even more refunds would be paid from plan funds than under Option 3. This option would be the most generous to members, the most costly and the hardest to administer. It may help provide consistent benefits for members who participated in periods of war.

Committee Activity

Staff briefed the Committee on this issue in September and November. The Committee held a public hearing in December and took executive action recommending Option 4 to the 2009 Legislature.

Executive Committee Recommendation

Option 3: Past and prospective service with refunds for recent service. Recommended November 18, 2008.

Recommendation To 2009 Legislature

Allow members of the open plans to receive up to five years of free service credit for interruptive military service during a period of war as defined in RCW 41.04.005, with refunds to members who have already made payments for such service (Option 4). Recommended December 16, 2008.

Stakeholder Input

Correspondence attached from:

Kelly Fox, Chair, LEOFF 2 Board, 5/12/2008 and 6/30/2008.

Correspondence on file from:

John Kvamme, WASA & AWSP Consultant, 5/12/2008.

Bill Draft

A Code Reviser bill draft implementing the Committee's recommendation is attached (Z-0408.1/09).

Draft Fiscal Note

Attached.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0408.1/09

ATTY/TYPIST: LL:lel

BRIEF DESCRIPTION: Addressing interruptive military service credit within plans 2 and 3 of the public employees' retirement system, plans 2 and 3 of the school employees' retirement system, plans 2 and 3 of the teachers' retirement system, plan 2 of the law enforcement officers' and firefighters' retirement system, plan 2 of the Washington state patrol retirement system, and the public safety employees' retirement system.

AN ACT Relating to interruptive military service credit within plans 2 and 3 of the public employees' retirement system, plans 2 and 3 of the school employees' retirement system, plans 2 and 3 of the teachers' retirement system, plan 2 of the law enforcement officers' and firefighters' retirement system, plan 2 of the Washington state patrol retirement system, and the public safety employees' retirement system; and amending RCW 41.40.710, 41.40.805, 41.37.260, 41.35.470, 41.35.650, 41.32.810, 41.32.865, 41.26.520, and 43.43.260.

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

Sec. 1. RCW 41.40.710 and 2005 c 64 s 2 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit as provided for under the provisions of RCW 41.40.610 through 41.40.740.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence.

This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The compensation earnable reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (4) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. Such credit may be obtained only if:

(a) The member makes both the plan 2 employer and member contributions plus interest as determined by the department for the period of the authorized leave of absence within five years of resumption of service or prior to retirement whichever comes sooner; or

(b) If not within five years of resumption of service but prior to retirement, pay the amount required under RCW 41.50.165(2).

The contributions required under (a) of this subsection shall be based on the average of the member's compensation earnable at both the time the authorized leave of absence was granted and the time the member resumed employment.

(4) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

(a) The member qualifies for service credit under this subsection if:

(i) Within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services; and

(ii) The member makes the employee contributions required under RCW 41.45.061 and 41.45.067 within five years of resumption of service or prior to retirement, whichever comes sooner; or

(iii) Prior to retirement and not within ninety days of the member's honorable discharge or five years of resumption of service the member pays the amount required under RCW 41.50.165(2)<u>; or</u>

<u>(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service in a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection</u>.

(b) Upon receipt of member contributions under (a)(ii), (d)(iii), or (e)(iii) of this subsection, <u>or adequate proof under (a)(iv), (d)(iv), or (e)(iv) of this subsection,</u> the department shall establish the member's service credit and shall bill the employer for its contribution required under RCW 41.45.060, 41.45.061, and 41.45.067 for the period of military service, plus interest as determined by the department.

(c) The contributions required under (a)(ii), (d)(iii), or (e)(iii) of this subsection shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(d) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under chapter 41.45 RCW within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or eligible child or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(e) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under chapter 41.45 RCW within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount

shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

Sec. 2. RCW 41.40.805 and 2005 c 64 s 3 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence. This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The earnable compensation reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (4) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. Such credit may be obtained only if:

(a) The member makes the contribution on behalf of the employer, plus interest, as determined by the department; and

(b) The member makes the employee contribution, plus interest, as determined by the department, to the defined contribution portion.

The contributions required shall be based on the average of the member's earnable compensation at both the time the authorized leave of absence was granted and the time the member resumed employment.

(4) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service if within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for

reemployment with the employer who employed the member immediately prior to the member entering the uniformed services. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

The department shall establish the member's service credit and shall bill the employer for its contribution required under RCW 41.45.060 and 41.45.067 for the period of military service, plus interest as determined by the department. Service credit under this subsection may be obtained only if the member makes the employee contribution to the defined contribution portion as determined by the department, or prior to retirement, the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

The contributions required shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(a) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under this subsection within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(b) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under this subsection within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount

shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

Sec. 3. RCW 41.37.260 and 2005 c 64 s 11 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit as provided for under RCW 41.37.190 through 41.37.290.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence. This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The compensation earnable reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (4) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. This credit may be obtained only if:

(a) The member makes both the employer and member contributions plus interest as determined by the department for the period of the authorized leave of absence within five years of resumption of service or prior to retirement whichever comes sooner; or

(b) If not within five years of resumption of service but prior to retirement, pay the amount required under RCW 41.50.165(2).

The contributions required under (a) of this subsection shall be based on the average of the member's compensation earnable at both the time the authorized leave of absence was granted and the time the member resumed employment.

(4) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

(a) The member qualifies for service credit under this subsection if:

(i) Within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services; and

(ii) The member makes the employee contributions required under RCW 41.37.220 within five years of resumption of service or prior to retirement, whichever comes sooner; or

(iii) Prior to retirement and not within ninety days of the member's honorable discharge or five years of resumption of service the member pays the amount required under RCW 41.50.165(2)<u>; or</u>

<u>(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection</u>.

(b) Upon receipt of member contributions under (a)(ii), (d)(iii), or (e)(iii) of this subsection, <u>or adequate proof under (a)(iv), (d)(iv), or (e)(iv) of this subsection,</u> the department shall establish the member's service credit and shall bill the employer for its contribution required under RCW 41.37.220 for the period of military service, plus interest as determined by the department.

(c) The contributions required under (a)(ii), (d)(iii), or (e)(iii) of this subsection shall be based on the compensation the member would

have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(d) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under chapter 41.45 RCW within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(e) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under chapter 41.45 RCW within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

Sec. 4. RCW 41.35.470 and 2005 c 64 s 4 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit as provided for under the provisions of RCW 41.35.400 through 41.35.599.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence. This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The compensation earnable reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (4) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. Such credit may be obtained only if:

(a) The member makes both the plan 2 employer and member contributions plus interest as determined by the department for the period of the authorized leave of absence within five years of resumption of service or prior to retirement whichever comes sooner; or

(b) If not within five years of resumption of service but prior to retirement, pay the amount required under RCW 41.50.165(2).

The contributions required under (a) of this subsection shall be based on the average of the member's compensation earnable at both the time the authorized leave of absence was granted and the time the member resumed employment.

(4) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

(a) The member qualifies for service credit under this subsection if:

(i) Within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services; and

(ii) The member makes the employee contributions required under RCW 41.35.430 within five years of resumption of service or prior to retirement, whichever comes sooner; or

(iii) Prior to retirement and not within ninety days of the member's honorable discharge or five years of resumption of service the member pays the amount required under RCW 41.50.165(2)<u>; or</u>

<u>(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form</u>

provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(b) Upon receipt of member contributions under (a)(ii), (d)(iii), or (e)(iii) of this subsection, or adequate proof under (a)(iv), (d)(iv), or (e)(iv) of this subsection, the department shall establish the member's service credit and shall bill the employer for its contribution required under RCW 41.35.430 for the period of military service, plus interest as determined by the department.

(c) The contributions required under (a)(ii), (d)(iii), or (e)(iii) of this subsection shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(d) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under chapter 41.45 RCW within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the

distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(e) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under chapter 41.45 RCW within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

Sec. 5. RCW 41.35.650 and 2005 c 64 s 5 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence. This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The earnable compensation reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (4) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. Such credit may be obtained only if:

(a) The member makes the contribution on behalf of the employer, plus interest, as determined by the department; and

(b) The member makes the employee contribution, plus interest, as determined by the department, to the defined contribution portion.

The contributions required shall be based on the average of the member's earnable compensation at both the time the authorized leave of absence was granted and the time the member resumed employment.

(4) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service if within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

The department shall establish the member's service credit and shall bill the employer for its contribution required under RCW 41.35.720 for the period of military service, plus interest as determined by the department. Service credit under this subsection may be obtained only if the member makes the employee contribution to the

defined contribution portion as determined by the department, or prior to retirement, the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

The contributions required shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(a) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under this subsection within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department,

request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(b) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under this subsection within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

Sec. 6. RCW 41.32.810 and 2005 c 64 s 7 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit as provided for under the provisions of RCW 41.32.755 through 41.32.825.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence. This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The earnable compensation reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (6) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. Such credit may be obtained only if the member makes both the employer and member contributions plus interest as determined by the department for the period of the authorized leave of absence within five years of resumption of service or prior to retirement whichever comes sooner.

(4) If a member fails to meet the time limitations of subsection (3) of this section, the member may receive a maximum of two years of service credit during a member's working career for those periods when a member is on unpaid leave of absence authorized by an employer. This may be done by paying the amount required under RCW 41.50.165(2) prior to retirement.

(5) For the purpose of subsection (3) of this section, the contribution shall not include the contribution for the unfunded supplemental present value as required by RCW 41.32.775. The contributions required shall be based on the average of the member's earnable compensation at both the time the authorized leave of absence was granted and the time the member resumed employment.

(6) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

(a) The member qualifies for service credit under this subsection if:

(i) Within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services; and

(ii) The member makes the employee contributions required under RCW 41.32.775 within five years of resumption of service or prior to retirement, whichever comes sooner; or

(iii) Prior to retirement and not within ninety days of the member's honorable discharge or five years of resumption of service the member pays the amount required under RCW 41.50.165(2)<u>; or</u>

<u>(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection</u>.

(b) Upon receipt of member contributions under (a)(ii), (d)(iii), or (e)(iii) of this subsection, <u>or adequate proof under (a)(iv), (d)(iv), or (e)(iv) of this subsection,</u> the department shall establish the member's service credit and shall bill the employer for its contribution required under RCW 41.32.775 for the period of military service, plus interest as determined by the department.

(c) The contributions required under (a)(ii), (d)(iii), or (e)(iii) of this subsection shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(d) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service

credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under chapter 41.45 RCW within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(e) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under chapter 41.45 RCW within five years of the director's determination of

total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

Sec. 7. RCW 41.32.865 and 2005 c 64 s 8 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence. This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The earnable compensation reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (4) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. Such credit may be obtained only if:

(a) The member makes the contribution on behalf of the employer, plus interest, as determined by the department; and

(b) The member makes the employee contribution, plus interest, as determined by the department, to the defined contribution portion.

The contributions required shall be based on the average of the member's earnable compensation at both the time the authorized leave of absence was granted and the time the member resumed employment.

(4) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service if within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

The department shall establish the member's service credit and shall bill the employer for its contribution required under chapter 239, Laws of 1995 for the period of military service, plus interest as determined by the department. Service credit under this subsection may be obtained only if the member makes the employee contribution to the defined contribution portion as determined by the department<u>, or prior to retirement, the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection</u>.

The contributions required shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(a) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may,

on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under this subsection within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(b) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under

this subsection within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

Sec. 8. RCW 41.26.520 and 2005 c 64 s 9 are each amended to read as follows:

(1) A member who is on a paid leave of absence authorized by a member's employer shall continue to receive service credit as provided for under the provisions of RCW 41.26.410 through 41.26.550.

(2) A member who receives compensation from an employer while on an authorized leave of absence to serve as an elected official of a labor organization, and whose employer is reimbursed by the labor organization for the compensation paid to the member during the period of absence, may also be considered to be on a paid leave of absence. This subsection shall only apply if the member's leave of absence is authorized by a collective bargaining agreement that provides that the member retains seniority rights with the employer during the period of leave. The basic salary reported for a member who establishes service credit under this subsection may not be greater than the salary paid to the highest paid job class covered by the collective bargaining agreement.

(3) Except as specified in subsection (7) of this section, a member shall be eligible to receive a maximum of two years service credit during a member's entire working career for those periods when a member is on an unpaid leave of absence authorized by an employer. Such credit may be obtained only if the member makes the employer, member,

and state contributions plus interest as determined by the department for the period of the authorized leave of absence within five years of resumption of service or prior to retirement whichever comes sooner.

(4) A law enforcement member may be authorized by an employer to work part time and to go on a part-time leave of absence. During a part-time leave of absence a member is prohibited from any other employment with their employer. A member is eligible to receive credit for any portion of service credit not earned during a month of part-time leave of absence if the member makes the employer, member, and state contributions, plus interest, as determined by the department for the period of the authorized leave within five years of resumption of full-time service or prior to retirement whichever comes sooner. Any service credit purchased for a part-time leave of absence is included in the two-year maximum provided in subsection (3) of this section.

(5) If a member fails to meet the time limitations of subsection (3) or (4) of this section, the member may receive a maximum of two years of service credit during a member's working career for those periods when a member is on unpaid leave of absence authorized by an employer. This may be done by paying the amount required under RCW 41.50.165(2) prior to retirement.

(6) For the purpose of subsection (3) or (4) of this section the contribution shall not include the contribution for the unfunded supplemental present value as required by RCW 41.45.060, 41.45.061, and 41.45.067. The contributions required shall be based on the average of the member's basic salary at both the time the authorized leave of absence was granted and the time the member resumed employment.

(7) A member who leaves the employ of an employer to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service. This subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

(a) The member qualifies for service credit under this subsection if:

(i) Within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services; and

(ii) The member makes the employee contributions required under RCW 41.45.060, 41.45.061, and 41.45.067 within five years of resumption of service or prior to retirement, whichever comes sooner; or

(iii) Prior to retirement and not within ninety days of the member's honorable discharge or five years of resumption of service the member pays the amount required under RCW 41.50.165(2)<u>; or</u>

<u>(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection</u>.

(b) Upon receipt of member contributions under (a)(ii), (d)(iii), or (e)(iii) of this subsection, <u>or adequate proof under (a)(iv), (d)(iv), or (e)(iv) of this subsection,</u> the department shall establish the member's service credit and shall bill the employer and the state for their respective contributions required under RCW 41.26.450 for the period of military service, plus interest as determined by the department.

(c) The contributions required under (a)(ii), (d)(iii), or (e)(iii) of this subsection shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(d) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(i) Provides to the director proof of the member's death while serving in the uniformed services;

(ii) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(iii) Pays the employee contributions required under chapter 41.45 RCW within five years of the date of death or prior to the distribution of any benefit, whichever comes first;or

(iv) Prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(e) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(i) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(ii) The member provides to the director proof of honorable discharge from the uniformed services; and

(iii) The member pays the employee contributions required under chapter 41.45 RCW within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(iv) Prior to retirement the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for

service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(8) A member receiving benefits under Title 51 RCW who is not receiving benefits under this chapter shall be deemed to be on unpaid, authorized leave of absence.

Sec. 9. RCW 43.43.260 and 2005 c 64 s 10 are each amended to read as follows:

Upon retirement from service as provided in RCW 43.43.250, a member shall be granted a retirement allowance which shall consist of:

(1) A prior service allowance which shall be equal to two percent of the member's average final salary multiplied by the number of years of prior service rendered by the member.

(2) A current service allowance which shall be equal to two percent of the member's average final salary multiplied by the number of years of service rendered while a member of the retirement system.

(3)(a) Any member commissioned prior to January 1, 2003, with twenty-five years service in the Washington state patrol may have the member's service in the uniformed services credited as a member whether or not the individual left the employ of the Washington state patrol to enter such uniformed services: PROVIDED, That in no instance shall military service in excess of five years be credited: AND PROVIDED FURTHER, That in each instance, a member must restore all withdrawn accumulated contributions, which restoration must be completed on the date of the member's retirement, or as provided under RCW 43.43.130, whichever occurs first: AND PROVIDED FURTHER, That this section shall not apply to any individual, not a veteran within the meaning of RCW 41.06.150.

(b) A member who leaves the Washington state patrol to enter the uniformed services of the United States shall be entitled to retirement system service credit for up to five years of military service. This

subsection shall be administered in a manner consistent with the requirements of the federal uniformed services employment and reemployment rights act.

(i) The member qualifies for service credit under this subsection if:

(A) Within ninety days of the member's honorable discharge from the uniformed services of the United States, the member applies for reemployment with the employer who employed the member immediately prior to the member entering the uniformed services; and

(B) The member makes the employee contributions required under RCW 41.45.0631 and 41.45.067 within five years of resumption of service or prior to retirement, whichever comes sooner; or

(C) Prior to retirement and not within ninety days of the member's honorable discharge or five years of resumption of service the member pays the amount required under RCW 41.50.165(2)<u>; or</u>

<u>(D) If the member was commissioned on or after January 1, 2003, and, prior to retirement, the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service credit during a period of war may receive no more than five years of free retirement system service credit under this subsection</u>.

(ii) Upon receipt of member contributions under (b)(i)(B), (b)(iv)(C), and (b)(v)(C) of this subsection, <u>or adequate proof under (b)(i)(D), (b)(iv)(D), or (b)(v)(D) of this subsection,</u> the department shall establish the member's service credit and shall bill the employer for its contribution required under RCW 41.45.060 for the period of military service, plus interest as determined by the department.

(iii) The contributions required under (b)(i)(B), (b)(iv)(C), and (b)(v)(C) of this subsection shall be based on the compensation the member would have earned if not on leave, or if that cannot be estimated with reasonable certainty, the compensation reported for the member in the year prior to when the member went on military leave.

(iv) The surviving spouse or eligible child or children of a member who left the employ of an employer to enter the uniformed services of the United States and died while serving in the uniformed services may, on behalf of the deceased member, apply for retirement system service credit under this subsection up to the date of the member's death in the uniformed services. The department shall establish the deceased member's service credit if the surviving spouse or eligible child or children:

(A) Provides to the director proof of the member's death while serving in the uniformed services;

(B) Provides to the director proof of the member's honorable service in the uniformed services prior to the date of death; and

(C) If the member was commissioned on or after January 1, 2003, pays the employee contributions required under chapter 41.45 RCW within five years of the date of death or prior to the distribution of any benefit, whichever comes first; or

(D) If the member was commissioned on or after January 1, 2003, and, prior to the distribution of any benefit, provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. If the deceased member made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005, the surviving spouse or eligible child or children may, prior to the distribution of any benefit and on a form provided by the department, request a refund of the funds standing to the deceased member's credit for up to five years of such service, and this amount shall be paid to the surviving spouse or children. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(v) A member who leaves the employ of an employer to enter the uniformed services of the United States and becomes totally incapacitated for continued employment by an employer while serving in the uniformed services is entitled to retirement system service credit under this subsection up to the date of discharge from the uniformed services if:

(A) The member obtains a determination from the director that he or she is totally incapacitated for continued employment due to conditions or events that occurred while serving in the uniformed services;

(B) The member provides to the director proof of honorable discharge from the uniformed services; and

(C) If the member was commissioned on or after January 1, 2003, the member pays the employee contributions required under chapter 41.45 RCW within five years of the director's determination of total disability or prior to the distribution of any benefit, whichever comes first; or

(D) If the member was commissioned on or after January 1, 2003, and, prior to retirement, the member provides to the director proof that the member's interruptive military service was during a period of war as defined in RCW 41.04.005. Any member who made payments for service credit for interruptive military service during a period of war as defined in RCW 41.04.005 may, prior to retirement and on a form provided by the department, request a refund of the funds standing to his or her credit for up to five years of such service, and this amount shall be paid to him or her. Members with one or more periods of interruptive military service during a period of war may receive no more than five years of free retirement system service credit under this subsection.

(4) In no event shall the total retirement benefits from subsections (1), (2), and (3) of this section, of any member exceed seventy-five percent of the member's average final salary.

(5) Beginning July 1, 2001, and every year thereafter, the department shall determine the following information for each retired member or beneficiary whose retirement allowance has been in effect for at least one year:

(a) The original dollar amount of the retirement allowance;

(b) The index for the calendar year prior to the effective date of the retirement allowance, to be known as "index A";

(c) The index for the calendar year prior to the date of determination, to be known as "index B"; and

(d) The ratio obtained when index B is divided by index A.

The value of the ratio obtained shall be the annual adjustment to the original retirement allowance and shall be applied beginning with the July payment. In no event, however, shall the annual adjustment:

(i) Produce a retirement allowance which is lower than the original retirement allowance;

(ii) Exceed three percent in the initial annual adjustment; or

(iii) Differ from the previous year's annual adjustment by more than three percent.

For the purposes of this section, "index" means, for any calendar year, that year's average consumer price index for the Seattle-Tacoma-Bremerton Washington area for urban wage earners and clerical workers, all items, compiled by the bureau of labor statistics, United States department of labor.

The provisions of this section shall apply to all members presently retired and to all members who shall retire in the future.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**1/02/09**	**Z-0408.1 / Z-0409.1**

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 and Law Enforcement Officers' and Fire Fighters' (LEOFF) Retirement System Plan 2 throughout the 2008 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 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 would allow up to five years free retirement system service credit for members whose interruptive military service is during a period of war as defined in RCW 41.04.005. It would also provide refunds to members who have already made payments for such service.

Impact on Pension Liability

(Dollars in Millions)	Current	Increase	Total
Today's Value of All Future Pensions	$67,081	$1.3	$67,082
Earned Pensions Not Covered by Today's Assets	$4,957	$0.0	$4,957

Impact on Contribution Rates: (Effective 9/1/2009)

2009-2011 State Budget	PERS	TRS	SERS	PSERS	LEOFF	WSPRS
Employee (Plan 2)	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Employer:						
Current Annual Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Total	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
State					0.00%	

Budget Impacts

(Dollars in Millions)	2009-2011	2011-2013	25-Year
General Fund-State	$0.0	$0.1	$1.1
Total Employer	$0.0	$0.2	$4.0

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

WHAT IS THE PROPOSED CHANGE?

Summary Of Benefit Improvement/Change

This proposal impacts the following systems:

- Public Employees' Retirement System (PERS) Plans 2/3
- Teachers' Retirement System (TRS) Plans 2, 3
- School Employees' Retirement System (SERS) Plans 2/ 3
- Public Safety Employees' Retirement System (PSERS)
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2
- Washington State Patrol Retirement System (WSPRS) Plan 2

The proposal would eliminate the member obligation to repay member contributions in order to receive up to five years of service credit for interruptive military service during a period of war. In the case of a military death, the survivor would also be relieved of paying the member cost for interruptive military service credit during a period of war. "Period of war" is defined in RCW 41.04.005.

The proposal also provides for refunds of member payments made for up to five years of interruptive military service credit during a period of war.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

Currently, for interruptive military service completed on or after October 6, 1994, a member must pay the missed employee contributions (no interest) to receive service credit. For interruptive military service completed on or after March 31, 1992, and before October 6, 1994, the member must pay the missed contributions plus interest to receive service credit. For interruptive military service completed on or after October 1, 1977, and before March 31, 1992, the member must pay both the missed employer and employee contributions plus interest to receive service credit.

Members must make the required contributions within five years of resuming service with their employer, or prior to retirement, whichever comes first. Members who fail to make timely payment have the option of purchasing the service credit by paying the actuarial cost of the resulting increase in their benefits. In the case of a military death, a survivor who applies for the member's interruptive military service credit must pay the member cost within five years of the member's death or prior to receiving a benefit, whichever comes first.

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Who Is Impacted And How?

We estimate that all 120,625 active members of PERS Plan 2, all 24,422 active members of PERS Plan 3, all 6,752 active members of TRS Plan 2, all 51,856 active members of TRS Plan 3, all 17,767 active members of SERS Plan 2, all 33,058 active members of SERS Plan 3, all 2,755 active members of PSERS Plan 2, all 16,099 active members of LEOFF Plan 2, and all 152 active members of WSPRS Plan 2 could be affected by this bill through improved benefits. However, we only expect approximately 1 out of 4,000 to be impacted in a given year.

We estimate that for a typical Plan 2 member impacted by this bill, the increase in benefits would be free interruptive military service credit versus the choice to pay for interruptive military service credit. For example, a 36 year old male in PERS 2 with 7 years of service and a $46,600 salary would receive free interruptive military service credit valued at approximately $2,500 per year of military service, whereas without this benefit the member could choose to purchase interruptive military service credit for that same amount.

The benefit for a typical Plan 3 member is the removal of the required contribution to their defined contribution account upon purchase of military service.

Additionally, Plan 2 members would be affected by this proposal through increased contribution rates in future biennia.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This bill has a cost because the system will now absorb the value of the portion of interruptive military service credit that is free to the affected members.

Who Will Pay For These Costs?

This bill does not allow for an alternate funding method. The individual plans will subsidize the increase in liability that results from this bill in the usual way. The result may be an increase in future contribution rates for members and employers of the respective systems.

HOW WE VALUED THESE COSTS

Assumptions We Made

We valued two pieces separately – future purchases of service credit and refunds of past purchases of service credit.

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For the future purchases of service credit we assumed a certain number of members would purchase service in a given year. We adjusted this number based on which plan the member was in. For example, we assumed that more members in public safety plans would purchase interruptive military service than members in TRS.

Next, we assumed how much service they would buy. We based this assumption on past data. Lastly, based on the same data, we assumed when the service would be purchased. The time when the service is purchased is important because it costs a lot more if it is purchased at retirement rather than within five years of the interruptive military service.

For the refunds of past purchases we used data provided by the Department of Retirement Systems (DRS) to determine how many members will get refunds. We assumed that all military service would qualify for this proposal.

For more detail please see Appendix A.

How We Applied These Assumptions

We valued two pieces separately – future purchases of service credit and refunds of past purchases of service credit.

For the future purchases of service credit we gathered grouped data for the members of each system. We ran the grouped data through a spreadsheet which models the likelihood of purchasing service credit and the associated cost of the service credit purchase.

For the refunds of past purchases we used the data provided by DRS. We started with the amount of the purchase and added interest until the effective date of this proposal. We then discounted the amount back to June 30, 2007, to be consistent with the future purchases portion.

For more detail please see Appendix B.

Special Data Needed

DRS sent us a file containing all past purchases that have been made for interruptive military service credit. The file contained the member's system, payment date, death date (if applicable), months of service credit purchased, begin date of interruptive service, end date of interruptive service, and payment amount. We relied on all the information provided as complete and accurate.

Otherwise, we developed these costs using the same assets and data as disclosed in the 2007 Actuarial Valuation Report (AVR).

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ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of the systems by increasing the present value of future benefits payable under the systems 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)			
PERS 1	$14,061	$0.0	$14,061
PERS 2/3	20,634	0.5	20,635
PERS Total	**$34,695**	**$0.5**	**$34,696**
TRS 1	11,021	0.0	11,021
TRS 2/3	7,078	0.0	7,078
TRS Total	**$18,099**	**$0.0**	**$18,099**
SERS 2/3	**$2,698**	**$0.0**	**$2,698**
PSERS 2	**$225**	**$0.0**	**$225**
LEOFF 1	4,358	0.0	4,358
LEOFF 2	6,149	0.7	6,150
LEOFF Total	**$10,507**	**$0.7**	**$10,508**
WSPRS 1/2	**$856**	**$0.0**	**$856**
Unfunded Actuarial Accrued Liability			
(The Portion of the Plan 1 Liability that is Amortized to 2024)			
PERS 1	**$3,609**	**$0.0**	**$3,609**
TRS 1	**$2,288**	**$0.0**	**$2,288**
LEOFF 1	**($939)**	**$0.0**	**($939)**
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)			
PERS 1	$3,990	$0.0	$3,990
PERS 2/3	(2,470)	0.3	(2,469)
PERS Total	**$1,520**	**$0.3**	**$1,521**
TRS 1	2,552	0.0	2,552
TRS 2/3	(1,229)	0.0	(1,229)
TRS Total	**$1,323**	**$0.0**	**$1,323**
SERS 2/3	**($443)**	**$0.0**	**($443)**
PSERS 2	**($2)**	**$0.0**	**($2)**
LEOFF 1	(975)	0.0	(975)
LEOFF 2	(974)	0.4	(973)
LEOFF Total	**($1,949)**	**$0.4**	**($1,948)**
WSPRS 1/2	**($121)**	**$0.0**	**($121)**

Note: Totals may not agree due to rounding.

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How Contribution Rates Changed

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01 percent; therefore, the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate increase to measure the fiscal budget changes in future biennia.

Impact on Contribution Rates: (Effective 9/1/2009)

System/Plan	PERS	TRS	SERS	PSERS	LEOFF	WSPRS
Current Members						
Employee (Plan 2)	0.000%	0.000%	0.000%	0.001%	0.002%	0.000%
Employer:						
Normal Cost	0.000%	0.000%	0.000%	0.001%	0.001%	0.000%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.000%	0.000%	0.000%	0.001%	0.001%	0.000%
State					0.001%	
New Entrants*						
Employee (Plan 2)	0.000%	0.000%	0.000%	0.001%	0.002%	0.000%
Employer:						
Normal Cost	0.000%	0.000%	0.000%	0.001%	0.001%	0.000%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.000%	0.000%	0.000%	0.001%	0.001%	0.000%
State					0.001%	

**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.*

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How This Impacts Budgets And Employees

	Budget Impacts						
(Dollars in Millions)	**PERS**	**TRS**	**SERS**	**PSERS**	**LEOFF**	**WSPRS**	**Total**
2009-2011							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
Local Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Employer	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2011-2013							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.1
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.1**
Local Government	0.1	0.0	0.0	0.0	0.0	0.0	0.1
Total Employer	**$0.1**	**$0.0**	**$0.0**	**$0.0**	**$0.1**	**$0.0**	**$0.2**
Total Employee	**$0.1**	**$0.0**	**$0.0**	**$0.0**	**$0.1**	**$0.0**	**$0.2**
2009-2034							
General Fund	$0.3	$0.0	$0.0	$0.0	$0.7	$0.0	$1.1
Non-General Fund	0.5	0.0	0.0	0.0	0.0	0.0	0.5
Total State	**$0.8**	**$0.0**	**$0.0**	**$0.0**	**$0.7**	**$0.0**	**$1.6**
Local Government	1.2	0.0	0.0	0.0	1.1	0.0	2.4
Total Employer	**$2.0**	**$0.1**	**$0.1**	**$0.0**	**$1.9**	**$0.0**	**$4.0**
Total Employee	**$1.4**	**$0.0**	**$0.0**	**$0.0**	**$1.9**	**$0.0**	**$3.4**

Note: Totals may not agree due to rounding.

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

As with the costs developed in the actuarial valuation, the emerging costs of the systems 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 assumption:

- The number of members expected to purchase free interruptive military service credit in the future.

The number of members expected to purchase free interruptive military service credit in the future would have to increase dramatically for this proposal to impact contribution rates in the current biennium. The table below shows the multiple of how many more

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members would need to receive free military service credit before the rate impact would reach 0.005 percent for each system. For example, in LEOFF 2, the employee rate impact would reach 0.005 percent if three times as many members as expected receive free interruptive military service credit in the future.

System	Multiple
PERS	16
TRS	175
SERS	67
PSERS	8
LEOFF	3
WSPRS	35

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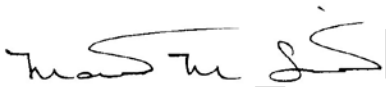
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost 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, assumptions, and data may also be reasonable, and might produce different results.
5. This draft fiscal note has been prepared for the Select Committee on Pension Policy and Law Enforcement Officers' and Fire Fighters' Retirement System Plan 2 Board.
6. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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APPENDIX A – ASSUMPTIONS WE MADE

We valued two pieces separately – future purchases of service credit and refunds of past purchases of service credit.

For the future purchases of service credit we assumed a certain number of members would purchase service in a given year. We used data from a DRS service credit report dated September 30, 2006, to estimate the number of members who would purchase future service. We used the average number of members from PERS over the 5-year period, which resulted in an assumption of 0.000214, or 1 in every 4,700 per year. We adjusted this number based on which plan the member was in. For example, we assumed that more members in public safety plans would purchase interruptive military service than members in TRS. More specifically, TRS and SERS were assumed to be at half of the assumed rate, whereas PSERS was assumed to be 1.5 times the assumed rate, and LEOFF and WSPRS were assumed to be at twice the assumed rate.

Next, we assumed how much service they would buy. We based this assumption on the same service credit report mentioned above. The average amount of service credit purchased was 10.6 months, which we used as the assumption in this pricing.

Lastly, based on the same data, we assumed when the service would be purchased. The time when the service is purchased is important because it costs a lot more if it is purchased at retirement rather than within five years of the interruptive military service. 209 of the 214 purchases were made within five years of the interruptive military service, while 5 of the 214 purchases were made at retirement. We used this data for our assumption of future purchases.

For simplicity, we assumed the population affected would be 100 percent male.

For the refunds of past purchases we used data provided by DRS to determine how many members will get refunds. We assumed that all military service would qualify for refunds.

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

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APPENDIX B – HOW WE APPLIED THESE ASSUMPTIONS

We valued two pieces separately – future purchases of service credit and refunds of past purchases of service credit.

For the future purchases of service credit we gathered average salary, average years of service, and total count for each age group of each system. We ran the grouped data through a spreadsheet which models the likelihood of purchasing service credit and the associated cost of the service credit purchase for each year of their future service. The likelihood of purchasing credit was based on the assumed rate of 0.000214, adjusted by system. The cost of the service credit purchase was the probability of purchasing the service within five years times the missed contributions times the assumed 10.6 months of service purchased plus the probability of purchasing the service at retirement times the actuarial value. This formula is shown below:

[209/214 * average of last 5 year's contribution rates * salary *10.6/12 months + 5/214 * Early Retirement Factor (ERF) * annuity factor * 0.02 * 10.6/12 months * final average salary]

Within the formula, future contribution rates must be assumed. Future contribution rates are consistent with contribution rates found on our website. Future contribution rates beyond 2013 are equal to the 2013 contribution rates.

The result for each grouping was multiplied by survivorship and discounted with 8 percent annual interest to determine the present value of future benefits. The sum of the present value of future benefits for each group was added up to determine the liability for each system.

For the refunds of past purchases we used the data provided by DRS. We started with the amount of the purchase and added 5.5 percent annual interest until the effective date of this proposal - September 1, 2009. We then discounted, at 8 percent, the amount back to June 30, 2007, to be consistent with the future purchases portion.

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

We used the Entry Age Normal Cost Method to determine the fiscal budget changes for future new entrants. We used the Aggregate actuarial funding method to determine the fiscal budget changes for current plan members.

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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.

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Office of
The State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

May 12, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

On behalf of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board (Board), I would like to thank you for the cooperative working relationship we have shared in the past and look forward to a similar partnership in the future.

I would like to bring several topics back to your attention as you begin preparation for the 2008 interim. It is our hope that the Select Committee on Pension Policy (SCPP) and the Board can work cooperatively on these issues to once again develop legislation. I have provided a brief summary of each topic for your reference:

Interruptive Military Service Credit
Working cooperatively last interim, the Board and the SCPP jointly endorsed a bill that would have eliminated a member's obligation to pay for interruptive military service credit if the member served during a period of war. The Board is once again interested in working cooperatively with the SCPP on the issue and feels the following additional question will need to be further explored:

- Should the benefit apply to all periods of interruptive military service which have not yet been recovered?

Inflationary Adjustment for $150,000 Death Benefit
The Board is interested in once again working with the SCPP to further study the effect of adding an inflationary adjustment to all the state retirement plans that provide the $150,000 death benefit. In addition to last year's study the Board feels following issues will need to be explored further:

- Should an adjustment in the lump sum amount be made to account for inflation since the creation of the benefit?

- Should both the lump sum adjustment and the addition of the inflationary adjustment be included in the bill?

Military Service Death Benefit

The Board and the SCPP jointly recommended legislation to the 2008 Legislature, which would have provided an unreduced annuity to qualifying survivors of members of all plans, who leave employment due to service in the National Guard or Reserves and die while in military service, during a period of war. The Board would like to continue our joint work to eliminate the "early retirement" actuarial reduction applied to the pensions of members who die while honorably serving our country.

Fish and Wildlife Enforcement Officer Service Credit Transfer

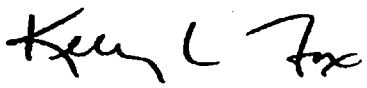
The Board and the SCPP also jointly recommended legislation last session that would have permitted Department of Fish and Wildlife Enforcement Officers to transfer service credit earned in the Public Employees' Retirement System (PERS) Plan 2 as enforcement officers into the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2. The Board feels the following issue may need to be further explored as well:

- Should PERS 3 members be included in the transfer group?

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

We would be happy to meet with you to discuss these topics at an upcoming SCPP or LEOFF Plan 2 Retirement Board meeting. Thank you for your consideration and we look forward to working with you.

Sincerely,



Kelly Fox, Chair

cc: Matt Smith, State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

June 30, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

At the recent meeting of the Select Committee on Pension Policy (SCPP) the chairman requested that the Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board (LEOFF 2 Board) provide a prioritized list of the suggested joint topics that the LEOFF 2 Board would like to work on cooperatively with the SCPP.

During the course of the most recent LEOFF 2 Board meeting we prioritized the suggested topics for cooperation in the following order:

1. **Fish and Wildlife Enforcement Officer Service Credit Transfer**
   Allow FWEO members to transfer their PERS Plan 2 service as enforcement officers to LEOFF Plan 2.

2. **Inflationary Adjustment for $150,000 Death Benefit**
   The $150,000 lump-sum death benefit paid to survivors of public employees who die in the line of duty is not adjusted for inflation.

3. **Interruptive Military Service Credit**
   Members whose public employment is interrupted by military service are required to pay member contributions in order to purchase service credit.

4. **Military Service Death Benefit**
   Beneficiaries of members who die while serving on active duty with the United States Military do not qualify for duty related death benefits.

5. **Purchase of Annuity**
   Members are limited in the amount of money they can convert to a defined benefit by the amount required to purchase 5 years of service.

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly Fox, Chair

cc: Matt Smith, State Actuary

Lower General Salary Increase Assumption

Description Of Issue

The issue is whether to lower the general salary increase assumption from 4.50 to 4.25 percent. The general salary increase assumption is an economic assumption that is used for the systematic actuarial funding of the Washington State retirement systems.

Economic assumptions are specified in the actuarial funding chapter of state law. See RCW 41.45.035. The funding chapter also provides that the Pension Funding Council (PFC) and ultimately, the Legislature, can modify these assumptions. As part of the contribution rate-setting process, the SCPP makes recommendations to the PFC regarding any changes to the assumptions based on changes in actuarial experience.

The State Actuary completed a six-year experience study in 2008, and recommended that the assumption be lowered to 4.25 percent.

Policy Highlights

- Matching assumptions to experience prevents the accumulation of excess gains and losses.
- The proposed legislation would align the statute with the recommendation of the State Actuary and the decision of the PFC.

Committee Activity

Staff briefed the Committee on this issue in July and the SCPP recommended to the PFC that it lower the general salary increase assumption from 4.50 to 4.25 percent. The PFC agreed and adopted this change on July 22, 2008. The SCPP held a public hearing in September and took executive action to recommend to the Legislature that the general salary increase assumption be lowered.

Recommendation To 2009 Legislature

Lower the statutory general salary increase assumption from 4.50 percent to 4.25 percent for all plans except the Law Enforcement Officers' and Fire Fighters' Retirement System Plan 2—consistent with the actions of the Pension Funding Council.

Staff Contact

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0119.2/09 2nd draft

ATTY/TYPIST: LL:seg

BRIEF DESCRIPTION: Lowering the general salary increase assumption for the actuarial funding of certain public retirement systems.

AN ACT Relating to lowering the general salary increase assumption from 4.5 percent to 4.25 percent for the actuarial funding of the public employees' retirement system, the teachers' retirement system, plan 1 of the law enforcement officers' and firefighters' retirement system, the school employees' retirement system, the public safety employees' retirement system, and the Washington state patrol retirement system; amending RCW 41.45.035; providing an effective date; and declaring an emergency.

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

Sec. 1. RCW 41.45.035 and 2004 c 93 s 2 are each amended to read as follows:

(1) Beginning July 1, 2001, the following long-term economic assumptions shall be used by the state actuary for the purposes of RCW 41.45.030:

(a) The growth in inflation assumption shall be 3.5 percent;

(b) The growth in salaries assumption, exclusive of merit or longevity increases, shall be 4.5 percent;

(c) The investment rate of return assumption shall be 8 percent; and

(d) The growth in system membership assumption shall be 1.25 percent for the public employees' retirement system, the school employees' retirement system, and the law enforcement officers' and firefighters' retirement system. The assumption shall be .90 percent for the teachers' retirement system.

(2) Beginning July 1, 2009, the following long-term economic assumption for growth in salaries, exclusive of merit or longevity increases, shall be used by the state actuary for the purposes of RCW 41.45.030: 4.25 percent for the public employees' retirement system, the teachers' retirement system, plan 1 of the law enforcement officers' and firefighters' retirement system, the school employees' retirement system, the public safety employees' retirement system, and the Washington state patrol retirement system.

(3)(a) Beginning with actuarial studies done after July 1, 2003, changes to plan asset values that vary from the long-term investment rate of return assumption shall be recognized in the actuarial value of assets over a period that varies up to eight years depending on the magnitude of the deviation of each year's investment rate of return relative to the long-term rate of return assumption. Beginning with actuarial studies performed after July 1, 2004, the actuarial value of assets shall not be greater than one hundred thirty percent of the market value of assets as of the valuation date or less than seventy percent of the market value of assets as of the valuation date. Beginning April 1, 2004, the council, by affirmative vote of four councilmembers, may adopt changes to this asset value smoothing technique. Any changes adopted by the council shall be subject to revision by the legislature.

(b) The state actuary shall periodically review the appropriateness of the asset smoothing method in this section and recommend changes to the legislature as necessary.

NEW SECTION. **Sec. 2.** This act is necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and takes effect July 1, 2009.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**01/05/09**	**Z-0119.2 / Z-0444.1**

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 throughout the 2008 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 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 changes the general salary increase assumption currently in statute to be consistent with the assumption change adopted by the Pension Funding Council (PFC) on July 22, 2008. The PFC lowered the general salary increase assumption for the actuarial funding of the state retirement systems from 4.5 percent to 4.25 percent for all state-administered plans and systems identified in Chapter 41.45 RCW except the Law Enforcement Officers' and Firefighters' (LEOFF) Plan 2.

There is no fiscal impact resulting from this proposal.

WHAT IS THE PROPOSED CHANGE?

Summary of Change

This proposal impacts the following systems and plans:

- Public Employees' Retirement System (PERS): Plans 1, 2, and 3
- Teachers' Retirement System (TRS): Plans 1, 2, and 3
- School Employees' Retirement System (SERS): Plans 2 and 3 [Note: there is no Plan 1 in SERS.]

DRAFT

- Public Safety Employees' Retirement System (PSERS) [Note: there is only one plan in PSERS.]
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF): Plan 1 [Note: LEOFF Plan 2 is excluded from this proposal.]
- Washington State Patrol Retirement System (WSPRS), "Plans 1 and 2" [Note: "Plan 2" covers commissioned employees who first became members of the system on or after January 1, 2003.]

The proposal changes the general salary increase assumption for the actuarial funding of the plans and systems listed above to be consistent with the assumption change adopted by the PFC. The PFC lowered the general salary increase assumption from 4.5 percent to 4.25 percent. This assumption is referred to in state statute as the "growth in salaries assumption, exclusive of merit or longevity increases," and is found in RCW 41.45.035(1)(b).

Assumed Effective Date: July 1, 2009

What Is The Current Situation?

Currently the actuarial funding chapter of state law specifies the general salary increase assumption to be used for the actuarial funding of the plans and systems identified within the chapter. The assumption in statute is 4.5 percent. On July 22, 2008, the Pension Funding Council adopted a change in this economic assumption. The assumption was lowered to 4.25 percent in response to a recommendation from the State Actuary based on the results of the 2008 Experience Study. The Board of Trustees for LEOFF Plan 2 also received this recommendation from the State Actuary and did not adopt the assumption change.

This proposal would make the statutory provision in the actuarial funding chapter consistent with the assumption change already adopted by the Pension Funding Council. Also, the proposal is crafted to retain the 4.5 percent assumption already in place for LEOFF Plan 2.

[Note: RCW 41.45.030(3) authorizes the Council to modify the long-term economic assumptions for those retirement systems identified in the actuarial funding chapter. Economic assumptions for LEOFF Plan 2 are set by the LEOFF Plan 2 Board of Trustees pursuant to RCW 41.26.720(1)(a).]

ACTUARIAL RESULTS

This proposal simply aligns the current assumptions which are set in statute with the latest actions of the PFC. The PFC also adopted contribution rates that reflect this assumption change and the fiscal impact is included in the current law budget. As a result, there is no additional impact on the actuarial liabilities or contribution rates for this proposal.

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ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
2. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

DRAFT

Select Committee on Pension Policy

P.O. Box 40914
Olympia, WA 98504-0914
actuary.state@leg.wa.gov

July 15, 2008

TO: **Pension Funding Council Members**
Senator Margarita Prentice, Chair Ways and Means Committee
Senator Joseph Zarelli, Ranking Minority Member Ways and Means Committee
Representative Helen Sommers, Chair Appropriations Committee
Representative Gary Alexander, Ranking Minority Member, Appropriations Committee
Ms. Sandra Matheson, Director Department of Retirement Systems
Mr. Victor Moore, Director Office of Financial Management

FROM: *Senator Mark Schoesler*, Chair Select Committee on Pension Policy
Representative Steve Conway, Vice-Chair Select Committee on Pension Policy

SUBJECT: **SELECT COMMITTEE ON PENSION POLICY RECOMMENDATION ON 2009-11 PENSION CONTRIBUTION RATES**

The Select Committee on Pension Policy recommends that the Pension Funding Council adopt the State Actuary's recommended contribution rates for the 2009-2011 biennium with projected mortality improvements, using the general salary increase assumption of 4.25 percent. The SCPP will recommend legislation for 2009 that reduces the salary growth assumption in RCW 41.45.035(b) from 4.5 to 4.25 percent.

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***Elaine M. Banks**
TRS Retirees

Representative Barbara Bailey

Lois Clement
PERS Retirees

***Representative Steve Conway, Vice Chair**

Representative Larry Crouse

Charles E. Cuzzetto
TRS and SERS Employers

Randy Davis
TRS Actives

Representative Bill Fromhold

Senator Steve Hobbs

Senator Janea Holmquist

Robert Keller
PERS Actives

***Sandra J. Matheson,** Director
Department of Retirement Systems

***Corky Mattingly**
PERS Employers

Doug Miller
PERS Employers

Victor Moore, Director
Office of Financial Management

Senator Ed Murray

Glenn Olson
PERS Employers

***Senator Mark Schoesler, Chair**

J. Pat Thompson
PERS Actives

***David Westberg**
SERS Actives

Executive Committee

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Military Death Benefits

Description Of Issue

The Public Employees' Retirement System (PERS) Plan 2 provides enhanced survivor benefits for members who are called to active duty military service and die while performing that service. The other Washington State retirement plans do not.

Enhanced PERS Plan 2 benefits were enacted in 2007 and provide a withdrawal of 200 percent of a member's account balance if the member died while serving in the Iraq or Afghanistan conflict after January of 2007.

Policy Highlights

- There is inconsistent pension treatment of survivors of members who die while actively serving in the armed forces.
- The federal government provides lump sum payouts to survivors of armed forces members who die while serving.
- Three comparative systems provide enhanced survivor benefits when the member dies while actively serving in the armed forces.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 session to provide an unreduced survivor annuity for members who die in certain military service (HB 3007/SB 6646). The bill did not pass the Legislature, but did pass the House.

The Committee held a public hearing and took executive action on this issue in July of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 session.

Recommendation To 2009 Legislature

Provide an unreduced joint and survivor annuity to the survivor of a member who dies in war while serving in the National Guard or Military Reserves.

Staff Contact

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Military Death Benefits

In Brief

ISSUE

The issue before the SCPP is whether to provide additional benefits to survivors of members who die while serving on active duty with the United States' military.

MEMBER IMPACT

This could impact survivors of members in each system and plan who die while on military duty.

The Federal government also provides survivor benefits for spouses and families of members who die while on military service.

Dave Nelsen
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Current Situation

Death benefits are provided to survivors of deceased members based upon system and plan-specific eligibility and benefit amounts. Prior to the passage of SHB 1266 in the 2007 Legislative session, no distinction was made in the survivor eligibility or benefit amount in any system or plan between members who died while no longer working for a public employer for any reason and members who died while fulfilling interruptive military service obligations.

SHB 1266 authorized a survivor of a Public Employees' Retirement System (PERS) Plan 2 member who was eligible to retire or had at least ten years of service, and who is killed in the current Iraq or Afghanistan conflict, a choice between 200 percent of the member's account balance or a monthly annuity reduced for each year of the member's age at death prior to age 65. The survivors of members who separate from employment for any other reason do not get the 200 percent option. They receive a choice between 100 percent of the account balance and the reduced survivor annuity.

Spouses and/or qualifying dependants are also eligible for benefits from the federal government if their spouse dies while on military duty. They receive a one time tax–free $100,000 payment and a monthly stipend of $1,067, increased by Consumer Price Index (CPI) based adjustments, with an additional $265 per month provided for each dependant. Additionally, military employees are automatically enrolled in group life insurance in the amount of $250,000. Employees can opt out, reduce or increase this coverage up to $400,000. The cost for the full amount is $29 monthly.

Policy Analysis

The primary policy in question is whether survivors of members who die while serving on military duty should receive additional pension benefits not available to survivors of members who left employment for other reasons.

The chart below outlines some general arguments for or against providing additional or special benefits to military personnel.

No Additional Special Benefits	Additional Special Benefits
Members serve voluntarily; no draft requires them to leave employment	Encourage military service; help avoid need for a draft
Members already receive adequate federal compensation and benefits for military service	Support ability to recruit more military personnel into state service and more state personnel into military service
Other members and employers would not have to absorb extra costs for these members	Support view that all WA citizens benefit, directly or indirectly, from military service rendered by public employees
More favorable service credit treatment is already given to these members via federal law (no interest, 5 years to repay)	Recognize that members who serve in conflicts are at higher risk for injury or death; pension plans typically offer extra support for high risk occupations that serve the public at large
Military service is unrelated to the service rewarded by state pension plans	Supplement federal benefits, which may not be viewed as adequate

Should survivor benefits of members who die while on military service differ from survivor benefits of members who die in other situations, such as in the line of duty?

If it is desirable to provide additional pension survivor benefits, the next question is: What additional survivor benefits? State pension benefits typically distinguish between duty-related death and non-duty related death.

Survivors whose spouses die from duty-related causes receive the most benefit from the state pensions. These spouses or dependants may be eligible for both a lump sum ($150,000 death benefit) and annuity (unreduced survivor annuity based upon salary and service credit). Survivors whose spouses die from non-duty related causes, whether as active employees or as separated members, typically only receive either a refund of contributions or a survivor annuity that is actuarially reduced for each year prior to the normal retirement age.

To provide enhanced survivor benefits, something greater than a refund of member contributions or an actuarially reduced annuity would need to be provided. Examining the benefits provided by the federal government and attempting to provide a benefit from the pension system that supplements the total benefits received may be a logical approach. In looking at the federal death benefits provided, given the likelihood of large lump sum payments ($100,000 guaranteed with up to $400,000 additional in

insurance) but limited monthly annuity amounts for income replacement ($1,067 per month with additional amounts for dependants), perhaps enhanced annuity payments from the state pensions would be most valuable.

Should the eligibility for and calculation of survivor benefits of members be standard across all systems and plans, or standard with other survivor benefits within the systems and plans?

One question that arises if providing an enhanced benefit is whether the eligibility and calculation method should be standard across systems and plans, or standardized with other survivor benefits within the system and plans. For example, Plan 1 of the Law Enforcement Officers' and Fire Fighters' (LEOFF) retirement system has different eligibility for survivor benefits based upon whether the member is active or inactive, while the Plans 2/3 have different eligibility based upon years of service but don't distinguish between active and inactive. As for the benefit calculations, the Plan 1 systems have different methods of providing post-retirement adjustments or cost-of-living-adjustments (COLA) than the Plans 2/3 systems.

If the eligibility and calculation methodology are standardized across plans, it would ensure two survivors would receive similar benefits regardless of plan membership. However, this may cause concerns with non-military death related survivors if their eligibility or calculation methodology is not as generous. Conversely, the other option would be to standardize the benefit according to the current plan methods. This would provide consistent benefits within each plan, but may lead to similarly situated survivors receiving different benefits. Currently, for survivor benefits within the state retirement systems, the eligibility for and the benefit provided is generally based upon plan specific methodology, regardless of the reason for the member's death.

What type of uniformed service should qualify for enhanced survivor benefits?

The final question faced when providing enhanced benefits for military service is what type of military or uniformed service. If the Committee chooses to provide enhanced military survivor benefits, should the benefits be provided for deaths during:

- Participation in all military service? Such as in times of conflict, active duty training, and peace-time.
- Service only in current conflicts?
- Service only in current and future conflicts?

- Service only in conflicts specifically identified for this benefit?

The federal government requires the same reemployment rights whether the person served in a conflict, a period of war, or in a time of peace. Within the state pension systems, free interruptive service credit is granted to members of PERS Plan 1, LEOFF Plan 1, and the Washington State Patrol Retirement System (WSPRS) Plan 1, but only if the member served during a period of war.

Other States*

What type of uniformed service should qualify for enhanced survivor benefits?

Research into our comparative states indicated that only three states provide enhanced survivor benefits to spouses of members who die while serving in the military; Idaho, California, and Iowa. Idaho provides a choice of a refund equaling twice the member's contributions or a reduced survivor annuity. California and Iowa provide more generous survivor benefits when the member dies while an active employee, and in both those states, members who die while serving in the military are treated as active employees. Both of these states also provide enhanced benefits for "public safety" members who die in the line of duty, but survivors of members who die while serving in the military do not qualify for this benefit in either state.

** Research into practices by other states was performed in December of 2007.*

Prior Executive Committee Action

In 2007, the Executive Committee asked OSA to price two general options and bring the information back for further consideration:

- Expand the 200 percent option currently in PERS Plan 2 to all systems and plans.
- Provide an option for an unreduced survivor annuity.

After discussing the possible alternatives, the Executive Committee recommended the following proposal be presented to the Full Committee and draft legislation be prepared:

Survivors of a member who dies while serving honorably in the uniformed services will have the same eligibility and survivor benefit options within each system and plan as the survivor of a member who dies in the line of duty. In general, this would provide an unreduced survivor annuity to those who qualify.

Possible Options

A first option is to endorse the Executive Committee proposal. This proposal provides an enhanced benefit in the form of an unreduced survivor annuity, but does not provide lesser eligibility standards or a greater benefit than what currently exists within the systems and plans, maintaining equity with other survivor benefits, such as line of duty deaths. This proposal is also the most expansive possible regarding the nature of the uniformed services in that it does not distinguish between periods of war or peace.

Other options to the Committee include the following:

- Provide a lump sum amount in lieu of or addition to the unreduced survivor annuity.
- Alter the pension-based eligibility standards for the benefit.
- Limit the eligibility for the benefit based upon the type of uniformed service provided, such as only during a time of war.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 Session to provide an unreduced survivor annuity for members who die in certain military service (HB 3007/SB 6646). The bill did not pass the Legislature, but did pass the House.

The Committee held a public hearing and took executive action on this issue in July 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 Session.

Stakeholder Input

Correspondence attached from:

Kelly Fox, Chair, LEOFF Plan 2 Board, 5/12/2008 and 6/30/2008.

Correspondence on file from:

John Kvamme, WASA & AWSP consultant, 5/15/2008.

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

Provide an unreduced joint and survivor annuity to the survivor of a member who dies in war while serving in the National Guard or Military Reserves. Recommended July 15, 2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0072.1/09).

Draft Fiscal Note

Attached.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0072.1/09

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Addressing the survivor benefits of employees who die while honorably serving in the national guard or military reserves during a period of war.

AN ACT Relating to the survivor benefits of employees who die while honorably serving in the national guard or military reserves during a period of war; and amending RCW 41.26.160, 41.26.510, 43.43.270, 43.43.295, 41.32.520, 41.32.805, 41.32.895, 41.35.460, 41.35.710, 41.37.250, 41.40.270, 41.40.700, and 41.40.835.

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

Sec. 1. RCW 41.26.160 and 2005 c 62 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, <u>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,</u> the surviving spouse shall become entitled, subject to RCW 41.26.162, to receive a monthly allowance equal to fifty percent of the final average salary at the date of death if active, 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), 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, <u>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,</u> 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 <u>or while honorably serving in the national guard or military reserves during a period of war as defined in RCW 41.04.005</u>, then if he or she was married at the time he or she was disabled <u>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</u>, 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), 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), 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 41.26.510 and 2006 c 345 s 1 are each amended to read as follows:

(1) Except as provided in RCW 11.07.010, if a member or a vested member who has not completed at least ten years of service dies, the amount of the accumulated contributions standing to such member's credit in the retirement system at the time of such member's death, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's estate, or such person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's accumulated contributions standing to such member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670,

shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, the surviving spouse or eligible child or children shall elect to receive either:

(a) A retirement allowance computed as provided for in RCW 41.26.430, actuarially reduced by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 and actuarially adjusted to reflect a joint and one hundred percent survivor option under RCW 41.26.460 and if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.26.430; if a surviving spouse who is receiving a retirement allowance dies leaving a child or children of the member under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority; if there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance share and share alike calculated as herein provided making the assumption that the ages of the spouse and member were equal at the time of the member's death; or

(b)(i) The member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670; or

(ii) If the member dies on or after July 25, 1993, one hundred fifty percent of the member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670. Any accumulated contributions attributable to restorations made under RCW 41.50.165(2) shall be refunded at one hundred percent.

(3) If a member who is eligible for retirement or a member who has completed at least ten years of service dies after October 1, 1977, and is not survived by a spouse or an eligible child, then the accumulated contributions standing to the member's credit, less any amount

identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid:

(a) To an estate, a person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there is no such designated person or persons still living at the time of the member's death, then to the member's legal representatives.

(4) The retirement allowance of a member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or the retirement allowance 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,</u> is not subject to an actuarial reduction. The member's retirement allowance is computed under RCW 41.26.420.

(5) The retirement allowance paid to the spouse and dependent children of a member who is killed in the course of employment, as set forth in RCW 41.05.011(14), shall include reimbursement for any payments of premium rates to the Washington state health care authority pursuant to RCW 41.05.080.

Sec. 3. RCW 43.43.270 and 2006 c 94 s 1 are each amended to read as follows:

For members commissioned prior to January 1, 2003:

(1) The normal form of retirement allowance shall be an allowance which shall continue as long as the member lives.

(2) If a member should die while in service<u>, or a member leaves the employ of the 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,</u> the member's lawful spouse shall be paid an allowance which shall be equal to fifty percent of the average final salary of the member. If the member should die after retirement the member's lawful spouse shall be paid an allowance which shall be equal to the retirement allowance then payable to the member or fifty percent of the final average salary used in computing the member's retirement allowance, whichever is less.

The allowance paid to the lawful spouse shall continue as long as the spouse lives: PROVIDED, That if a surviving spouse who is receiving benefits under this subsection marries another member of this retirement system who subsequently predeceases such spouse, the spouse shall then be entitled to receive the higher of the two survivors' allowances for which eligibility requirements were met, but a surviving spouse shall not receive more than one survivor's allowance from this system at the same time under this subsection. To be eligible for an allowance the lawful surviving spouse of a retired member shall have been married to the member prior to the member's retirement and continuously thereafter until the date of the member's death or shall have been married to the retired member at least two years prior to the member's death. The allowance paid to the lawful spouse may be divided with an ex spouse of the member by a dissolution order as defined in RCW 41.50.500(3) incident to a divorce occurring after July 1, 2002. The dissolution order must specifically divide both the member's benefit and any spousal survivor benefit, and must fully comply with RCW 41.50.670 and 41.50.700.

(3) If a member should die, either while in service or after retirement, the member's surviving unmarried children under the age of eighteen years shall be provided for in the following manner:

(a) If there is a surviving spouse, each child shall be entitled to a benefit equal to five percent of the final average salary of the member or retired member. The combined benefits to the surviving spouse and all children shall not exceed sixty percent of the final average salary of the member or retired member; and

(b) If there is no surviving spouse or the spouse should die, the child or children shall be entitled to a benefit equal to thirty percent of the final average salary of the member or retired member for one child and an additional ten percent for each additional child. The combined benefits to the children under this subsection shall not exceed sixty percent of the final average salary of the member or retired member. Payments under this subsection shall be prorated equally among the children, if more than one.

(4) If a member should die in the line of duty while employed by the Washington state patrol, <u>or a member leaves the employ of the employer due to service in the national guard or military reserves and dies while honorably serving in the national guard or military reserves</u>

during a period of war as defined in RCW 41.04.005, the member's surviving children under the age of twenty years and eleven months if attending any high school, college, university, or vocational or other educational institution accredited or approved by the state of Washington shall be provided for in the following manner:

(a) If there is a surviving spouse, each child shall be entitled to a benefit equal to five percent of the final average salary of the member. The combined benefits to the surviving spouse and all children shall not exceed sixty percent of the final average salary of the member;

(b) If there is no surviving spouse or the spouse should die, the unmarried child or children shall be entitled to receive a benefit equal to thirty percent of the final average salary of the member or retired member for one child and an additional ten percent for each additional child. The combined benefits to the children under this subsection shall not exceed sixty percent of the final average salary. Payments under this subsection shall be prorated equally among the children, if more than one; and

(c) If a beneficiary under this subsection reaches the age of twenty-one years during the middle of a term of enrollment the benefit shall continue until the end of that term.

(5)(a) The provisions of this section shall apply to members who have been retired on disability as provided in RCW 43.43.040 if the officer was a member of the Washington state patrol retirement system at the time of such disability retirement.

(b) For the purposes of this subsection, average final salary as used in subsection (2) of this section means:

(i) For members commissioned prior to January 1, 2003, the average monthly salary received by active members of the patrol of the rank at which the member became disabled, during the two years prior to the death of the disabled member; and

(ii) For members commissioned on or after January 1, 2003, the average monthly salary received by active members of the patrol of the rank at which the member became disabled, during the five years prior to the death of the disabled member.

(c) The changes to the definitions of average final salary for the survivors of disabled members in this subsection shall apply retroactively. The department shall correct future payments to

eligible survivors of members disabled prior to June 7, 2006, and, as soon as administratively practicable, pay each survivor a lump sum payment reflecting the difference, as determined by the director, between the survivor benefits previously received by the member, and those the member would have received under the definitions of average final salary created in chapter 94, Laws of 2006.

Sec. 4. RCW 43.43.295 and 2004 c 171 s 1 are each amended to read as follows:

(1) For members commissioned on or after January 1, 2003, except as provided in RCW 11.07.010, if a member or a vested member who has not completed at least ten years of service dies, the amount of the accumulated contributions standing to such member's credit in the retirement system at the time of such member's death, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's estate, or such person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's accumulated contributions standing to such member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, the surviving spouse or eligible child or children shall elect to receive either:

(a) A retirement allowance computed as provided for in RCW 43.43.260, actuarially reduced, except under subsection (4) of this section, by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 and actuarially adjusted to reflect a joint and one hundred percent survivor option under RCW 43.43.278 and if the member was not eligible for normal retirement at the date of death a further reduction from age fifty-five or when the

member could have attained twenty-five years of service, whichever is less; if a surviving spouse who is receiving a retirement allowance dies leaving a child or children of the member under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority; if there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance share and share alike calculated under this section making the assumption that the ages of the spouse and member were equal at the time of the member's death; or

(b)(i) The member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670; or

(ii) If the member dies, one hundred fifty percent of the member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670. Any accumulated contributions attributable to restorations made under RCW 41.50.165(2) shall be refunded at one hundred percent.

(3) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, and is not survived by a spouse or an eligible child, then the accumulated contributions standing to the member's credit, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid:

(a) To an estate, a person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there is no such designated person or persons still living at the time of the member's death, then to the member's legal representatives.

(4) The retirement allowance of a member who is killed in the course of employment, as determined by the director of the department of labor and industries<u>, or the retirement allowance of a member who has left the employ of an employer due to service in the national guard</u>

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, is not subject to an actuarial reduction.

Sec. 5. RCW 41.32.520 and 2003 c 155 s 1 are each amended to read as follows:

(1) Except as specified in subsection (3) of this section, upon receipt of proper proofs of death of any member before retirement or before the first installment of his or her retirement allowance shall become due his or her accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, and/or other benefits payable upon his or her death shall be paid to his or her estate or to such persons, trust, or organization as he or she shall have nominated by written designation duly executed and filed with the department. If a member fails to file a new beneficiary designation subsequent to marriage, divorce, or reestablishment of membership following termination by withdrawal, lapsation, or retirement, payment of his or her accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, and/or other benefits upon death before retirement shall be made to the surviving spouse, if any; otherwise, to his or her estate. If a member had established ten or more years of Washington membership service credit or was eligible for retirement, the beneficiary or the surviving spouse if otherwise eligible may elect, in lieu of a cash refund of the member's accumulated contributions, the following survivor benefit plan actuarially reduced, except under subsection (4) of this section, by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670:

(a) A widow or widower, without a child or children under eighteen years of age, may elect a monthly payment of fifty dollars to become effective at age fifty, provided the member had fifteen or more years of Washington membership service credit. A benefit paid under this subsection (1)(a) shall terminate at the marriage of the beneficiary.

(b) The beneficiary, if a surviving spouse or a dependent (as that

term is used in computing the dependent exemption for federal internal revenue purposes) may elect to receive a joint and one hundred percent retirement allowance under RCW 41.32.530.

(i) In the case of a dependent child the allowance shall continue until attainment of majority or so long as the department judges that the circumstances which created his or her dependent status continue to exist. In any case, if at the time dependent status ceases, an amount equal to the amount of accumulated contributions of the deceased member has not been paid to the beneficiary, the remainder shall then be paid in a lump sum to the beneficiary.

(ii) If at the time of death, the member was not then qualified for a service retirement allowance, the benefit shall be based upon the actuarial equivalent of the sum necessary to pay the accrued regular retirement allowance commencing when the deceased member would have first qualified for a service retirement allowance.

(2) If no qualified beneficiary survives a member, at his or her death his or her accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to his or her estate, or his or her dependents may qualify for survivor benefits under benefit plan (1)(b) in lieu of a cash refund of the members accumulated contributions in the following order: Widow or widower, guardian of a dependent child or children under age eighteen, or dependent parent or parents.

(3) If a member dies within sixty days following application for disability retirement under RCW 41.32.550, the beneficiary named in the application may elect to receive the benefit provided by:

(a) This section; or

(b) RCW 41.32.550, according to the option chosen under RCW 41.32.530 in the disability application.

(4) The retirement allowance of a member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or the retirement allowance 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,</u> is not subject to an actuarial reduction. The member's retirement allowance is computed under RCW 41.32.480.

Sec. 6. RCW 41.32.805 and 2003 c 155 s 2 are each amended to read as follows:

(1) Except as provided in RCW 11.07.010, if a member or a vested member who has not completed at least ten years of service dies, the amount of the accumulated contributions standing to such member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, at the time of such member's death shall be paid to the member's estate, or such person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's accumulated contributions standing to such member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, the surviving spouse or eligible children shall elect to receive either:

(a) A retirement allowance computed as provided for in RCW 41.32.765, actuarially reduced by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 and actuarially adjusted to reflect a joint and one hundred percent survivor option under RCW 41.32.785 and, except under subsection (4) of this section, if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.32.765; if a surviving spouse who is receiving a retirement allowance dies leaving a child or children of the member under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority; if there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance share and

share alike calculated as herein provided making the assumption that the ages of the spouse and member were equal at the time of the member's death; or

(b) The member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670.

(3) If a member who is eligible for retirement or a member who has completed at least ten years of service dies after October 1, 1977, and is not survived by a spouse or an eligible child, then the accumulated contributions standing to the member's credit, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid:

(a) To an estate, a person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there is no such designated person or persons still living at the time of the member's death, then to the member's legal representatives.

(4) A member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or 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,</u> is not subject to an actuarial reduction under RCW 41.32.765. The member's retirement allowance is computed under RCW 41.32.760.

Sec. 7. RCW 41.32.895 and 2003 c 155 s 3 are each amended to read as follows:

(1) If a member dies prior to retirement, the surviving spouse or eligible child or children shall receive a retirement allowance computed as provided in RCW 41.32.851 actuarially reduced to reflect a joint and one hundred percent survivor option and, except under subsection (2) of this section, if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.32.875.

If the surviving spouse who is receiving the retirement allowance dies leaving a child or children under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority.

If there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance, share and share alike. The allowance shall be calculated with the assumption that the age of the spouse and member were equal at the time of the member's death.

(2) A member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or 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,</u> is not subject to an actuarial reduction under RCW 41.32.875. The member's retirement allowance is computed under RCW 41.32.840.

Sec. 8. RCW 41.35.460 and 2003 c 155 s 4 are each amended to read as follows:

(1) Except as provided in RCW 11.07.010, if a member or a vested member who has not completed at least ten years of service dies, the amount of the accumulated contributions standing to such member's credit in the retirement system at the time of such member's death, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's estate, or such person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's accumulated contributions standing to such member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's surviving spouse as if in fact such

spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, the surviving spouse or eligible child or children shall elect to receive either:

(a) A retirement allowance computed as provided for in RCW 41.35.420, actuarially reduced by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 and actuarially adjusted to reflect a joint and one hundred percent survivor option under RCW 41.35.220 and, except under subsection (4) of this section, if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.35.420; if a surviving spouse who is receiving a retirement allowance dies leaving a child or children of the member under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority; if there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance, share and share alike, calculated as herein provided making the assumption that the ages of the spouse and member were equal at the time of the member's death; or

(b) The member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670.

(3) If a member who is eligible for retirement or a member who has completed at least ten years of service dies and is not survived by a spouse or an eligible child, then the accumulated contributions standing to the member's credit, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid:

(a) To a person or persons, estate, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there is no such designated person or persons still living

at the time of the member's death, then to the member's legal representatives.

(4) A member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or 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,</u> is not subject to an actuarial reduction under RCW 41.35.420. The member's retirement allowance is computed under RCW 41.35.400.

Sec. 9. RCW 41.35.710 and 2003 c 155 s 5 are each amended to read as follows:

(1) If a member dies prior to retirement, the surviving spouse or eligible child or children shall receive a retirement allowance computed as provided in RCW 41.35.620 actuarially reduced to reflect a joint and one hundred percent survivor option and, except under subsection (2) of this section, if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.35.680.

If the surviving spouse who is receiving the retirement allowance dies leaving a child or children under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority.

If there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance, share and share alike. The allowance shall be calculated with the assumption that the age of the spouse and member were equal at the time of the member's death.

(2) A member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or 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,</u> is not subject to an actuarial

reduction under RCW 41.35.680. The member's retirement allowance is computed under RCW 41.35.620.

Sec. 10. RCW 41.37.250 and 2005 c 327 s 7 are each amended to read as follows:

(1) Except as provided in RCW 11.07.010, if a member or a vested member who has not completed at least ten years of service dies, the amount of the accumulated contributions standing to that member's credit in the retirement system at the time of the member's death, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's estate, or the person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department. If there is no designated person or persons still living at the time of the member's death, the member's accumulated contributions standing to the member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's surviving spouse as if in fact that spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, the surviving spouse or eligible child or children shall elect to receive either:

(a) A retirement allowance computed as provided for in RCW 41.37.210, actuarially reduced by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 and actuarially adjusted to reflect a joint and one hundred percent survivor option under RCW 41.37.170 and, except under subsection (4) of this section, if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.37.210; if a surviving spouse who is receiving a retirement allowance dies leaving a child or children of the member under the age of majority, then the child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until the child or children reach the age of majority;

if there is no surviving spouse eligible to receive an allowance at the time of the member's death, the member's child or children under the age of majority shall receive an allowance, share and share alike, calculated under this section making the assumption that the ages of the spouse and member were equal at the time of the member's death; or

(b) The member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670.

(3) If a member who is eligible for retirement or a member who has completed at least ten years of service dies and is not survived by a spouse or an eligible child, then the accumulated contributions standing to the member's credit, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid:

(a) To a person or persons, estate, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there is no designated person or persons still living at the time of the member's death, then to the member's legal representatives.

(4) A member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or 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,</u> is not subject to reduction under RCW 41.37.210. The member's retirement allowance is computed under RCW 41.37.190.

Sec. 11. RCW 41.40.270 and 2003 c 155 s 6 are each amended to read as follows:

(1) Except as specified in subsection (4) of this section, should a member die before the date of retirement the amount of the accumulated contributions standing to the member's credit in the employees' savings fund, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, at the time of death:

(a) Shall be paid to the member's estate, or such person or

persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there be no such designated person or persons still living at the time of the member's death, or if a member fails to file a new beneficiary designation subsequent to marriage, remarriage, dissolution of marriage, divorce, or reestablishment of membership following termination by withdrawal or retirement, such accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the surviving spouse as if in fact such spouse had been nominated by written designation as aforesaid, or if there be no such surviving spouse, then to the member's legal representatives.

(2) Upon the death in service, or while on authorized leave of absence for a period not to exceed one hundred and twenty days from the date of payroll separation, of any member who is qualified but has not applied for a service retirement allowance or has completed ten years of service at the time of death, the designated beneficiary, or the surviving spouse as provided in subsection (1) of this section, may elect to waive the payment provided by subsection (1) of this section. Upon such an election, a joint and one hundred percent survivor option under RCW 41.40.188, calculated under the retirement allowance described in RCW 41.40.185 or 41.40.190, whichever is greater, actuarially reduced, except under subsection (5) of this section, by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 shall automatically be given effect as if selected for the benefit of the designated beneficiary. If the member is not then qualified for a service retirement allowance, such benefit shall be based upon the actuarial equivalent of the sum necessary to pay the accrued regular retirement allowance commencing when the deceased member would have first qualified for a service retirement allowance.

(3) Subsection (1) of this section, unless elected, shall not apply to any member who has applied for service retirement in RCW 41.40.180, as now or hereafter amended, and thereafter dies between the date of separation from service and the member's effective retirement date, where the member has selected a survivorship option under RCW

41.40.188. In those cases the beneficiary named in the member's final application for service retirement may elect to receive either a cash refund, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, or monthly payments according to the option selected by the member.

(4) If a member dies within sixty days following application for disability retirement under RCW 41.40.230, the beneficiary named in the application may elect to receive the benefit provided by:

(a) This section; or

(b) RCW 41.40.235, according to the option chosen under RCW 41.40.188 in the disability application.

(5) The retirement allowance of a member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or the retirement allowance 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,</u> is not subject to an actuarial reduction. The member's retirement allowance is computed under RCW 41.40.185.

Sec. 12. RCW 41.40.700 and 2007 c 487 s 8 are each amended to read as follows:

(1) Except as provided in RCW 11.07.010, if a member or a vested member who has not completed at least ten years of service dies, the amount of the accumulated contributions standing to such member's credit in the retirement system at the time of such member's death, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's estate, or such person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's accumulated contributions standing to such member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670,

shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, the surviving spouse or eligible child or children shall elect to receive one of the following:

(a) A retirement allowance computed as provided for in RCW 41.40.630, actuarially reduced by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 and actuarially adjusted to reflect a joint and one hundred percent survivor option under RCW 41.40.660 and, except under subsection (4) of this section, if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.40.630; if a surviving spouse who is receiving a retirement allowance dies leaving a child or children of the member under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority; if there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance share and share alike calculated as herein provided making the assumption that the ages of the spouse and member were equal at the time of the member's death;

(b) The member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670; or

(c) For a member who leaves the employ of an employer to enter the uniformed services of the United States and who dies after January 1, 2007, while honorably serving in the uniformed services of the United States in Operation Enduring Freedom or Persian Gulf, Operation Iraqi Freedom, an amount equal to two hundred percent of the member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670.

(3) If a member who is eligible for retirement or a member who has completed at least ten years of service dies after October 1, 1977, and

is not survived by a spouse or an eligible child, then the accumulated contributions standing to the member's credit, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid:

(a) To a person or persons, estate, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there is no such designated person or persons still living at the time of the member's death, then to the member's legal representatives.

(4) A member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or 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,</u> is not subject to an actuarial reduction under RCW 41.40.630. The member's retirement allowance is computed under RCW 41.40.620.

Sec. 13. RCW 41.40.835 and 2003 c 155 s 8 are each amended to read as follows:

(1) If a member dies prior to retirement, the surviving spouse or eligible child or children shall receive a retirement allowance computed as provided in RCW 41.40.790 actuarially reduced to reflect a joint and one hundred percent survivor option and, except under subsection (2) of this section, if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.40.820.

If the surviving spouse who is receiving the retirement allowance dies leaving a child or children under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority.

If there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under

the age of majority shall receive an allowance, share and share alike. The allowance shall be calculated with the assumption that the age of the spouse and member were equal at the time of the member's death.

(2) A member who is killed in the course of employment, as determined by the director of the department of labor and industries, <u>or 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,</u> is not subject to an actuarial reduction under RCW 41.40.820. The member's retirement allowance is computed under RCW 41.40.790.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/3/08**	**Z-0072.1 / Z-0393.1**

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 and the Law Enforcement Officers' and Fire Fighters' Retirement System Plan 2 Board throughout the 2008 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 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 bill would provide an unreduced joint and survivor annuity to the survivor of a member who dies in war while serving in the National Guard or Military Reserves.

Impact on Pension Liability

(Dollars in Millions)	Current	Increase	Total
Today's Value of All Future Pensions	$67,081	$0.6	$67,081
Earned Pensions Not Covered by Today's Assets	$4,957	$0.0	$4,957

Impact on Contribution Rates: (Effective 9/1/2009)

2009-2011 State Budget	PERS	TRS	SERS	PSERS	LEOFF	WSPRS
Employee (Plan 2)	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Employer:						
Current Annual Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Total	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
State					0.00%	

Budget Impacts

(Dollars in Millions)	2009-2011	2011-2013	25-Year
General Fund-State	$0.0	$0.0	$0.6
Total Employer	$0.0	$0.1	$1.8

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

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WHAT IS THE PROPOSED CHANGE?

Summary of Benefit Improvement

This proposal impacts the following systems:

- Public Employees' Retirement System (PERS) Plans 1, 2, and 3
- Teachers' Retirement System (TRS) Plans 1, 2, and 3
- School Employees' Retirement System (SERS) Plans 2 and 3
- Public Safety Employees' Retirement System (PSERS)
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plans 1 and 2
- Washington State Patrol Retirement System (WSPRS) Plans 1 and 2

This proposal increases the benefits offered to survivors of members who leave employment to serve in the National Guard or Military Reserves and die while serving honorably during a period of war. Period of war is defined in RCW 41.04.005. Under this proposal, a military survivor who met the existing eligibility standard for a monthly annuity option is now entitled to receive a survivor annuity that is *not* actuarially reduced for each year of retirement prior to the normal retirement age of the specific system and plan.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

Death benefits are provided to qualifying survivors of deceased members in all systems and plans. The eligibility for, and the value of, those survivor benefits differ according to the specific statutory language contained in each section of retirement law. Except in PERS Plan 2, the survivor benefits statutes of each system and plan do not provide different death benefits or eligibility standards for survivors of members who separate from employment for any type of military service and die while performing that service. In these systems and plans, military death survivors are treated the same as a survivor of a deceased member who separated for any other reason.

With the passage of 2SHB 1266 in the 2007 Legislative Session, a qualifying survivor of a PERS Plan 2 member who separates from employment to enter the uniformed services of the United States and dies while serving in the Iraq and Afghanistan conflicts on or after January 1, 2007, is entitled to the following:

- A refund of 200 percent of the member's retirement account balance; *or*
- A survivor annuity actuarially reduced to reflect the difference in age between the age of the member at the time of death and age 65.

The survivor annuity portion of the benefit provided is typically actuarially reduced for each year of retirement prior to the normal retirement age of that system/plan.

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Who Is Impacted And How?

We estimate that all 158,022 active members of PERS Plans 1, 2 and 3, all 64,939 active members of TRS Plans 1, 2 and 3, all 50,825 active members of SERS Plans 2 and 3, all 2,755 active members of PSERS Plan 2, all 16,612 active members of LEOFF Plans 1 and 2, and all 1,037 active members of WSPRS Plans 1 and 2 could be affected by this proposal through improved benefits. However, we only expect this to happen to approximately 1 in 240,000 PERS members per year.

We estimate that for a typical survivor impacted by this bill, the increase in benefits would be an unreduced annuity versus a reduced annuity. For example, the 30 year old beneficiary of a 33 year old male, with 6 years of service in PERS Plan 2 and a $44,000 average final salary, would annually receive a $400 reduced joint and 100 percent survivor annuity, whereas the annual unreduced benefit would be a $4,000 joint and survivor annuity.

Additionally, Plan 2 members would have increased contribution rates in future biennia.

WHY THIS PROPOSL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This bill has a cost because it provides an unreduced joint and survivor annuity instead of a reduced joint and survivor annuity.

Who Will Pay For These Costs?

This bill does not allow for an alternate funding method. The individual plans will subsidize the increase in liability that results from this bill in the usual way. The result may be an increase in future contribution rates for members and employers of the respective systems.

HOW WE VALUED THESE COSTS

Assumptions We Made

We assumed a certain number of members would enter military service in a given year. We adjusted this number based on which plan the member was in. For example, we assumed that more members in public safety plans would enter military service than members in TRS.

Next, we assumed how many members would die during military service. This assumption does not vary by plan.

For more detail please see Appendix A.

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How We Applied These Assumptions

We gathered data for the members of each system and plan. We ran the grouped data through a spreadsheet which models the likelihood of entering military service, the probability of a military death, and the associated cost of an unreduced survivor benefit.

For more detail please see Appendix B.

Special Data Needed

We relied on a Washington Post article, based on Department of Defense records, dated August 23, 2006, that specifies the annual death rate for military personnel in Iraq is 3.92 deaths per 1,000 people. The article also states that troops aged 17-19 are 4.6 times more likely to die than those age 50 and older.

Also, we relied on a Department of Retirement Systems service credit report dated September 30, 2006, to estimate the number of members who enter military service.

Otherwise, we developed these costs using the same assets and data as disclosed in the 2007 Actuarial Valuation Report (AVR).

ACTUARIAL RESULTS

How The Liabilities Changed

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

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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)			
PERS 1	$14,061	$0.0	$14,061
PERS 2/3	20,634	0.3	20,635
PERS Total	**$34,695**	**$0.3**	**$34,696**
TRS 1	11,021	0.0	11,021
TRS 2/3	7,078	0.1	7,078
TRS Total	**$18,099**	**$0.1**	**$18,099**
SERS 2/3	**$2,698**	**$0.0**	**$2,698**
PSERS 2	**$225**	**$0.0**	**$225**
LEOFF 1	4,358	0.0	4,358
LEOFF 2	6,149	0.1	6,149
LEOFF Total	**$10,507**	**$0.1**	**$10,507**
WSPRS 1/2	**$856**	**$0.0**	**$856**
Unfunded Actuarial Accrued Liability			
(The Portion of the Plan 1 Liability that is Amortized to 2024)			
PERS 1	**$3,609**	**$0.0**	**$3,609**
TRS 1	**2,288**	**0.0**	**2,288**
LEOFF 1	**($939)**	**$0.0**	**($939)**
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)			
PERS 1	$3,990	$0.0	$3,990
PERS 2/3	(2,470)	0.2	(2,469)
PERS Total	**$1,520**	**$0.2**	**$1,520**
TRS 1	2,552	0.0	2,552
TRS 2/3	(1,229)	0.0	(1,229)
TRS Total	**$1,323**	**$0.0**	**$1,323**
SERS 2/3	**(443)**	**0.0**	**(443)**
PSERS 2	**(2)**	**0.0**	**(2)**
LEOFF 1	(975)	0.0	(975)
LEOFF 2	(974)	0.1	(974)
LEOFF Total	**($1,949)**	**$0.1**	**($1,949)**
WSPRS 1/2	**($121)**	**$0.0**	**($121)**

Note: Totals may not agree due to rounding.

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How Contribution Rates Changed

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01 percent, therefore the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate increase to measure the fiscal budget changes in future biennia.

Impact on Contribution Rates: (Effective 9/1/2009)

System/Plan	PERS	TRS	SERS	PSERS	LEOFF	WSPRS
Current Members						
Employee (Plan 2)	0.000%	0.000%	0.000%	0.000%	0.000%	0.001%
Employer:						
Normal Cost	0.000%	0.000%	0.000%	0.000%	0.000%	0.001%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.000%	0.000%	0.000%	0.000%	0.000%	0.001%
State					0.000%	
New Entrants*						
Employee (Plan 2)	0.000%	0.000%	0.000%	0.000%	0.000%	0.001%
Employer:						
Normal Cost	0.000%	0.000%	0.000%	0.000%	0.000%	0.001%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.000%	0.000%	0.000%	0.000%	0.000%	0.001%
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.*

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How This Impacts Budgets And Employees

	Budget Impacts						
(Dollars in Millions)	**PERS**	**TRS**	**SERS**	**PSERS**	**LEOFF**	**WSPRS**	**Total**
2009-2011							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
Local Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Employer	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2011-2013							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
Local Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Employer	**$0.1**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.1**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.1**
2009-2034							
General Fund	$0.2	$0.2	$0.0	$0.0	$0.1	$0.0	$0.6
Non-General Fund	0.3	0.0	0.0	0.0	0.0	0.0	0.3
Total State	**$0.5**	**$0.2**	**$0.0**	**$0.0**	**$0.1**	**$0.0**	**$0.9**
Local Government	0.5	0.1	0.0	0.0	0.2	0.0	0.9
Total Employer	**$1.0**	**$0.4**	**$0.1**	**$0.0**	**$0.4**	**$0.0**	**$1.8**
Total Employee	**$0.7**	**$0.2**	**$0.0**	**$0.0**	**$0.4**	**$0.0**	**$1.3**

Note: Totals may not agree due to rounding.

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

As with the costs developed in the actuarial valuation, the emerging costs of the systems 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 assumptions and methods:

- The number of members expected to enter military service and die while serving.

The number of members expected to die while serving in the military would have to increase significantly for this proposal to impact contribution rates in the current biennium. The table below shows the multiple of how many more members would need to die while serving in the military before the rate impact would reach 0.005 percent for

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each system. For example, in LEOFF Plan 2, the employee rate impact would reach 0.005 percent if 11 times as many members as expected die during military service in the future.

System	Multiple
PERS 2/3	20
TRS 2/3	29
SERS 2/3	51
PSERS 2	24
LEOFF 2	11
WSP 1/2	6

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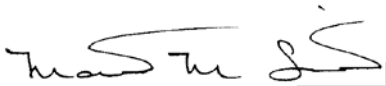
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost 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, assumptions, and data may also be reasonable, and might produce different results.
5. This draft fiscal note has been prepared for the Select Committee on Pension Policy and the Law Enforcement Officers' and Fire Fighters' Retirement System Plan 2 Board.
6. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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APPENDIX A – ASSUMPTIONS WE MADE

We made two main assumptions for this pricing – the number of members who enter military service and the number of members who die while serving in the military.

We assumed a certain number of members would enter military service in a given year. Using the DRS service credit report, we estimated 1 out of every 1,000 PERS members will enter the military. We adjusted this number based on which plan the member was in. For example, we assumed that more members in public safety plans would enter military service than members in TRS. More specifically, TRS and SERS members were assumed to enter at 1 out of every 2,000 members, PSERS members were assumed to enter at 1 out of every 750 members, and LEOFF and WSP members were assumed to enter at 1 out of every 500 members.

For simplicity, we assumed the population affected would be 100 percent male. We assumed there would be 20 percent fewer members entering military service after age 42 due to military age restrictions. Also, we assumed that all members leaving state employment to serve in the military will be in the National Guard or Military Reserves during a period of war.

Next, we estimated how many members would die during military service. We used the Washington Post article (cited in the data section) to set this assumption. The annual death rate for military personnel in Iraq is 3.92 deaths per 1,000 people. The article further explains the fact that troops aged 17-19 are 4.6 times more likely to die than those age 50 and older. Therefore, we approximated the age-based probability of death in the military using these two facts. The overall probability of death was maintained while significantly weighting higher probabilities to younger ages. Furthermore, the addition of accounting for non-combat related deaths will increase the overall assumption rate to approximately 4.4 deaths per 1,000 people. This assumption does not vary by plan.

The two assumptions for PERS can be seen in the table below. When combined, they create one overall assumption for the probability of a survivor receiving an increased benefit in this proposal.

Age	Probability of Interruptive Military Service	Probability of a Military Death	Probability of Receiving Survivor Benefit
20	0.00100	0.009667	0.0000097
25	0.00100	0.008406	0.0000084
30	0.00100	0.007145	0.0000071
35	0.00100	0.005884	0.0000059
40	0.00100	0.004623	0.0000046
45	0.00080	0.003362	0.0000027
50	0.00080	0.002102	0.0000017
55	0.00080	0.002102	0.0000017
60	0.00080	0.002102	0.0000017
65	0.00080	0.002102	0.0000017
70	0.00080	0.002102	0.0000017

Otherwise, we developed these costs using the same assumptions as disclosed in the 2007 AVR.

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APPENDIX B – HOW WE APPLIED THESE ASSUMPTIONS

We gathered average salary, average years of service, and total count for each age group of each plan. We ran the grouped data through a spreadsheet which models the likelihood of a military death and the associated cost of the unreduced survivor benefit for each year of their future service. The likelihood of a military death is outlined in the assumption section. The cost of the benefit increase (unreduced survivor benefit instead of reduced survivor benefit) was calculated as the present value of the unreduced life annuity times one minus the early retirement factor (ERF). The formula is shown below:

[Multiplier (0.01 or 0.02) * service * final average salary * annuity factor * survivorship * interest discount * (1-ERF)] * Probability of receiving survivor benefit.

The annual discount rate is 8 percent, consistent with the AVR.

Formula example: 30 year old TRS Plan 2 male, with 10 years of service and $50,000 final average salary. This member has an immediate annuity factor of 18.92 at age 30. The early retirement factor (ERF) for this member is 0.11.

Unreduced annuity (with ERF): 0.02 * 10 * 50,000 * 18.92 * 1 * 1 * 1 = $189,200
Reduced annuity (with ERF): 0.02 * 10 * 50,000 * 18.92 * 1 * 1 * 0.11 = $20,812
Difference: $189,200 - $20,812 = $168,388
Formula (1-ERF): 0.02 * 10 * 50,000 * 18.92 * 1 * 1 * 0.89 = $168,388

The formula was applied to each future year of the group's service to determine the present value of future benefits for the group. The sum of the present value of future benefits for each group was added up to determine the liability for each system.

Otherwise, we developed these costs using the same methods as disclosed in the June 30, 2007 AVR.

We used the Aggregate Funding Method to determine the fiscal budget changes for current plan members and future new entrants.

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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.

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PLAN 2 RETIREMENT BOARD
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May 12, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

On behalf of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board (Board), I would like to thank you for the cooperative working relationship we have shared in the past and look forward to a similar partnership in the future.

I would like to bring several topics back to your attention as you begin preparation for the 2008 interim. It is our hope that the Select Committee on Pension Policy (SCPP) and the Board can work cooperatively on these issues to once again develop legislation. I have provided a brief summary of each topic for your reference:

Interruptive Military Service Credit
Working cooperatively last interim, the Board and the SCPP jointly endorsed a bill that would have eliminated a member's obligation to pay for interruptive military service credit if the member served during a period of war. The Board is once again interested in working cooperatively with the SCPP on the issue and feels the following additional question will need to be further explored:

- Should the benefit apply to all periods of interruptive military service which have not yet been recovered?

Inflationary Adjustment for $150,000 Death Benefit
The Board is interested in once again working with the SCPP to further study the effect of adding an inflationary adjustment to all the state retirement plans that provide the $150,000 death benefit. In addition to last year's study the Board feels following issues will need to be explored further:

- Should an adjustment in the lump sum amount be made to account for inflation since the creation of the benefit?

- Should both the lump sum adjustment and the addition of the inflationary adjustment be included in the bill?

Military Service Death Benefit

The Board and the SCPP jointly recommended legislation to the 2008 Legislature, which would have provided an unreduced annuity to qualifying survivors of members of all plans, who leave employment due to service in the National Guard or Reserves and die while in military service, during a period of war. The Board would like to continue our joint work to eliminate the "early retirement" actuarial reduction applied to the pensions of members who die while honorably serving our country.

Fish and Wildlife Enforcement Officer Service Credit Transfer

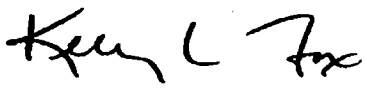
The Board and the SCPP also jointly recommended legislation last session that would have permitted Department of Fish and Wildlife Enforcement Officers to transfer service credit earned in the Public Employees' Retirement System (PERS) Plan 2 as enforcement officers into the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2. The Board feels the following issue may need to be further explored as well:

- Should PERS 3 members be included in the transfer group?

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

We would be happy to meet with you to discuss these topics at an upcoming SCPP or LEOFF Plan 2 Retirement Board meeting. Thank you for your consideration and we look forward to working with you.

Sincerely,



Kelly Fox, Chair

cc: Matt Smith, State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

June 30, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

At the recent meeting of the Select Committee on Pension Policy (SCPP) the chairman requested that the Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board (LEOFF 2 Board) provide a prioritized list of the suggested joint topics that the LEOFF 2 Board would like to work on cooperatively with the SCPP.

During the course of the most recent LEOFF 2 Board meeting we prioritized the suggested topics for cooperation in the following order:

1. **Fish and Wildlife Enforcement Officer Service Credit Transfer**
   Allow FWEO members to transfer their PERS Plan 2 service as enforcement officers to LEOFF Plan 2.

2. **Inflationary Adjustment for $150,000 Death Benefit**
   The $150,000 lump-sum death benefit paid to survivors of public employees who die in the line of duty is not adjusted for inflation.

3. **Interruptive Military Service Credit**
   Members whose public employment is interrupted by military service are required to pay member contributions in order to purchase service credit.

4. **Military Service Death Benefit**
   Beneficiaries of members who die while serving on active duty with the United States Military do not qualify for duty related death benefits.

5. **Purchase of Annuity**
   Members are limited in the amount of money they can convert to a defined benefit by the amount required to purchase 5 years of service.

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly Fox, Chair

cc: Matt Smith, State Actuary

OSA Request Legislation

Description Of Issue

The State Actuary is seeking to update the actuarial funding chapter to clarify how the State Actuary studies salary growth and to codify current practices around actuarial experience studies.

The State Actuary studies economic and demographic components of total salary growth together and makes recommendations as needed. However, current statute can be read to suggest that they are studied at different times.

The State Actuary makes recommendations to the Pension Funding Council (PFC) concerning long-term demographic assumptions based on the results of actuarial experience studies. The PFC considers these recommendations when adopting biennial contribution rates. Current statute only requires the State Actuary to *file* the experience study results—not make recommendations for the PFC to consider.

State Actuary's Proposal

- Clarify that the State Actuary may study all components of total salary growth together.
- Codify current practice that the State Actuary makes recommendations to the PFC based on actuarial experience studies and the PFC considers these recommendations when adopting biennial contribution rates.

Policy Highlights

The proposed changes are consistent with the Actuarial standards of practice and have no fiscal impact on the retirement systems.

Committee Activity

Staff briefed the Committee at its June and October meetings, and a public hearing was held in November. The Committee took executive action to recommend the State Actuary's proposal as SCPP request legislation in 2009.

Recommendation To 2009 Legislature

Clarify how the State Actuary studies salary growth, and codify current practices relating to recommendations of the State Actuary following an actuarial experience study.

Staff Contact

Laura Harper, Policy and Research Services Manager
360.786.6145
harper.laura@leg.wa.gov

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0222.1/09

ATTY/TYPIST: LL:seg

BRIEF DESCRIPTION: Addressing the state actuary's recommendations for assumptions used in the actuarial funding of the state retirement systems.

AN ACT Relating to the state actuary's recommendations for assumptions used in the actuarial funding of the state retirement systems; and amending RCW 41.45.030 and 41.45.090.

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

Sec. 1. RCW 41.45.030 and 2007 c 280 s 1 are each amended to read as follows:

(1) Beginning September 1, 2007, and every two years thereafter, the state actuary shall submit to the council information regarding the experience and financial condition of each state retirement system, and make recommendations regarding the long-term economic assumptions set forth in RCW 41.45.035. <u>When making recommendations regarding the general salary increase assumption, the state actuary may also consider the demographic components of total salary growth and make recommendations to the council concerning any changes to the demographic assumptions within total salary growth.</u> The council shall review this and such other information as it may require.

(2) By October 31, 2007, and every two years thereafter, the council, by affirmative vote of four councilmembers, may adopt changes

to the long-term economic assumptions established in RCW 41.45.035. Any changes adopted by the council shall be subject to revision by the legislature.

The council shall consult with the economic and revenue forecast supervisor and the executive director of the state investment board, and shall consider long-term historical averages, in reviewing possible changes to the economic assumptions.

(3) The assumptions and the asset value smoothing technique established in RCW 41.45.035, as modified in the future by the council or legislature, shall be used by the state actuary in conducting all actuarial studies of the state retirement systems, including actuarial fiscal notes under RCW 44.44.040. The assumptions shall also be used for the administration of benefits under the retirement plans listed in RCW 41.45.020, pursuant to timelines and conditions established by department rules.

Sec. 2. RCW 41.45.090 and 2003 c 295 s 9 are each amended to read as follows:

(1) The department shall collect and keep in convenient form such data as shall be necessary for an actuarial valuation of the assets and liabilities of the state retirement systems, and for making an actuarial investigation into the mortality, service, compensation, and other experience of the members and beneficiaries of those systems. The department and state actuary shall enter into a memorandum of understanding regarding the specific data the department will collect, when it will be collected, and how it will be maintained. The department shall notify the state actuary of any changes it makes, or intends to make, in the collection and maintenance of such data.

(2) At least once in each six-year period, the state actuary shall conduct an actuarial experience study of the mortality, service, compensation, and other experience of the members and beneficiaries of each state retirement system((~~, and into the financial condition of each system~~)). The state actuary shall make recommendations to the council regarding the long-term demographic assumptions for the state retirement systems. Concurrently, when considering the demographic components of total salary growth, the state actuary may also study the general salary increase assumption and make recommendations to the council regarding any change to the noninflationary component of that

economic assumption. The council shall review the experience study results, the recommendations of the state actuary, and other information as it may require.

The results of each investigation shall be filed with the department, the office of financial management, the budget writing committees of the Washington house of representatives and senate, the select committee on pension policy, and the pension funding council. Upon the basis of such actuarial investigation the department shall adopt such tables, schedules, factors, and regulations as are deemed necessary in the light of the findings of the actuary for the proper operation of the state retirement systems.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/08**	**Z-0222.1 / Z-0406.1**

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 (SCPP) throughout the 2008 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 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.

RESULTS

There is no fiscal impact resulting from this proposal.

This proposal affects the processes around actuarial assumption-setting. First, the proposal would clarify how the State Actuary studies total salary growth. Total salary growth is an actuarial assumption with both economic and demographic components. The current statute could be read to suggest that the components are studied at different times. Under this proposal, the State Actuary is specifically authorized to study various components of total salary growth at the same time and make recommendations as needed.

The proposal also codifies current practice related to experience studies. Under current practice and based on experience study results, the State Actuary makes recommendations to the Pension Funding Council (PFC) concerning long-term demographic assumptions. The PFC considers these recommendations when adopting biennial rates. Current statute does not require these steps; it only requires the State Actuary to file the experience study results. The new law would codify current practice.

Both process changes are consistent with the Actuarial Standards of Practice.

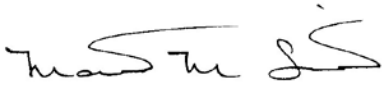
DRAFT

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. This draft fiscal note has been prepared for the SCPP.
2. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

DRAFT

PERS To SERS Auto-Transfer

Description Of Issue

There are statutory provisions to automatically transfer the membership and service credit of certain Public Employees' Retirement System (PERS) Plan 2 members into the School Employees' Retirement System (SERS). This "auto-transfer" was designed to move classified school employees to SERS when the system first opened in 2000.

Policy Highlights

- The advantages of the auto-transfer have diminished since the initial creation of SERS.
- The auto-transfer may be impacting members never intended—most notably PERS 2 members whose primary careers are unrelated to school employment.
- Continuing the auto-transfer may lead to potential legal risk in the future.

Policy Options

- **Target Auto-transfer To Former School Employees.**
  - More consistent with Legislative intent.
  - Eliminates most member complaints.
  - Doesn't address concerns about potential legal risk of continuing the transfer indefinitely.
- **End Auto-transfer.**
  - There is less need for the auto-transfer today.
  - Potential legal risk increases the longer the transfer continues.
  - Members may receive full value for prior school employment in PERS under dual-membership provisions.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 session to end the auto-transfer and allow certain affected members to reverse it (HB 3005/SB 6655). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways & Means.

The Committee held a public hearing and took executive action on this issue in May of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 session.

Recommendation To 2009 Legislature

End the conditional automatic transfer of membership from PERS to SERS and allow certain auto-transferred members to reverse the transfer.

Staff Contact

Dave Nelsen, Senior Policy Analyst
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nelsen.dave@leg.wa.gov

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PERS to SERS Auto-Transfer

In Brief

ISSUE

The membership and service credit of certain PERS 2 members is being automatically transferred to SERS. This transfer, which was designed to move classified school employees to SERS when the system was first opened, occurs even if the member's primary career is unrelated to school employment.

The statutes governing the transfer of PERS membership to SERS may be impacting members that the Legislature did not intend to impact. Further, the open-ended nature of the auto-transfer may lead to unintended consequences in future years.

MEMBER IMPACT

On average, nearly 50 PERS 2 members a month have their membership and service credit transferred to SERS.*

**As of June, 2007.*

Dave Nelsen
Policy Analyst
360.786.6144
Nelsen.dave@leg.wa.gov

Current Situation

There are statutory provisions to automatically transfer the membership and service credit of certain Public Employees' Retirement System (PERS) Plan 2 members to the School Employees' Retirement System (SERS) Plan 2. This will be referred to as the "auto-transfer" throughout this paper. Affected members have their PERS membership and service credit automatically transferred to SERS if they become employed in a SERS eligible position*. If the member has withdrawn any contributions, such contributions and the associated service credit may be restored to SERS. PERS 2 members currently being affected by the auto-transfer provisions if they become employed in a SERS eligible position* include:

- Members who first entered PERS employment after SERS was opened.
- Members who were working for non-educational employers when SERS was opened.
- Members who left or retired from PERS employment prior to the opening of SERS.
- Members whose last employment was for a school district or educational district and who retired from PERS 2 prior to the opening of SERS and opt to re-establish membership.

A PERS 2 member's service and membership will only be automatically transferred to SERS one time – even if the member alternates between PERS and SERS positions throughout their career in public service.

**Or establish membership in SERS as a substitute employee.*

History

The SERS system was created in 1998 and opened to membership on September 1, 2000. Initial membership was comprised of PERS 2 members who were employed by

school districts and educational service districts on September 1, 2000.

The intent of the Legislature in creating SERS was "to achieve similar retirement benefits for all educational employees by transferring the membership of classified school employees in [PERS 2] to [SERS 2]. The transfer of membership to [SERS 2] is not intended to cause a diminution or expansion of benefits for affected members. It is enacted solely to provide public employees working under the same conditions with the same options for retirement planning." See RCW 41.35.005.

SERS was created to allow classified school employees access to Plan 3 benefits.

When the SERS system was created, Plan 3 had been established for teachers, but not for public employees. At that time, classified school employees in PERS wanted the same Plan 3 benefits that were available to teachers. SERS was created to provide that option. SERS featured both a Plan 2 and a Plan 3 when it was created. SERS Plan 2 had the same benefit structure as PERS Plan 2, and SERS Plan 3 had the same benefit structure as the Teachers' Retirement System (TRS) Plan 3. PERS 2 members employed in SERS-eligible positions on the day SERS opened were initially transferred to SERS 2 - where they then had the opportunity to transfer to SERS 3. The transfer of all service, and corresponding contributions, from PERS 2 to SERS 2 provided members who were intending to transfer to SERS 3 the largest possible balance in their SERS Plan 3 defined contribution accounts.

The transfer of PERS 2 members to SERS 2 was extended beyond the initial opening date of SERS.

The transfer of PERS 2 members to SERS 2 was extended beyond the initial opening date of SERS. PERS 2 members who were not employed in a SERS-eligible position when SERS first opened have their PERS 2 membership and service transferred to SERS 2 if they later become employed in a SERS-eligible position. This transfer is accomplished through means of the auto-transfer statutes (see **Current Situation** above for a complete description). In addition to returning school employees, the auto-transfer is impacting PERS members whose primary careers are unrelated to school employment.

Since the initial transfer of PERS 2 classified school employees to SERS 2, over 5,000* PERS 2 members who became employed in SERS eligible positions have had their PERS membership and service credit automatically transferred to SERS. It is unknown how many of these

members' PERS service was related to school employment. The Department of Retirement Systems has received complaints from some members who have had their PERS 2 service automatically transferred to SERS 2 when their primary career was not in SERS.

During the 2004 Legislative Session a bill was introduced that would have removed the provisions for the automatic transfer of PERS 2 members into SERS 2 upon employment in a SERS eligible position. This bill (SB 6610) did not go through the SCPP and did not receive a hearing.

**As of June, 2007.*

Examples

Example 1: School Employee With Break In Service

A PERS 2 member employed by a school district leaves employment after five years of service and prior to the opening of SERS. Two years later the member returns to an eligible position in a school district. The member's five years of prior PERS 2 service are automatically transferred to SERS 2.

Example 2: County Employee Taking A Part-Time SERS job

PERS members taking a part-time SERS job for the first time have their PERS membership automatically transferred to SERS.

A county employee with 15 years of service in PERS 2 takes an additional part-time job with a school district to earn extra money. This is the first time the member has held a SERS-eligible position. Because the member is now employed in a SERS-eligible position, his PERS membership and 15 years of PERS service are automatically transferred to SERS. Any future service rendered for the county remains in PERS.

Policy Analysis

Possible Inconsistency With SERS Intent

The PERS to SERS auto-transfer allows classified school employees who experienced a break in service when SERS first opened to transfer their past service into SERS if they

The Legislature may not have intended the auto-transfer statutes to impact PERS members whose primary careers are unrelated to school employment.

become re-employed in a SERS-eligible position. This is in keeping with the Legislature's stated intent to "provide public employees working under the same conditions with the same options for retirement planning". See RCW 41.35.005. However, the auto-transfer also transfers the membership and service credit of PERS members whose primary careers are unrelated to school employment. This appears to be inconsistent with the original intent of the Legislature in creating SERS. It is possible that the auto-transfer was designed around career school employees. Little consideration may have been given to PERS members who take part-time SERS positions in addition to their primary PERS career. The Legislature may not have intended the auto-transfer statutes to impact PERS members whose primary careers are unrelated to school employment.

Clarifying the language in the existing statutes so the auto-transfer only impacts former school employees would be more consistent with the Legislature's original intent. Such a fix would likely eliminate most, if not all, of the member complaints about the auto-transfer process. However, even if the auto-transfer statutes were amended to only impact this group, there are still policy concerns with having an open-ended auto-transfer.

Implications Of Continuing The Auto-Transfer

Continuing the PERS to SERS auto-transfer may not make as much sense today.

While it may have made sense when SERS was first opened to transfer members' service over from PERS, it may not make as much sense to continue that policy today. Transferring prior PERS service into SERS would have simplified the initial transfer process from both the member's and plan administrator's perspective. From the member's perspective, having all of one's service in a single plan makes retirement planning less complicated. Transferring the prior PERS service provided SERS members the same opportunity that teachers had to move their Plan 2 service into Plan 3 and maximize their Plan 3 defined contribution accounts. This was consistent with the legislative intent to achieve similar retirement benefits for all educational employees. See RCW 41.35.005. From the administrator's perspective, a one-time transfer may have been preferable to maintaining over 40,000 new dual-members.

The advantages of the auto-transfer have diminished since the initial creation of SERS.

The advantages of the auto-transfer, however, have diminished since the initial creation of SERS. The number of former classified school employees returning to service and being impacted by the auto-transfer is relatively small compared to the initial number who transferred to SERS. Some of these members have already experienced a fairly long break in service - nearly seven years – or transitioned to public employment outside of a school district. This raises the question of whether special accommodations should be made for these members if they return to classified school employment. Since PERS now has a Plan 3 and experience has shown that members are generally less interested in transferring from Plan 2 to Plan 3 today, there is likely less need to provide a mechanism for members to transfer prior PERS 2 service into SERS 3. Additionally, it is not guaranteed that benefits will be the same in PERS 2 and SERS 2 in the future, which may result in unintended consequences.

When SERS was first created, the benefit provisions of SERS 2 and PERS 2 were identical. Thus, members did not experience either a diminution or expansion of benefits by having their PERS 2 membership and service transferred to SERS 2. However, the more time that passes following the creation of SERS, the greater the likelihood that the benefit provisions of PERS 2 and SERS 2 will start to diverge. Divergent benefits often result from pension legislation that does not go through a policy committee like the SCPP. If the differences in the plans were to become substantial enough, members may actually begin to experience a diminution or expansion of benefits by having their PERS membership automatically transferred to SERS. Such an outcome was likely not envisioned as a possibility at that time and was clearly not part of the Legislature's original intent in transferring members to SERS (see RCW 41.35.005). If benefits were to diverge to the point that some members were being inadvertently harmed by the auto-transfer, it may create potential legal risk for the state.

In the future, there could be increased legal risk.

Given the diminished benefits of the auto-transfer today and the potential legal risk that may arise from a mandatory transfer of membership in the future, it may be preferable from both a policy and administrative perspective to discontinue the auto-transfer. Policy makers may wish to consider making the transfer of prior PERS 2 service to SERS optional for returning educational

employees, or as an alternative, allowing such employees to become dual-members.

Implications For Dual-Membership

Transferring service credit between systems is counter to the policy of dual-membership which is codified within the "portability" chapter of state law (see RCW 41.54). Dual-membership allows members to combine service from all their systems to qualify for benefits and use the highest salary from any system to determine their benefits. Each system then pays out benefits based on that system's provisions and the service in that system. Dual-membership is designed to ensure that members are neither advantaged nor disadvantaged by changing public careers – even when the underlying benefits of the systems differ.

Members may still receive full value for past school employment under dual-membership provisions.

While dual-membership will effectively make "whole" the retirement benefits for classified school employees whose service crosses from PERS to SERS, it is not an exact substitute for transferring service. Members may still receive full value for their past school employment in PERS under the dual-membership provisions; however, they would not be able to transfer their prior Plan 2 service into Plan 3 as they would under the auto-transfer provisions*. Currently, very few active members opt to transfer from Plan 2 to Plan 3 under the annual transfer window. Cases where a returning classified school employee would wish to transfer all their past Plan 2 service to Plan 3 will likely be the exception.

The PERS to SERS auto-transfer is an exception to the basic policy of dual-membership. Maintaining such an exception may, in rare cases, benefit a few members. However, policy makers may wish to weigh the potential benefits against the potential legal risk.

**The member's PERS 2 service would be transferred to SERS 2 and the member could later opt to transfer that service to SERS 3.*

Implications for Optional Transfer

Making the auto-transfer optional instead of mandatory would reduce the risk of the exposure to one kind of liability while increasing the risk of exposure to another. Making

An optional transfer may result in a cost to other plan members or employers.

the transfer optional would likely eliminate the potential legal risk of members being harmed by the transfer. However, members may be able to take advantage of an optional transfer to increase their benefits while passing the cost of those benefits on to others. This situation could occur if the benefits in SERS were to become more generous than the benefits in PERS. Members electing to transfer their service would essentially be able to "buy" the more expensive SERS benefits using cheaper PERS service. This would result in a cost to the SERS system which would be subsidized by all plan members and/or employers.

Other States

Due to the narrow focus and technical nature of this issue, the experience of other states, if any, would be of limited value to policy makers and would be impractical to obtain.

Policy Questions

Policy makers may wish to consider the following questions when deliberating on this issue:

- Should the auto-transfer statutes be amended so that they only impact members whose prior PERS service was rendered for a school or educational service district?
- Should the PERS to SERS auto-transfer be made optional? Discontinued? If discontinued, what is the appropriate date to discontinue it?

Conclusion

The PERS to SERS auto-transfer was designed to facilitate the initial creation of the SERS system for classified school employees. The auto-transfer was extended beyond the initial opening date of SERS, and is impacting both returning school employees and PERS members whose primary careers are unrelated to school employment. The Legislature may not have intended to impact this latter group of PERS members.

The automatic transfer of PERS 2 membership and service to SERS 2 at the initial opening of SERS was advantageous for both members and the plan administrator. The advantages of the auto-transfer; however, have diminished since the initial creation of SERS. Continuing the mandatory auto-transfer indefinitely may expose the state to potential legal risk if the benefits in SERS 2 and PERS 2 diverge in the future. Making the auto-transfer optional would eliminate one source of potential liability, but it may result in costs being shifted to other SERS members or employers. In the absence of transfer provisions, SERS members may still receive full value for any past school employment in the PERS system under dual-membership provisions.

Policy makers may wish to weigh the potential benefits and risks of continuing the auto-transfer.

Policy makers may wish to weigh the potential benefits against the potential risks of continuing the auto-transfer in its present form.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 Session to end the auto-transfer and allow certain affected members to reverse it (HB 3005/SB 6655). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways & Means.

The Committee held a public hearing and took executive action on this issue in May of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 Session.

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

End the conditional automatic transfer of membership from PERS to SERS and allow certain auto-transferred members to reverse the transfer. Recommended May 13, 2008.

Stakeholder Input

Correspondence on file from:

John Kvamme, WASA & AWSP consultant, 4/15/2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0071.2/09).

Draft Fiscal Note

Attached.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0071.2/09 2nd draft

ATTY/TYPIST: LL:seg

BRIEF DESCRIPTION: Transferring public employees' retirement system plan 2 members to the school employees' retirement system plan 2.

AN ACT Relating to the transfer of public employees' retirement system plan 2 members to the school employees' retirement system plan 2; and amending RCW 41.40.750.

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

Sec. 1. RCW 41.40.750 and 2001 2nd sp.s. c 10 s 13 are each amended to read as follows:

(1) Effective September 1, 2000, the membership of all plan 2 members currently employed in eligible positions in a school district or educational service district and all plan 2 service credit for such members, is transferred to the Washington school employees' retirement system plan 2. Plan 2 members who have withdrawn their member contributions for prior plan 2 service may restore contributions and service credit to the Washington school employees' retirement system plan 2 as provided under RCW 41.40.740.

(2)(a) The membership and previous service credit of a plan 2 member not employed in an eligible position on September 1, 2000, will be transferred to the Washington school employees' retirement system plan 2 when he or she becomes employed in an eligible position <u>prior to August 1, 2009</u>. Plan 2 members not employed in an eligible position on

September 1, 2000, who have withdrawn their member contributions for prior plan 2 service may restore contributions and service credit to the Washington school employees' retirement system plan 2 as provided under RCW 41.40.740, if they first establish eligibility in the Washington school employees' retirement system plan 2 prior to August 1, 2009.

(b) The membership and previous service credit of a plan 2 member last employed by a school district or educational service district and retired prior to September 1, 2000, will be transferred to the Washington school employees' retirement system plan 2 if the member opts to reestablish membership prior to August 1, 2009.

(3) Members who restore contributions and service credit under subsection (1) or (2) of this section shall have their contributions and service credit transferred to the Washington school employees' retirement system.

(4) From September 1, 2009, through November 30, 2009, upon written request to the department, active and inactive members transferred under subsection (2) of this section who did not establish membership and earn service credit for employment with a school district or educational service district prior to the transfer, and who have not transferred to plan 3 of the Washington school employees' retirement system or plan 3 of the public employees' retirement system, may restore their transferred membership and previous service credit to plan 2. All previously transferred contributions and interest, and additional interest as determined by the department, shall be returned to plan 2. An additional amount shall be transferred from the Washington school employees' retirement system sufficient to offset the liabilities returned to plan 2 under this subsection, as determined by the state actuary.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/19/08**	**Z-0071.2 / Z-0392.1**

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 throughout the 2008 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 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

No change to the unfunded liabilities of the affected systems.

This proposal gives certain School Employees' Retirement System (SERS) members who had service automatically transferred from the Public Employees' Retirement System (PERS) the option to move their service and associated savings funds back to PERS. This proposal provides for an additional transfer of assets from SERS to PERS to offset the liability transferred to PERS.

Passage of this proposal would result in a transfer of liabilities of about $28.1 million to PERS from SERS. Transfers of savings funds and additional assets from SERS to PERS totaling $11.5 million and $16.6 million, respectively, totally offset the transferred liability. Because the transfer of assets fully offsets the transfer of liabilities, this proposal will not affect the contribution rates of either PERS or SERS.

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

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WHAT IS THE PROPOSED CHANGE?

Summary of Change

This proposal impacts PERS Plan 2 and SERS Plan 2 by amending RCW 41.40.750 to do the following:

- Stop the automatic transfer of prior PERS Plan 2 service to SERS Plan 2:
  - Upon employment in a SERS eligible position. Prior PERS Plan 2 members hired into SERS eligible positions after the proposal's effective date become dual members under the provisions of Chapter 41.54 RCW.
  - For former PERS Plan 2 members who worked in SERS eligible positions, retired prior to September 1, 2000, later returned to work in a SERS eligible position, and opted back into SERS membership.
- Remove the requirement to restore withdrawn prior PERS Plan 2 service in SERS Plan 2. Restorations for members hired after the proposal's effective date will occur under the dual membership provisions of Chapter 41.54 RCW.
- Provide a three month window for current and former SERS Plan 2 members to choose to reverse the transfer of prior PERS Plan 2 service and savings accounts. To reverse the transfer members must have:
  - Not worked in a SERS eligible position prior to their transfer.
  - Been automatically transferred after September1, 2000.
- Transfer additional funds from the SERS Plan 2 trust fund to the PERS Plan 2 trust fund to offset the liability transferred to PERS under this proposal.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

The provisions of RCW 41.40.750 provide the following:

- All prior PERS Plan 2 members hired into SERS eligible positions after September 1, 2000, have their PERS Plan 2 membership automatically transferred to SERS Plan 2.
- SERS Plan 2 members who withdrew prior PERS Plan 2 service must restore that service in SERS Plan 2.
- PERS Plan 2 members who worked in a SERS eligible position, retired prior to September 1, 2000, and opt into membership upon employment in a SERS eligible position will have their prior service in PERS Plan 2 transferred to SERS Plan 2.

Who Is Impacted And How?

We estimate that 5,799 PERS members had service transferred to SERS after September 1, 2000. Of those we estimate this proposal impacts about 1,860 members by giving them the ability to move their service and associated savings funds back to PERS. The affected members include actives, terminated vested members, and Terminated Non-Vested (TNV) members. TNV members can only receive their contributions with interest.

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This proposal also impacts members who withdrew their PERS service and savings funds, but upon becoming a SERS member had the right to restore that service credit. We estimate that 1,915 members had a right to restore PERS service credit automatically transferred to SERS. Since these members withdrew their PERS service, no service credit was transferred to SERS. These members have five years from the time they become SERS members to restore their PERS service for a subsidized amount. After five years the members can still restore the withdrawn service credit, but they must pay the full actuarial value.

We don't believe the members impacted by this proposal will receive improved benefits. The only difference between the benefits in PERS 2 and SERS 2 is the availability of a 200 percent refund of contributions benefit for PERS 2 members who interrupt their PERS service to join the uniformed services and are subsequently killed while on active duty.

See the Special Data Needed section of this draft fiscal note for more details.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

Transferring service from SERS to PERS decreases the pension costs in SERS and increases them in PERS. To offset the pension cost change this proposal transfers the savings funds back to PERS from SERS attributable to the transferred service. The transfer of savings funds in most cases does not fully offset the transferred pension costs for two main reasons. First, this proposal transfers only the member contributions not the employer contributions. Second, the Department of Retirement Systems (DRS) credits 5.5 percent interest to the savings funds. But we assume 8 percent interest when we calculate the liabilities. This difference in credited and assumed interest implies the assets will never accumulate in the members' saving funds at a high enough rate to cover the cost of their pensions.

In a few cases the accumulated value of a member's savings fund exceeds the value of the transferred service. We believe this situation results for a few reasons: decreases in a member's salary, changes in a member's working status, or both.

When a member's salary decreases, so does their Average Final Compensation (AFC). A lower AFC leads to lower liabilities. Also the contributions collected on the prior higher salaries lead to higher savings funds relative to the liabilities calculated on current lower salaries. Since the data we have only shows current salaries, we cannot identify specific cases where lower salaries lead to savings funds being more valuable than the associated liabilities.

Members who no longer work in a pension system do not receive salary increases. Since these members' salaries don't increase, neither does their AFC. This leads to lower liabilities. Also the contribution rates charged while the member worked reflected the assumption that members would continue to receive salary increases. The result is again

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that the savings funds for these members transferred back to PERS exceed the corresponding liabilities.

For members who withdrew their PERS service prior to taking a position with a SERS employer, DRS transferred the members' right to restore service credit to SERS. This proposal provides that members who restore PERS service credit in SERS can elect to move the restored service and associated savings fund back to PERS.

Who Will Pay For These Costs?

The proposal mandates an additional asset transfer from the SERS trust fund to the PERS trust fund to fully offset the change in pension cost. As a result this proposal does not impact contribution rates in either PERS or SERS.

HOW WE VALUED THESE COSTS

Assumptions We Made

For each member we determined the value of their eligible prior PERS service and the value of the savings funds attributable to that service as of June 30, 2007. The value of the service depends on when we expect the member to retire and how much salary they earned prior to retirement. The value of the savings fund only depends on when the member transferred.

We assumed all members would retire at the earliest of the following:

- Upon reaching 30 years of service between ages 55 and 65.
- At age 65.
- Immediately if currently older than age 65.

Finally, the amount of the total liability and assets transferred back to PERS depends on the number of people who elect to participate under this proposal. The liabilities and assets shown in this draft fiscal reflect that we valued this proposal assuming every member who could transfer would.

For more detail please see Appendix A.

How We Applied These Assumptions

We used a spreadsheet model to apply the assumptions to the individual members impacted by this proposal. We used the SERS salary growth and mortality assumptions to determine the value of the liability for each member. We accumulated each member's savings fund with interest to the valuation date. The assets required to ensure this proposal doesn't impact contribution rates equals the difference between the liabilities and savings funds.

For more detail please see Appendix B.

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Special Data Needed

DRS provided a data file containing records for the 5,799 members automatically transferred from PERS to SERS since September 1, 2000. This data file contained the months of service, the savings fund balance transferred for each member, the date the service and savings funds transferred, the plans in both PERS and SERS the members were in, and whether or not the member had prior service in PERS for an educational employer. We relied upon this data as complete and accurate. We combined this data file with the PERS and SERS 2007 valuation data to determine each member's current status, current salary, and total service.

The data DRS provided doesn't identify members who restored PERS service in SERS. As of the date of this draft fiscal note we requested an updated data file from DRS. We will include the results in the final fiscal note we produce for the 2009 Legislative Session. We did not attempt to value liability for members who could restore prior PERS service credit in SERS and elect to transfer that service credit back to PERS under this proposal.

For more details please see Appendix C.

ACTUARIAL RESULTS

How The Liabilities Changed

The transfer of service from SERS Plan 2 to PERS Plan 2 will result in a liability decrease in SERS and a liability increase in PERS. This liability represents the value in today's dollars of all the future pension payments we expect DRS to pay as a result of the service transferred. This proposal also transfers from SERS Plan 2 to PERS Plan 2 the accumulated value of the member contributions paid at time the member earned the service. This asset transfer will result in a decrease in SERS assets and an increase in PERS assets. Since the accumulated value of all the savings funds does not exceed the value of the future pension payments, this proposal mandates that SERS transfer additional assets to PERS to ensure the contribution rates stay the same in both systems.

The following table summarizes the results.

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Table 1

Summary of Liabilities and Assets Expected to be Transferred		
	System/Plan	
(Dollars in Millions)	PERS 2	SERS 2
Liability change	$28.1	-$28.1
Savings Fund asset change	11.5	-11.5
Additional asset transfer	16.6	-16.6
Change in Unfunded Liability	$0.0	$0.0

The analysis of this proposal does not consider any other proposed changes to the system. The combined effect of several changes to the system 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 2007 Actuarial Valuation Report (AVR) or this fiscal note to the extent that actual experience differs from the actuarial assumptions.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

We did not perform specific sensitivity tests for this pricing. The liabilities and assets calculated for this fiscal note depend heavily on the number of members transferring service from SERS back to PERS. If half of the 1860 members elect to transfer service back to PERS, we would expect the liabilities and assets to be approximately half of the values displayed in Table 1.

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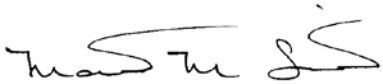
ACTUARY'S CERTIFICATION

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, assumptions, and data 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 gave 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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APPENDIX A – ASSUMPTIONS WE MADE

We assumed no pre-retirement terminations or disablment. That is, we assumed that each member would reach retirement age. For members currently age 65 or older, we assumed they would retire immediately.

We calculated the deferred annuity factors using SERS Plan 2 mortality regardless of whether the member had previously resumed employment in PERS. We used the SERS assumptions for blending the annuity factors between male and female. In SERS we assume 55 percent of the population is female.

We assumed that all members would elect to transfer their eligible service from SERS back to PERS.

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

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APPENDIX B – HOW WE APPLIED THESE ASSUMPTIONS

We used an individual annuity factor model to determine the liability associated with the service being transferred from SERS to PERS. The total liability being transferred equals the sum of the individual liabilities. We received the data used to calculate the liabilities and savings funds from DRS listing all the members with service transferred since September 1, 2000. For a description of the data please see Appendix C. For each member we determined their current age, their current total service and salary, and their projected service and age at retirement. From the original transfer to SERS the data included the number of months of service credit transferred, the savings fund, and the date of transfer.

We used the SERS salary inflation, salary merit, AFC calculation, and mortality assumptions described below to create the following factors:

- Pay Factor – based on the member's total current service earned to date. For non-vested members no longer employed in either PERS or SERS, we set this factor equal to one.
- Average Final Compensation (AFC) Factor – based on the member's projected service at retirement. For members no longer active in PERS or SERS we used a five-year AFC factor of 0.92; based solely on the SERS general salary increase assumption of 4.25 percent per year.
- Annuity Factors – deferred life-annuity factors with a 3 percent cost of living adjustment after the deferral period. We used factors deferred to ages 55 through 65 depending on the age and service combination of a given member.
- Present Value of Future Benefits (PVFB) Factor – calculated using the other factors as follows: (AFC Factor x Annuity Factor) / Pay Factor

The liability for each individual equals the product of their years of service transferred times the 2 percent plan accrual rate times their current salary times their calculated PVFB factor times an early retirement reduction factor.

Because DRS doesn't report salaries for TNV members, the calculation just described yields a liability of zero. We set their liability equal to the value of their transferred savings funds with interest accumulated to the valuation date.

For terminated vested members without a salary, we assigned them the SERS Plan 2 average salary from the 2007 AVR of $26,531.

The value of the assets transferred from SERS Plan 2 to PERS Plan 2 equals the sum of the individual member savings funds with interest. DRS reported the original savings fund values transferred to SERS from PERS in the data along with the dates the individual transfers took place. We applied the 5.5 percent interest rate, compounded quarterly, to determine the savings fund values as of the valuation date. DRS prepared the data file from after the valuation date; therefore, we discounted some of the members' savings funds back to the valuation date.

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

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APPENDIX C – SPECIAL DATA NEEDED

Of the 5,799 records in the data file, we excluded 3,939 from this pricing for the following reasons:

- The member transferred to or from a Plan 3.
- The member had previous service in PERS in a SERS eligible position.
- The member didn't have any data in the PERS or SERS 2007 valuation data. This implies the member either terminated and withdrew their service, or transferred to a different system. In either case we didn't include these members because we could not accurately value their liability or savings funds.
- The member didn't have any months of service credit transferred, just the right to restore PERS service credit in SERS.

The following table summarizes the number of records excluded by cause. We identified some of the records as not being eligible for more than one reason; therefore, the "Total Count Excluded by Reason" in the table below totals to more than the 3,939 records excluded from this pricing.

Table 2

Summary Counts of Excluded Records by Cause of Exclusion

Reason for Exclusion	Total Count Excluded by Reason	Additional Records Excluded when Reasons are Taken in Order (top to bottom)
Member of a Plan 3	422	422
Prior PERS Educational Service	1,926	1,725
No data in any system	377	303
No months of service transferred	1,915	1,489
Total	**4,640**	**3,939**

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

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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 not covered by plan assets.

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Pre-LEOFF Survivor Benefits

Description Of Issue

The ability of some spouses to collect survivor benefits in the Firemen's Relief and Pension Plans (FRP) is restricted. Some spouses do not qualify for survivor benefits from the plan, and survivor benefits for certain other spouses are stopped upon remarriage.

Stakeholders are proposing two changes:

- Continue paying survivor benefits when a surviving spouse remarries.
- Provide a new, member-paid survivor benefit option for spouses who are otherwise ineligible to receive a survivor benefit from the plan.

The FRP covered fire fighters prior to the creation of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Retirement System in 1970. There are no active members remaining in the FRP plan. It is unknown how many retired members or survivors would be impacted by these proposals since the plan is not administered by the state.

Policy Highlights

- The proposed changes are consistent with earlier changes in LEOFF.
- There is also a pre-LEOFF police system with provisions for surviving spouses similar to those currently in the FRP.
- Policy makers may take different views on this issue depending on whether benefits are member-paid or offered at no additional cost to the member.
- Not providing survivor pensions may raise broader public policy concerns around
    - financially supporting spouses, and
    - benefit designs that may discourage marriage.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 session implementing the proposed changes (HB 3020/SB 6650). The 2008 SCPP bill did

not pass the Legislature, but did pass the House and the Senate Committee on Ways and Means.

The Committee held a public hearing and took executive action on this issue in December of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 session.

Recommendation To 2009 Legislature

Provide a new, member-paid survivor benefit option for spouses who are ineligible to receive a survivor benefit from the plan, and continue paying survivor benefits when a surviving spouse remarries.

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Pre-LEOFF Survivor Benefits

In Brief

ISSUE

Stakeholders are proposing two changes to survivor benefits provided in the pre-LEOFF Firemen's Relief and Pension Plans (FRP).

Stakeholders are requesting that survivor pensions not stop when a surviving spouse remarries.

Stakeholders are also requesting that members be allowed to provide a survivor annuity to a spouse who is otherwise ineligible to receive one. This annuity would be provided at member cost.

MEMBER IMPACT

There are no active members remaining in the FRP plan. It is unknown how many retired members or survivors would be impacted by these proposals since the plan is not administered by the State.

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Current Situation

Stakeholder Proposals

Stakeholders are proposing two changes to survivor benefits provided in the Firemen's Relief and Pension Plans:

- Continue paying survivor benefits when a surviving spouse remarries.
- Provide a new, member-paid survivor benefit option for spouses not eligible for a benefit from the plan.

Stakeholders have requested that the new survivor benefit option be modeled after an option currently provided in the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF). The option would allow members to provide an actuarially equivalent survivor annuity to a spouse who is otherwise ineligible for a survivor annuity. Members electing this new option would have their pensions actuarially reduced to pay the cost of providing the survivor annuity. The actuarial reduction would be removed if the spouse predeceases the member.

Background

The FRP covered fire fighters prior to the creation of LEOFF. The plan provides retirement, disability, and survivor benefits for paid members of a fire department who were actively employed as a fire fighter or a fire dispatcher prior to March 1, 1970. The plan closed to new members on March 1, 1970, and all active members were transferred to LEOFF. The plan is administered by local governments for remaining members, and benefits are paid out of local government funds.

Benefits in the plan are funded through a property tax levy and a portion of fire insurance premium taxes. Each municipality may levy property taxes of up to 45 cents per $1,000 of assessed value against all taxable property to support the FRP. If all or a portion of the property tax is not necessary to maintain the FRP, the taxes may be reduced

or used for any other municipal purpose. Additionally, the State distributes 25 percent of the tax collected on fire insurance premiums to support the FRP. Each eligible city, town, or fire protection district receives its share of the premium taxes based on their current number of active fire fighters.

Currently, FRP provides different survivor benefits depending on the circumstances of the member's death. The surviving spouse of a member who is killed in the line of duty receives a survivor pension of 50 percent of the member's basic salary. The surviving spouse of a member who dies while retired for service or for a duty-related disability continues to receive the member's benefit. The surviving spouse of a member who dies from a disability not related to duty receives a survivor pension of one-third of the member's basic salary with additional amounts provided for each child. If there is no surviving spouse, the pension that would otherwise have been payable to the spouse is divided among the eligible children in equal shares. Survivor benefits are provided at no additional cost to the member.

Some spouses are not eligible to receive survivor benefits from the plan.

In order to qualify for survivor benefits, a surviving spouse must have been married to the member at the time of the member's death in the line of duty or retirement for disability, or married five years prior to the member's retirement for service.

The survivor benefit paid to a surviving spouse of a member who died in the line of duty or was retired for disability is stopped if the spouse remarries. In contrast, the survivor benefit paid to the surviving spouse of a member retired for service continues even if the spouse remarries. Survivor benefits paid to child survivors cease when the child attains the age of eighteen or is married.

History

Survivor Benefits In LEOFF

The changes stakeholders are proposing for FRP are similar to changes that have been made in the LEOFF system.

The changes stakeholders are proposing for FRP are similar to changes that have been made in the LEOFF system.

Initially, survivor benefits payable to surviving spouses in LEOFF Plan 1 were stopped if the spouse remarried. Over time, the plan was amended so that benefits payable to

surviving spouses continued even if the spouse remarried. The plan was further amended in 2002 to allow members to provide an actuarially equivalent survivor annuity to a spouse otherwise ineligible for a survivor annuity from the plan. The cost of the new survivor benefit was paid for by members electing it. Members who were already married to an ineligible spouse were given a one-year window to designate their spouse as a beneficiary for the new survivor benefit option.

The SCPP Has Recommended Bills On This Issue

The SCPP studied this issue in 2007 and recommended a bill in the 2008 Session implementing the stakeholders' proposed changes. See below for more details concerning the SCPP legislation.

Bills Have Been Introduced In Two Sessions

In 2007, non-SCPP legislation was introduced that would have addressed one of the stakeholder proposals regarding survivor pensions in the FRP. HB 1824 would have removed provisions in the FRP that stop the survivor pension for certain spouses who remarry. The bill did not address the other stakeholder proposal concerning a new survivor benefit option. The bill passed the House, but did not receive a hearing in the Senate.

The SCPP introduced legislation on this issue in 2008.

In 2008, the SCPP introduced a bill that would have implemented both of the stakeholders' proposed changes (HB 3020/SB 6650). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways and Means.

Examples

Remarriage Of Surviving Spouse

Emma is the widow of a fire fighter who retired from the FRP for disability. Emma has been collecting a survivor pension for 20 years, and is currently receiving $3,000 per month. If Emma were to remarry, her survivor pension would be stopped. However, if Emma's husband had been retired for service, Emma would be able to remarry without having her survivor pension stopped.

Ineligible Spouse – Post-Retirement Marriage

Bill is a former fire fighter who retired for *disability* from the FRP 37 years ago. At the time of his retirement, Bill was not married. Five years after retiring, Bill married Becky. Because Becky was not married to Bill *at the time of his retirement*, she is not eligible for a survivor benefit from the plan.

Ineligible Spouse – Married At Retirement

John is a former fire fighter who retired for *service* from the FRP 37 years ago. Six months prior to his retirement, John was married to his current wife Joan. Because Joan was not married to John *one year prior to his retirement*, she is not eligible for a survivor benefit from the plan

Policy Analysis

Other Washington Plans

The majority of fire fighters in Washington State are covered by the LEOFF system, and this paper will use the LEOFF system as the basis for comparison.

The first stakeholder proposal relates to the remarriage of surviving spouses. In both plans of the LEOFF system, survivor pensions do not cease when a surviving spouse remarries -- regardless of whether the survivor benefit was paid for by the member or provided at no additional cost to the member.

Surviving spouses in the LEOFF system may generally qualify for a member-paid survivor pension regardless of when or how long they were married to the member. Pensions are not stopped even if the spouse remarries.

The second stakeholder proposal relates to the eligibility of a spouse to qualify for a survivor pension. Here, the approach taken by the plans differs depending on whether the survivor benefit is paid for by the member or provided at no additional member cost.

In LEOFF 1, a surviving spouse must be married to the member one year prior to retirement for service to qualify for a survivor benefit at no member cost. LEOFF 1 also provides an additional member-paid survivor benefit option for spouses not otherwise eligible for the free survivor annuity (including post-retirement spouses).

LEOFF 2 generally provides survivor benefits at member cost and does not generally limit the ability of a spouse to receive a benefit based on when or how long they were married to the member (including post-retirement spouses).

In both plans of the LEOFF system, member-paid survivor benefits are administered by means of an actuarial reduction to the member's pension. Both plans have provisions to restore the member's pension to the unreduced amount if the spouse predeceases the member -- commonly referred to as a "pop-up" provision.

There is also a pre-LEOFF police system with provisions for surviving spouses similar to the FRP.

There also exists a pre-LEOFF Police Relief and Pensions (PRP) system that has provisions similar to the FRP in regards to survivor benefits for spouses. The PRP closed to new members on March 1, 1970, and all active members were transferred to LEOFF. Like the FRP, the plan is administered by local governments for remaining members, and benefits are paid out of local government funds. As in the FRP, survivor pensions paid to surviving spouses are stopped if the spouse remarries, and a spouse must be married five years prior to the member's retirement for service to qualify for survivor benefits. The PRP also provides a $300 per month pension for a surviving spouse who is otherwise ineligible for a survivor pension.

Other States

An examination of how plans covering fire fighters in Washington's comparative states handle spousal eligibility for survivor pensions and the remarriage of surviving spouses is relevant to the discussion of this issue.

Other states generally provide options for most spouses to receive a survivor pension and do not stop such pensions if the survivor remarries.

Research conducted in 2007 showed that Washington's comparative states generally provide survivor benefits at member-cost. These states do not have length of marriage requirements for a spouse of a service retiree to be eligible for a member-paid survivor annuity. The majority of other states also allow members some opportunity to designate a post-retirement spouse for a survivor benefit, and "Pop-up" provisions are common.

In addition to member-paid benefits, California also offers an employer-provided (at no member cost) survivor annuity benefit. The spouse must have been married at least one year prior to the member's retirement to qualify for the employer-provided annuity.

Plans covering fire fighters in Washington's comparative states do not stop a survivor pension if the surviving spouse remarried.

See **Appendix A** for more detailed information on survivor benefits in other states.

Free Versus Member-Paid Benefits

Policy makers may take different views depending on whether benefits are member-paid or offered at no additional cost to the member.

The two stakeholder proposals on FRP survivor benefits generally address the ability of a spouse to qualify for a survivor pension from the plan. Policy makers may take different views on this issue depending on whether benefits are member-paid or offered at no additional cost to the member.

When survivor benefits are paid for entirely by the member, they may be viewed more along the lines of providing member flexibility in payment options. There may be little perceived need to place restrictions on who may qualify for such benefits since the cost is entirely born by the member. When survivor benefits are paid for by the member, there is little reason from both a plan design and public policy perspective to either limit a spouse's ability to receive a survivor benefit or to stop survivor benefits if a surviving spouse remarries.

When survivor benefits are provided free to the member, there may be greater reason to limit who qualifies.

In contrast, survivor benefits that are provided free to the member may be viewed more along the lines of a public benefit. In such cases, policy makers may wish to place restrictions on who qualifies for such benefits and limit the circumstances under which the benefits are paid. Such restrictions may serve many purposes such as:

- Lowering the cost of providing survivor benefits.
- Directing benefit dollars to recipients with the greatest perceived need.
- Preventing perceived abuse.

For example, policy makers may require a spouse to be married to the member for a certain number of years prior to the member's retirement or death. Such a restriction may serve to ensure survivor benefits are going to spouses who were married to the member for some portion of their public career. It may also serve to prevent "death-bed" marriages—where a member who has a short time to live

marries simply to provide the free survivor benefit to someone.

Policy makers may also choose to stop survivor benefits when a surviving spouse remarries. Such a restriction may serve to prevent a spouse from collecting more than one survivor benefit from the plan if they remarry another plan member. It may also serve to direct survivor pension dollars to those surviving spouses who do not have access to income from another marriage.

Some restrictions may run counter to broader public policy concerns.

While there are reasons from a plan design perspective to restrict the ability of a spouse to collect a survivor pension, some restrictions may run counter to broader public policy concerns. Restrictions related to the length and timing of marriage may result in a member not being able to provide a survivor annuity for a spouse of many years. Restrictions related to collecting survivor pensions after remarriage may serve as a disincentive for a surviving spouse to ever remarry. For those spouses who do remarry, the loss of a survivor pension may create financial difficulty —particularly if the pension had been collected and relied upon for many years.

Cost Implications

The two stakeholder proposals relating to FRP survivor benefits have very different cost implications. Continuing survivor pension payments that would otherwise be stopped upon the remarriage of the surviving spouse has a direct cost to the plan. Because the FRP has been closed for many years and there are no longer any active members, such additional costs cannot be funded over the working lifetime of plan members. It is unknown whether the tax revenue currently allocated to pay the benefits of the plan is sufficient to cover the cost of any additional benefit improvements.

Providing members a new actuarially equivalent survivor benefit option for otherwise ineligible spouses has no cost to the plan—the benefit is entirely paid for by the member. However, implementing such an option may generate administrative costs for the various local governments that still pay FRP benefits. Plan administrators may need to consult with actuaries or other experts to develop the new survivor option.

The total cost of the stakeholder proposals relating to FRP survivor benefits is indeterminate at this time due to lack of available data (see attached fiscal note). The plan is administered by local boards and there is no State oversight or centralized reporting. The cost of the proposals would be entirely born by the local governments paying the benefits. SCPP members may wish to consider whether the policy concerns warrant advancing a legislative proposal with an unknown cost.

Members may wish to consider if policy concerns warrant advancing a legislative proposal with an unknown cost.

Conclusion

Stakeholders have made two proposals regarding survivor benefits in the FRP. Both of the proposals generally address the ability of a spouse to collect a survivor pension from the plan. One proposal is to continue paying survivor pensions when a surviving spouse remarries. This proposal has a cost that is indeterminate at the present time due to insufficient data. The other proposal is to provide a new member-paid survivor benefit option for an otherwise ineligible spouse. This proposal has no cost to the plan. Both proposals are consistent with current practice in the LEOFF system.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 Session implementing the proposed changes (HB 3020/SB 6650). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways and Means.

The Committee held a public hearing and took executive action on this issue in December of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 Session.

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

Provide a new, member-paid survivor benefit option for spouses who are ineligible to receive a survivor benefit from the plan, and continue paying survivor benefits when a surviving spouse remarries. Recommended December 16, 2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0401.1/09).

Draft Fiscal Note

Attached.

Stakeholder Input

The following correspondence is on file with the Office of the State Actuary.

Correspondent	Affiliation	Date
Richard Warbrouk	President, RFFOW	09/25/2008
Harold Kershner		11/24/2008
Gail Swan		12/12/2008
Joseph Burns		12/23/2008

Stakeholder Input

Four items regarding this issue are on file with OSA.

Supporting Information

Appendix A

Plans Covering Fire Fighters in Other States				
State	**Survivor Benefit Ceases on Remarriage**	**Restrictions on Eligible Spouse for Service Retirement Survivor Benefit**	**May Designate a Post-Retirement Spouse for Survivor Benefits**	**Pop-Up**
California				
Employer-Provided	No	Married 1 year prior	No	
Member-Paid	No	No	Yes	Yes
Iowa	No	No	Yes	Yes
Missouri	No	No	No	Yes
Ohio	No	No	Yes	Not specified
Colorado	No	No	Yes	Yes
Florida	No	No	Yes	Not specified
Idaho	No	No	Yes	Yes
Iowa	No	No	No	Yes
Minnesota	No	No	No	Yes
Oregon	No	No	Yes	Yes
Wisconsin	No	No	Yes	Yes

Data obtained from plan administrator websites, member handbooks, and other publications available online as of 11/26/2007.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0401.1/09

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Providing benefits for the survivors of certain firefighters.

AN ACT Relating to benefits for the survivors of certain firefighters; amending RCW 41.18.080 and 41.18.100; and adding a new section to chapter 41.18 RCW.

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

NEW SECTION. **Sec. 1.** A new section is added to chapter 41.18 RCW to read as follows:

(1) Any retired firefighter married to a spouse ineligible for survivor benefits under RCW 41.18.040, 41.18.080, and 41.18.100 may choose an actuarially equivalent benefit adopted by the board that pays the retired firefighter a reduced retirement allowance, and upon death such portion of the retired firefighter's reduced retirement allowance as designated by the retired firefighter shall be continued throughout the life of the spouse.

(2) A retired firefighter who married a spouse ineligible for survivor benefits under RCW 41.18.040, 41.18.080, and 41.18.100 prior to the effective date of this section has one year after the effective date of this section to designate their spouse as a survivor beneficiary.

(3) The benefit provided to a child survivor beneficiary under RCW 41.18.040, 41.18.080, and 41.18.100 shall not be affected or reduced by the retired firefighter's selection of the actuarially reduced spousal survivor benefit provided by this section, and shall be equivalent to the amount payable as if the choice under subsection (1) of this section was not made.

(4)(a) Any retired firefighter who chose to receive a reduced retirement allowance under subsection (1) of this section is entitled to receive a retirement allowance adjusted in accordance with (b) of this subsection if:

(i) The retiree's survivor spouse designated in subsection (1) of this section predeceases the retiree; and

(ii) The retiree provides to the board proper proof of the designated beneficiary's death.

(b) The retirement allowance payable to the retiree from the beginning of the month following the date of the beneficiary's death shall be the current monthly amount payable as if the selection under subsection (1) of this section was not made.

Sec. 2. RCW 41.18.080 and 2007 c 218 s 49 are each amended to read as follows:

Any firefighter who has completed his or her probationary period and has been permanently appointed, and sustains a disability not in the performance of his or her duty which renders him or her unable to continue his or her service, may request to be retired by filing a written request with his or her retirement board within sixty days from the date of his or her disability. The board may, upon such request being filed, consult such medical advice as it deems fit and proper. If the board finds the firefighter capable of performing his or her duties, it may refuse to recommend retirement and order the firefighter back to duty. If no request for retirement has been received after the expiration of sixty days from the date of his or her disability, the board may recommend retirement of the firefighter. The board shall give the firefighter a thirty-day written notice of its recommendation, and he or she shall be retired upon expiration of said notice. Upon retirement he or she shall receive a pension equal to fifty percent of his or her basic salary. For a period of ninety days following such disability the firefighter shall receive an allowance from the fund

equal to his or her basic salary. He or she shall during said ninety days be provided with such medical, hospital, and nursing care as the board deems proper. No funds shall be expended for such disability if the board determines that the firefighter was gainfully employed or engaged for compensation in other than fire department duty when the disability occurred, or if such disability was the result of dissipation or abuse. Whenever any firefighter shall die as a result of a disability sustained not in the line of duty, his widow or her widower shall receive a monthly pension equal to one-third of his or her basic salary ((~~until remarried~~)); if such widow or widower has dependent upon her or him for support a child or children of such deceased firefighter, he or she shall receive an additional pension as follows: One child, one-eighth of the deceased's basic salary; two children, one-seventh; three or more children, one-sixth. If there be no widow or widower, monthly payments equal to one-third of the deceased firefighter's basic salary shall be made to his or her child or children. The widow or widower may elect at any time in writing to receive a cash settlement, and if the board after hearing finds it financially beneficial to the pension fund, he or she may receive the sum of five thousand dollars cash in lieu of all future monthly pension payments, and other benefits, including benefits to any child and/or children.

Sec. 3. RCW 41.18.100 and 2007 c 218 s 51 are each amended to read as follows:

In the event a firefighter is killed in the performance of duty, or in the event a firefighter retired on account of service connected disability shall die from any cause, his widow or her widower shall receive a monthly pension under one of the following applicable provisions: (1) If a firefighter is killed in the line of duty his widow or her widower shall receive a monthly pension equal to fifty percent of his or her basic salary at the time of his or her death; (2) if a firefighter who has retired on account of a service connected disability dies, his widow or her widower shall receive a monthly pension equal to the amount of the monthly pension such retired firefighter was receiving at the time of his or her death. If she or he at any time so elects in writing and the board after hearing finds it to be financially beneficial to the pension fund, he or she may

receive in lieu of all future monthly pension and other benefits, including benefits to child or children, the sum of five thousand dollars in cash. If there be no widow or widower at the time of such firefighter's death or upon the widow's or widower's death the monthly pension benefits ((~~hereinabove~~)) provided for under this section shall be paid to and divided among his or her child or children share and share alike, until they reach the age of eighteen or are married, whichever occurs first. ((~~The widow's or widower's monthly pension benefit, including increased benefits to his or her children shall cease if and when he or she remarries: PROVIDED, That no~~)) A pension payable under the provisions of this section shall not be less than that specified under RCW 41.18.200.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/08**	**Z0401.1 / Z-0402.1**

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 throughout the 2008 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 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 impacts the Firemen's Relief and Pensions (FRP) Plans (1955 Act) by providing a new survivor benefit option and allowing certain survivor benefits to continue if the survivor remarries.

The cost for this proposal is indeterminate as we do not have any data to perform a sufficient analysis.

WHAT IS THE PROPOSED CHANGE?

Summary Of Benefit Improvement

This proposal impacts the FRP Plans (1955 Act).

This proposal will create a new actuarially equivalent survivor benefit for spouses who are otherwise ineligible to receive ongoing survivor benefits under the plan. If a member who is married to an ineligible spouse elects this option, the member's retirement allowance will be actuarially reduced. Then, upon the death of the member, the reduced retirement allowance will continue throughout the life of the spouse. The selection of this survivor option will not affect any payments due to child beneficiaries. Members

married to an ineligible spouse prior to the effective date of this proposal will have one year from the effective date of this proposal to designate their spouse as a survivor beneficiary. This new survivor option also provides a “pop-up” provision in the event the designated spouse predeceases the member. This provision would increase the amount of the member’s retirement allowance to the amount the member would have received had the member not selected the option.

This proposal also allows survivor benefits, for members who retired on disability or who died in the line of duty, to continue if the survivor remarries.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

The FRP Plans (1955 Act) provides retirement, disability, and survivor benefits for paid members of a fire department who are actively employed as a fire fighter or a fire dispatcher. The plan closed to new members on March 1, 1970, and the majority of members transferred to the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF). The plan is administered by local governments with benefits paid out of local government funds.

Currently, the plan provides different survivor benefits depending on the circumstances of the member's death. The surviving spouse of a member who is killed in the line of duty receives a survivor pension of fifty percent of the member's basic salary. The surviving spouse of a member who dies while retired for service or for a duty-related disability continues to receive the member's benefit. The surviving spouse of a member who dies from a disability not related to duty receives a survivor pension of one-third of the member's basic salary with additional amounts provided for each child. If there is no surviving spouse, the pension that would otherwise have been payable to the spouse is divided among the eligible children in equal shares.

In order to qualify for survivor benefits, a surviving spouse must have been married to the member at the time of the member’s death in service or disability, or married five years prior to the member’s retirement for service. The survivor benefit paid to a surviving spouse of a member retired for service continues even if the spouse remarries, while in all other cases, the survivor benefits stop if the spouse remarries. Survivor benefits paid to child survivors cease when the child marries or attains the age of eighteen.

Who Is Impacted And How?

We do not have any data to determine the number of members impacted by this bill.

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WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

Some intrinsic costs exist when offering an actuarially equivalent survivor benefit because local governments will have to administer this additional benefit and possibly obtain actuarial services to calculate the actuarially equivalent values.

The cost to continue a survivor pension when the survivor remarries equals the cost of a benefit continuing when otherwise it would have stopped under the current terms of the plan.

Who Will Pay For These Costs

Local governments administer the FRP Plan with benefits and administrative costs paid out of local funds. The benefit improvements do not impact the LEOFF Plans or any other State retirement plans.

HOW WE VALUED THESE COSTS

The provision of an actuarially equivalent survivor benefit for spouses who are otherwise ineligible is cost neutral as far as the benefit provision itself. An actuarially equivalent benefit has the same present value as the benefit it replaces.

The cost to continue a survivor pension when the survivor remarries is essentially the "loss of savings" to the fund that would have occurred without this provision. We do not have any data to support a fiscal cost determination for this part of the proposal.

Based on information provided in HB 3020 during the 2008 Legislative Session, The City of Seattle, with the largest FRP membership, assumes that no surviving spouse will remarry when budgeting for the Plan. They also report that the number of surviving spouses who remarry is very small. This suggests that the impact of this part of the proposal is a small "loss of savings" to the Plan's fund. If, however, this provision was made retroactive, the cost to provide this benefit back many years, plus the administrative work to find the impacted surviving spouses, could be significant.

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ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
2. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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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.

DRAFT

SERS Past Part-Time Service Credit

Description Of Issue

In the past, some SERS members made contributions to the retirement system without receiving service credit. This occurred because contributions were required even if a member did not work enough hours to qualify for service credit. Current rules do not allow for such "non-credited" service.

SERS members have suggested that the current, more generous, service credit rules be retroactively applied to their non-credited past service.

Nearly 4,000 SERS members and over 15,000 members of other systems may have non-credited past service.

Policy Highlights

- Impacts more than SERS.
- The Legislature has dealt with this before (1986 and 1991) and did not change past non-credited service–except for some teachers.
- Differs from other retroactive benefit increases since contributions were already collected.
- A 2008 non-SCPP bill would have given SERS members credit for non-credited past service (HB 3182, no hearing).
- Idaho refunds contributions for non-credited service at retirement.

Policy Options

- **Option 1: Refund Contributions For Non-credited Service.**
  - Does not require a retroactive policy change.
  - Consistent with past legislative actions in not retroactively changing service credit policy.
  - Less generous than granting service credit.
- **Option 2: Apply Current Service Credit Rules To Past Service.**
  - Requires a retroactive policy change.
  - Inconsistent with past legislative actions.

- Ensures that members receive some service credit for any hours worked.
- May be targeted to educational employees only.

❖ **Option 3: Apply Current Half-Time Service Credit Rules To Past Service.**

- Requires a limited retroactive policy change.
- Consistent with an earlier retroactive service credit change provided for teachers.
- Only impacts educational employees working at least half-time.

❖ **Option 4: Take No Action.**

- Generally consistent with approach taken by past legislatures.
- No cost impact.

Committee Activity

Staff briefed the Committee on this issue in June and October. In November, the Committee held a public hearing and took executive action recommending Option 3 to the Legislature.

Recommendation To 2009 Legislature

Grant half-time service to certain Plan 2/3 members who worked at least half-time for an educational employer prior to 1987.

Staff Contact

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SERS Past Part-Time Service Credit

In Brief

ISSUE

In the past, some SERS members have made contributions for work covered by the retirement system without receiving service credit. This occurred because contributions were required even if a member did not work enough hours to qualify for service credit. Current rules do not allow for such "non-credited" service.

Stakeholders are suggesting that the current, more generous service credit rules be retroactively applied to their past service.

MEMBER IMPACT

As of 2008, nearly 4,000 SERS members and over 15,000 members of other systems may have non-credited service.

Darren Painter
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Current Situation

Some members of the School Employees' Retirement System (SERS) who worked prior to January 1, 1987, have made contributions to the retirement system for part-time or partial-month work for which they did not receive any service credit. This occurred because, under the rules in place at that time, contributions were required even if a member did not work enough hours to qualify for service credit. This situation no longer occurs under current rules. *Service for which contributions were made but no service credit granted will be referred to as "non-credited" service throughout this paper.*

How Service Credit Works

Classified (i.e. non-teacher) school employees in retirement-system eligible positions make contributions to the retirement system on their salaries and receive service credit under applicable rules. Service credit is granted on either a monthly or yearly basis. Employees working in positions that are ineligible for retirement system participation (generally temporary or requiring few hours) do not pay any contributions or earn any service credit.

Currently, service credit is earned and contributions are made for any hours worked in an eligible position. Members who do not work enough hours to receive full service credit for the year or month will receive partial service credit for the year or month. Thus, under current rules, some service credit is always earned for periods in which contributions are made. See **Appendix A** for details of current service credit provisions.

How Did This Issue Come About?

The current rules allowing for partial service credit were put into place on September 1, 1991. Prior to that, service credit rules used to grant service credit on an all-or-nothing basis. Members who worked at least 90 hours in a month

received full service credit for the month. Members who worked less than the minimum hours in a month did not receive any service credit for the month at all.

Some members might have made contributions for months in which service credit was not earned, depending on the contribution policy in effect. Prior to January 1, 1987, contributions were paid on all salaries in eligible positions whether or not service credit was earned. Beginning January 1, 1987, contributions were not required for any month in which service credit was not granted.

History

Service credit rules and contribution policies related to part-time and partial-month service credit have changed over time. Two bills are particularly relevant to an understanding of how this issue evolved. There has also been recent legislative activity on this issue.

Background On Service Credit And Contributions

Until 1987, contributions were required whether or not service credit was earned.

Prior to September 1, 1991, partial service credit was generally not provided in Washington State retirement systems.* However, until 1987, members were required to make contributions on salaries earned in an eligible position—whether or not service credit was also earned for the month.

All classified school employees were covered by the Public Employees' Retirement System (PERS) prior to 2000, and their service credit was granted under PERS rules. In 2000, classified school employees in PERS 2 were transferred to SERS. Classified school employees in PERS 1 remained in PERS.

**Except for Plan 1 of the Teachers' Retirement System, which provided partial service credit at that time.*

Contribution Policy Changed In 1987

In 1986, a bill was passed that changed the contribution policy in relation to service credit for PERS, the Teachers' Retirement System (TRS), and the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF). (See Chapter 268, Laws of 1986.) Under the new policy, no

After 1987, contributions weren't required unless service credit was earned.

member or employee contributions were required for any calendar month in which the member did not receive service credit. This change went into effect January 1, 1987, and did not apply to contributions made prior to the effective date. Ultimately, the provision was not administrable due to limitations in the way payrolls were processed.

JCPP Studied Part-Time Employment In 1990

In 1990, the Joint Committee on Pension Policy (JCPP) studied issues related to part-time employment. The JCPP looked at retirement benefits for job-share and other part-time positions as well as current and past contribution requirements for such positions. The JCPP recommended legislation on this topic for the 1991 Session.

Partial Service Credit Rules Established In 1991

In 1991, a version of the JCPP's bill on part-time employment passed the Legislature (Chapter 343, Laws of 1991). This bill made several changes related to service credit including:

In 1991, service credit was granted for all work in an eligible position.

- Setting forth a new legislative retirement policy that persons hired into eligible positions shall earn some service credit for any service rendered.
- Establishing the current structure for granting partial service credit for service rendered <u>after</u> September 1, 1991, in PERS, TRS 2, and LEOFF 2.
- Requiring refunds of contributions paid on and after January 1, 1987, for non-credited service. These refunds were made to members of PERS, TRS 2, and LEOFF 2. (This provision ensured compliance with the earlier contribution policy change.)
- Granting half-time service credit for TRS 2 members who worked under half-time contracts prior to December 31, 1986.

Recent Legislation On This Issue

A non-SCPP bill was introduced in 2008 that would have given SERS members non-credited past service.

During the 2008 Legislative Session, a non-SCPP bill was introduced that dealt with non-credited past service for SERS members. HB 3182 would have allowed active SERS members to receive service credit for any non-credited service in an eligible position prior to September 1, 1987. The bill would allow service credit to be granted for those months based on current service credit rules; no additional contributions would be required. The fiscal note indicated a cost to the system and a rate impact in the current biennium. This bill did not receive a hearing.

Example

Sally is a food service worker for a school district. She worked part-time for the district between 1978 and 1987 before becoming a full-time employee. Sally's part-time position was eligible for participation in the retirement system. During the years that Sally worked part-time, she made contributions to the system on her earnings each month. During some months Sally was not able to work the 90 hours required to receive service credit under the rules in place at that time. For these months, Sally received no service credit but still paid her contributions to the system. These non-credited months were often months with fewer scheduled classroom days such as December, April, and June.

Policy Analysis

Impact On Members

The impact of non-credited service varies based on a couple of factors. One factor is whether members draw a pension from the plan and the other factor is what plan they are in.

Some members receive value from contributions for non-credited service, while others do not.

Non-credited service is not used in the calculation of pensions. Members with non-credited service who receive their contributions back with interest do get added value from contributions made for that service. Included in this group are Plan 3 members, and Plan 2 members who withdraw from the system (hence giving up their rights to a pension). In contrast, Plan 2 members who go on to receive a pension do not get any added value from

contributions for non-credited service. In effect, these Plan 2 members end up paying more for their pension. However, they will still receive back more in pension payments than they paid in contributions. This is because pensions are also paid for by employer contributions and investment earnings.

Other Examples Of Paying Without Adding Value

The previous section explored how Plan 2 members with non-credited past service pay more for their pension without receiving any added value. There are other examples within Washington's retirement systems of members paying without adding value to their retirement benefit.

There are other examples in Washington's systems of members paying without receiving added value.

One example is the recently enacted subsidized early retirement factors for Plans 2/3 members with 30 years of service. All Plan 2 members will pay for this through higher contribution rates. However, some members will never be able to take advantage of the new factors because they won't earn the required service prior to age 65.

Service credit rules provide another example. Members who work more than the minimum number of hours required for full service credit effectively pay extra for their service. They pay contributions on all hours worked over the minimum but receive no additional service credit.

To illustrate, consider two SERS members. One member works 90 hours in a month, the other works 160 hours. Both members contribute for all hours worked and both members receive exactly one month of service credit. Salary considerations aside, the member who worked 160 hours will not receive any extra pension value for the contributions made for hours worked over 90.

Other Washington Plans

Over 15,000 non-SERS members might have non-credited past service.

The Department of Retirement Systems estimates that, as of April 2008, over 15,000 members of the state's other retirement systems might have non-credited past service. This includes both active and inactive, non-retired members.

Members of PERS, TRS 2, and LEOFF 2 who worked prior to January 1, 1987, might have contributed to the retirement

system during months in which they did not work enough hours to earn service credit. PERS members are the most likely to be impacted since there are more part-time positions in PERS than the other systems. (Note: Impacted Plan 2 members of PERS and TRS may have since transferred to Plan 3.)

Current and future members of LEOFF Plan 1 and the Washington State Patrol Retirement System (WSPRS) might be impacted as well. LEOFF Plan 1 and WSPRS do not provide partial service credit. Members in these plans who work less than 70 hours a month in an eligible position do not receive any service credit for the month. However, they are still required to make contributions for the month. Since these plans are only open to full-time employees, members are most likely impacted if they are hired near the end of a month or leave near the beginning.

While this issue may impact members of other systems, only SERS members are seeking a solution at this time.

Other States

Idaho refunds contributions for non-credited service.

Idaho is the only one of ten Washington peer states in which classified school employees might be required to make contributions to a defined benefit plan without earning service credit.* However, any contributions made for non-credited service are refunded to the member with interest when they withdraw or retire from the system. Members who retire receive the refunded contributions in addition to their service-based pension. Generally, only members who withdraw from the system can have their contributions refunded (as with Plans 1/2 of Washington's systems).

**As of June, 2008.*

Implications Of Retroactive Policy Changes

This issue illustrates what often happens when retirement policy is changed midstream. Inconsistencies might be created in benefits among various generations of workers. Consequently, members may seek to have the more favorable policy applied to past service. In this instance, members are suggesting that the current, more generous, service credit rules be applied to service rendered prior to

when the rules were adopted. Changes applied to past service are often referred to as retroactive changes.

What happens when a benefit change is retroactively applied? In most cases, the cost of the improvement is spread to future workers and taxpayers since the benefit was not funded when it was earned. However, this issue differs in that contributions were collected while the member was working, but no additional pension benefit was provided.

It could be claimed that non-credited past service has already been paid for.

While it could be claimed that members and taxpayers have already paid for the cost of the non-credited past service, there is still a cost to grant this service today. This is because the retirement system has already realized a gain for non-credited service. (The system "gains" when contributions are collected but no pension benefit is provided.) There will be a cost to the retirement system if the prior gains realized for non-credited service are given back in new benefit improvements.

Legislative Precedent On Non-Credited Past Service

With one exception, the Legislature has chosen to not retroactively apply a solution.

At least twice, the Legislature has had the opportunity to address the issue of non-credited past service. With one limited exception, the Legislature has chosen to not retroactively apply a solution. One opportunity was in 1986 when the Legislature established the policy that contributions were not required when service credit was not granted. At that time, the Legislature did not require a refund of contributions for past non-credited service. A second opportunity occurred in 1991 when the Legislature established the policy that persons hired into eligible positions shall earn service credit for all service rendered. The resulting new service credit rules were not applied to prior service. (The Legislature created a special service credit rule applied retroactively applied to half-time teachers.)

Why Not Make Policy Changes Retroactive?

There are many reasons that policy makers may not apply a policy change retroactively. It might be a matter of practicality: it costs too much or is too difficult to administer. Policy makers may also be concerned about

maintaining fairness across generations by not shifting costs to future generations (less of an issue with non-credited service). Another reason is that policy makers may wish to support the flexibility of the retirement systems. Requiring every policy change to apply retroactively might hamper the ability of policy makers to adapt retirement systems to changing circumstances.

Implications For Recent SCPP Work On Service Credit

Retroactive changes for non-credited past service may lead to calls for the recent TRS and SERS half-year contract changes to be applied retroactively as well. In 2007, the SCPP recommended new, more generous service credit rules for teachers and school employees working half-year contracts. The changes that were recommended by the SCPP and passed by the Legislature did not apply to prior service.

Policy Implications Of HB 3182

HB 3182 requires a retroactive application of service credit rules and only applies to SERS.

HB 3182 is a non-SCPP bill introduced in 2008 that addresses the issue of non-credited past service. (Refer to the **History** section of this paper for a more complete description.) This bill requires a retroactive application of current service credit rules and only applies to active SERS members. The earlier discussion of the policy implications of retroactive changes and impacts on other Washington retirement systems apply to HB 3182.

Also, there is likely a technical problem with the date used in the bill draft for granting non-credited past service. The date used in the bill (September 1, 1987), falls after the date when contributions for non-credited service were refunded (January 1, 1987).

Conclusion

The issue of non-credited past service has implications around retroactive policy changes and equity across systems. It also raises questions about charging members without providing additional value in retirement benefits. The issue was first identified many years ago and the Legislature has had opportunities to address it. A bill was

introduced in 2008 that proposes one possible solution for some impacted members. The state of Idaho found a different way to address non-credited service. SCPP members may wish to consider both these and other options in response to this issue.

Policy Options

The way policy makers respond to this issue will likely depend upon how they view the issue. Policy makers may view this in one of two ways:

Policy makers may view this issue in one of two ways.

- As a contribution policy issue.
- As a service credit issue.

Policy makers who view this as a contribution policy issue may be more inclined to consider refund options. Policy makers who view this as a service credit issue may be more inclined to consider options that grant additional service credit. No matter what their view, some policy makers may be inclined to take no action on this issue for various policy reasons.

Policy options for each view are discussed below. These options are not necessarily mutually exclusive. Policy makers may elect to provide a combination of options that grant refunds in some cases and grant service credit in others.

Service credit options are limited to those that retroactively apply current service credit rules to periods of past service. Other service credit approaches touch on the fundamental policies of how service credit should be awarded. This is a much larger issue with potentially greater impacts and very different policy considerations.

The policy options apply to a broader group of members than just SERS.

This issue was originally brought before the Legislature as a SERS issue. Subsequent research by staff revealed that non-credited service impacts members of most Washington plans. The policy options provided are designed to apply to a broader group of members than just SERS.

Preliminary pricing for each of the policy options was provided at the October meeting.

Option1: Refund Contributions For Non-Credited Service

This option provides a refund of contributions with interest at retirement for members who made contributions for a month in which they did not receive any service credit.

This option does not require a retroactive policy change, which is consistent with past legislative actions.

This option has several broad policy implications. It does not require a retroactive policy change, which is consistent with past legislative actions. This option ensures that members will receive some benefit for all contributions made—though refunds are less generous to members than granting additional service credit. In addition to taking care of past, non-credited service, this option would address future non-credited service in those plans where it may still occur—without opening up the issue of service credit in general. This option will not lead to earlier retirements because it does not impact service credit. This option is relatively easy to administer and refunds would be provided without requiring the member to separately apply or provide proof of hours worked.

This option impacts Plan 1 and Plan 2 members of PERS, TRS, SERS, LEOFF, and WSPRS. Plan 3 members currently receive their contributions with interest if they retire. Other systems are not impacted by non-credited service.

Option 2: Apply Current Service Credit Rules To Past Service

This option retroactively applies current service credit rules to periods of service prior to January 1, 1987, similar to the 2008 Legislation (HB 3182).

This option requires a retroactive policy change and is a departure from past legislative actions.

This option has several broad policy implications. It requires a retroactive policy change by applying current service credit policy to periods of past service rendered under different policy. This is a departure from the actions of past Legislatures that generally didn't choose to retroactively apply service credit rules. (See the **Policy Analysis** section for a more thorough discussion of retroactive policy changes.) This option is the most generous to members. It ensures that members receive some service credit for any hours worked. This option may lead to earlier retirements

since it increases service credit and service credit is a factor in the ability to access improved retirement benefits.

Service credit may be granted for all non-credited service, or limited to non-credited service with an educational employer. One policy reason for limiting it to educational employment is that part-time educational employees may have been disadvantaged due to the nature of educational employment. During some months, part-time educational employees may not have been able to work enough hours to earn service credit under the past rules because schools were closed for holidays and other breaks.

This option would only apply to PERS, TRS 2/3, SERS, and LEOFF 2. These are the only plans where service credit policy was changed to address non-credited service.

Option 3: Apply Current Half-Time Service Credit Rules To Past Service

This option is similar to Option 2 except that it retroactively applies only the current *half-time* service credit rules for educational employees to periods of past educational service.

This option allows members who worked for an educational employer prior to January 1, 1987, to receive six months of service credit if they worked at least 630 hours during a full school year.

This option is consistent with an earlier retroactive service credit change provided for teachers.

This option is consistent with a retroactive service credit change that was provided for half-time teachers in 1991 (see **History** section). In other respects, this option has broad policy implications similar to Option 2. This option is less generous than Option 2 since it only impacts members who were working at least half-time. Members working less than half-time will not benefit under this option.

This option would only apply to members in PERS Plans 2/3 and SERS Plans 2/3. Half-time service credit rules only apply to Plans 2/3 educational employees. Non-credited past service for half-time teachers was addressed in 1991.

Policy makers may choose to take no action for a variety of reasons.

Option 4: Take No Action

Policy makers who view this as a service credit issue may choose to take no action if they want to avoid retroactive policy changes or are not overly concerned that prior service credit rules were not as generous as they could have been.

Policy makers who view this as a contribution issue may choose to take no action for a couple of reasons related to the underlying plan design:

- The benefits in a Defined Benefit (DB) plan like the Plans 1 and Plans 2 are not determined by the contributions made.
- It is not uncommon in a DB plan for members to pay additional contributions without adding additional value to their retirement benefits.

This option has no cost impact and is consistent with the general approach taken by the Legislature in the past.

Committee Activity

Staff first briefed the Committee on this issue at the June meeting. The Executive Committee of the SCPP directed staff to develop new policy options—including Option 3—and bring those options back to the full SCPP with pricing.

Staff briefed the Committee on the policy options at the October meeting. Following, the Executive Committee recommended that the full SCPP consider Option 3 for possible executive action at the November meeting.

The Committee held a public hearing and took executive action on this issue in November recommending Option 3 to the Legislature.

Executive Committee Recommendation

Option 3: Apply current half-time rules to past service. Recommended October 21, 2008.

Recommendation To 2009 Legislature

Grant half-time service to certain Plan 2/3 members who worked at least half-time for an educational employer prior to 1987. Recommended November 18, 2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0284.1/09).

Draft Fiscal Note

Attached.

Stakeholder Input

Correspondence on file from:

Carey Ensign, (e-mail and related attachment), 1/29/2008.

Appendix A
Service Credit Rules

Plans 2/3 Service Credit Rules

Educational Employees

Plan 2/3 members working for an educational employer (includes all SERS, all TRS, and some PERS members) earn service credit as follows*:

- At least 810 hours worked in a full school year = 12 months of service credit.
- At least 630 hours but less than 810 hours worked in a full school year = 6 months of service credit.
- At least 630 or more hours worked in five months of a six month period within a school year = 6 months of service credit.

Educational employees who work less than a full school year or less than 630 hours earn service credit on a month by month basis as described for non-educational employees.

Non-Educational Employees

Plans 2/3 members working for non-educational employers (includes PERS and LEOFF) earn service credit on a month by month basis as follows:

- 90 hours or more in a month = 1 month of service credit.
- At least 70, but less than 90 hours in a month = ½ month of service credit.
- Less than 70 hours in a month = ¼ month of service credit.

**Note: Members are awarded service credit under whichever rule provides the most service credit.*

PERS Plan 1 Service Credit Rules

Educational Employees

PERS 1 members working for an educational employer earn one year of service credit if they work at least 630 hours in a full school year.

Non-Educational Employees

PERS 1 members working for non-educational employers receive service credit on a month-by-month basis as follows:

- 70 hours or more in a month = 1 month of service credit.
- Less than 70 hours in a month = ¼ month of service credit.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0284.1/09

ATTY/TYPIST: LL:lel

BRIEF DESCRIPTION: Granting half-time service credit for half-time educational employment prior to January 1, 1987, in plans 2 and 3 of the school employees' retirement system and the public employees' retirement system.

AN ACT Relating to granting half-time service credit for half-time educational employment prior to January 1, 1987, in plans 2 and 3 of the school employees' retirement system and the public employees' retirement system; adding a new section to chapter 41.35 RCW; and adding a new section to chapter 41.40 RCW.

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

NEW SECTION. **Sec. 1.** A new section is added to chapter 41.35 RCW under the subchapter heading "provisions applicable to plan 2 and plan 3" to read as follows:

(1) By no later than December 31, 2010, the department shall recalculate service credit for periods of qualifying prior service by an eligible member, as provided for in this section.

(2) An eligible member is a member who is active in the retirement system and who earns service credit after the effective date of this section and before September 1, 2010.

(3) A qualifying period of prior service is a school year prior to January 1, 1987, in which the member:

(a) Was employed in an eligible position by a school district or

districts, educational service district, the state school for the deaf, the state school for the blind, an institution of higher education, or a community college;

(b) Earned earnable compensation for at least six hundred thirty hours as determined by the department;

(c) Received less than six months of service credit; and

(d) Has not withdrawn service credit for the school year or has restored any withdrawn service credit for the school year.

(4) The department shall recalculate service credit for qualifying periods of prior service for an eligible member as follows:

(a) The member shall receive one-half service credit month for each month of the period from September through August of the following year if he or she earned earnable compensation during that period for at least six hundred thirty hours as determined by the department, and was employed nine months of that period; and

(b) A member's service credit shall not be reduced under this section for a qualifying period of prior service.

NEW SECTION. **Sec. 2.** A new section is added to chapter 41.40 RCW under the subchapter heading "provisions applicable to plan 2 and plan 3" to read as follows:

(1) By no later than December 31, 2010, the department shall recalculate service credit for periods of qualifying prior service by an eligible member, as provided for in this section.

(2) An eligible member is a member of plan 2 or 3 who is active in the retirement system and who earns service credit after the effective date of this section and before September 1, 2010.

(3) A qualifying period of prior service is a school year prior to January 1, 1987, in which the member:

(a) Was employed in an eligible position by a school district or districts, educational service district, the state school for the deaf, the state school for the blind, an institution of higher education, or a community college;

(b) Earned earnable compensation for at least six hundred thirty hours as determined by the department;

(c) Received less than six months of service credit; and

(d) Has not withdrawn service credit for the school year or has restored any withdrawn service credit for the school year.

(4) The department shall recalculate service credit for qualifying periods of prior service for an eligible member as follows:

(a) The member shall receive one-half service credit month for each month of the period from September through August of the following year if he or she earned earnable compensation during that period for at least six hundred thirty hours as determined by the department, and was employed nine months of that period; and

(b) A member's service credit shall not be reduced under this section for a qualifying period of prior service.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/08**	**Z-0284.1 / Z-0404.11**

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, throughout the 2008 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 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 grants half-time service credit to certain Plan 2/3 members who worked half-time for an educational employer during school years prior to January 1, 1987.

Impact on Pension Liability

(Dollars in Millions)	Current	Increase	Total
Today's Value of All Future Pensions	$67,081	$0.2	$67,081
Earned Pensions Not Covered by Today's Assets	$4,957	$0.0	$4,957

Impact on Contribution Rates: (Effective 09/01/2009)

2009-2011 State Budget	PERS	SERS
Employee (Plan 2)	0.00%	0.00%
Employer:		
Current Annual Cost	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%
Total	0.00%	0.00%

Budget Impacts

(Dollars in Millions)	2009-2011	2011-2013	25-Year
General Fund-State	$0.0	$0.0	$0.1
Total Employer	$0.0	$0.0	$0.4

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

WHAT IS THE PROPOSED CHANGE?

Summary of Change

This proposal impacts the following systems:

- Public Employees' Retirement System (PERS) Plans 2/3
- School Employees' Retirement System (SERS) Plans 2/3

This proposal grants half-time service credit to certain PERS and SERS Plan 2/3 members who worked half-time for an educational employer during school years prior to January 1, 1987.

This proposal requires the Department of Retirement Systems (DRS) to recalculate service credit for periods of qualifying prior service by an eligible member. An eligible member is a Plan 2/3 member who is active in the retirement system and earns service credit after the effective date of the bill and before September 1, 2010. A qualifying period of prior service is a school year prior to January 1, 1987, in which the member:

- Was employed in an eligible position by one of the following employers: school districts, educational service districts, the state school for the deaf, the state school for the blind, institutions of higher education, or community colleges.
- Worked at least 630 hours.
- Received less than six months of service credit.
- Has not withdrawn service or has restored any withdrawn service.

Effective Date: 90 days after session

What Is The Current Situation?

Currently, Plan 2/3 members who work for an educational employer earn service credit as follows:

- At least 810 hours worked in a full school year = 12 months of service.
- At least 630 but less than 810 hours worked in a full school year = 6 months of service.
- At least 630 hours worked in five months of a six month period within a school year = 6 months of service.

Working less than a full school year or less than 630 hours: service credit is calculated on a month to month basis as follows:

- 90 hours or more in a month = 1 month of service.
- At least 70 but less than 90 hours in a month = ½ month of service.
- Less than 70 hours in a month = ¼ month of service.

Prior to January 1, 1987, Plan 2/3 members who worked for educational employers received 12 months of service credit if they were continuously employed for 9 months and worked at least 90 hours a month in at least 9 months of the school year. If they did not qualify to receive 12 months of service credit, they received 1 service credit month for each month of 90 hours worked. No service was awarded for any month of less than 90 hours. Members and employers made retirement contributions on all salary, regardless of the amount of service credit earned, if any.

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Who Is Impacted And How?

We estimate this proposal could affect 192 active and vested terminated members out of the total 227,473 active and vested terminated members of these systems through improved benefits. Furthermore, we expect 132 active members will actually receive improved benefits.

We estimate this proposal will increase the benefits for a typical member by providing an increased retirement benefit to current active members. The average member affected by this proposal has a salary of $30,000 and will receive 0.25 years of additional service. This will increase their initial unreduced retirement benefit by $150 per year.

This proposal impacts all 138,392 active Plan 2 members of these systems through increased contribution rates. This proposal will not affect member contribution rates in Plan 3 since Plan 3 members do not contribute to their employer-provided defined benefit.

See Appendix A of this draft fiscal note for more details on members impacted.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This proposal has a cost since it allows active educational employees of PERS and SERS Plans 2/3 to have periods of half-time service credit earned prior to January 1, 1987, credited to their retirement account. This will increase their retirement benefit by the additional service provided under this proposal.

Who Will Pay For These Costs?

The affected members, who did not receive the half-time service credit prior to January 1, 1987, made contributions commensurate with the effective contribution rate. Therefore, these individuals already made the appropriate contributions. The entire system will provide for any additional costs through increased contribution rates.

HOW WE VALUED THESE COSTS

Assumptions We Made

We assumed all 132 current active members will receive the increase in service credit as provided under this proposal. Please see the Sensitivity Analysis section for how the results change when vested terminated members receive the increase in service credit.

Otherwise, we developed these costs using the same assumptions as disclosed in the June 30, 2007 Actuarial Valuation Report (AVR).

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How We Applied These Assumptions

DRS identified the affected members in their database and provided the information to us. We isolated these members in our valuation data and increased their service by the additional service credits provided by DRS. The resulting change in service provides the source of the increase in actuarial liabilities, contribution rates, and fiscal costs.

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

We used the Aggregate actuarial funding method to determine the fiscal budget changes for current plan members.

Special Data Needed

DRS provided special data for this proposal. The data indicated the number of months of service credit members received prior to January 1, 1987, under the half-time service credit rules at that time. The data also provided the number of months of service credit members would have received for the same period of service under the current half-time service credit rules.

For more detail please see Appendix A.

ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of PERS and SERS Plans 2/3 by increasing the present value of future benefits payable under the systems 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)			
PERS 2/3	**$20,634**	**$0.0**	**$20,635**
SERS 2/3	**$2,698**	**$0.2**	**$2,698**
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)			
PERS 2/3	**($2,470)**	**$0.0**	**($2,470)**
SERS 2/3	**($443)**	**$0.2**	**($443)**

Note: Totals may not agree due to rounding.

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How The Present Value of Future Salaries (PVFS) Changed

This proposal will impact the actuarial funding of PERS and SERS Plans 2/3 by decreasing the PVFS of the members of the systems as shown below.

Present Value of Future Salaries			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Future Salaries			
(The Value of the Future Salaries Expected to be Paid to Current Members)			
PERS 2	$56,420	$0.0	$56,420
PERS 3	11,717	0.0	11,717
PERS 2/3	**$68,137**	**$0.0**	**$68,137**
SERS 2	$3,837	$0.0	$3,837
SERS 3	7,153	0.0	7,153
SERS 2/3	**$10,990**	**$0.0**	**$10,990**

Note: Totals may not agree due to rounding.

How Contribution Rates Changed

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01%, therefore the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate increase to measure the fiscal budget changes in future biennia.

Impact on Contribution Rates: (Effective 09/01/2009)

System/Plan	PERS	SERS
Current Members		
Employee (Plan 2)	0.000%	0.001%
Employer:		
Normal Cost	0.000%	0.001%
Plan 1 UAAL	0.000%	0.000%
Total	0.000%	0.001%

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How This Impacts Budgets And Employees

Budget Impacts			
(Dollars in Millions)	**PERS**	**SERS**	**Total**
2009-2011			
General Fund	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**
2011-2013			
General Fund	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**
2009-2034			
General Fund	$0.0	$0.1	$0.1
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.1**	**0.2**
Local Government	0.0	0.2	0.2
Total Employer	**0.1**	**0.3**	**0.4**
Total Employee	**$0.1**	**$0.1**	**$0.2**

Note: Totals may not agree due to rounding.

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

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

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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 assumption:

- The number of members who will receive the increased benefits.

Currently this proposal provides increased benefits to active members who earn service after the effective date of this proposal and before the end of the 2010 school year. We priced this proposal assuming all 132 current active members will receive the service credit. However, the actual number of members may differ. Current active members may choose to retire or terminate from active service before they become eligible to receive the increase in service credit, and current vested terminated members may choose to return to work and would then qualify to receive the increase in service credit. A decrease in the number of members eligible to receive this service credit would decrease the liabilities and associated budget costs compared to the proposal.

The following tables show the impact if:

- Current active members receive the increase in service as assumed ("Proposal").
- Current active and vested terminated members receive the increase in service ("All").

Members Impacted

All Systems	Proposal	All
Number of Members Affected	132	192
Increase in Service (Years)	37.84	57.09

Impact on Pension Liability - All Systems

(Dollars in Millions)	Proposal	All
Today's Value of All Future Pensions	$0.2	$0.3
Earned Pensions Not Covered by Today's Assets	$0.0	$0.0

Budget Impacts - All Systems

(Dollars in Millions)	Proposal	All
2009-2011		
General Fund - State	$0.0	$0.0
Total Employer	0.0	0.0
2011-2013		
General Fund - State	0.0	0.0
Total Employer	0.0	0.0
2009-2034		
General Fund - State	0.1	0.2
Total Employer	$0.4	$0.5

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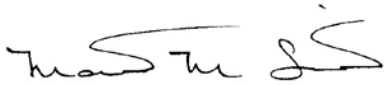
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost 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. This draft fiscal note is based upon data provided by the Department of Retirement Systems (DRS). An audit of the data was not performed. I relied on the data provided as complete and accurate for the purposes of this pricing exercise.
4. Use of another set of methods, assumptions, and data may also be reasonable, and might produce different results.
5. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
6. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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APPENDIX A – SPECIAL DATA NEEDED

DRS provided the unaudited data for this proposal. The data contained 212 records, with the current service credited under the old rules and the new service credited based on DRS' understanding and application of this proposal. The difference between the new service credited and the current service credited equals the additional service amount the member would receive under this proposal.

We matched the records provided with our valuation file. Only 192 of the 212 records are active (132) or terminated vested (60) members of the retirement system as of our last valuation, June 30, 2007. For each matched record, we increased their total service by the additional service amount provided by DRS.

The following table summarizes the active member data we used for this proposal.

	PERS 2/3			SERS 2/3		
Year of Hire	**Number of Members**	**Total Additional Service**	**Average Additional Service**	**Number of Members**	**Total Additional Service**	**Average Additional Service**
1977	1	0.08	0.08	1	0.33	0.33
1978	4	1.17	0.29	19	10.08	0.53
1979	2	0.33	0.17	31	8.08	0.26
1980	4	0.92	0.23	16	5.17	0.32
1981	1	0.08	0.08	9	2.17	0.24
1982	1	0.25	0.25	12	2.67	0.22
1983	2	0.42	0.21	14	2.67	0.19
1984	2	0.58	0.29	5	1.08	0.22
1985	1	0.17	0.17	5	0.92	0.18
1986	1	0.17	0.17	0	0.00	0.00
1987	1	0.50	0.50	0	0.00	0.00
Total	**20**	**4.67**	**0.23**	**112**	**33.17**	**0.30**

Otherwise, we developed these costs using the same assets and data as disclosed in the Actuarial Valuation Report (AVR).

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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.

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Survivors Of PERS 1 Inactives

Description Of Issue

The Public Employees' Retirement System (PERS) Plan 1 does not provide a survivor annuity for *inactive* members who die prior to retirement—even if the member was eligible for a pension at the time of death. In contrast, the plan does provide a survivor annuity for *active* members who die prior to retirement.

Policy Highlights

- Current policy views active members who die as early retirements, while inactive members who die are viewed as withdrawals from the plan.
- Differences in pre-retirement death benefits for active and inactive members may be an oversight or a deliberate policy decision.
- All other comparable Washington State plans provide the same pre-retirement death benefits for both active and inactive members.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 session to provide the same pre-retirement survivor annuity for inactive members as is provided for active members (HB 3006/SB 6652). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways & Means.

The Committee held a public hearing and took executive action on this issue in May of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 session.

Recommendation To 2009 Legislature

Provide the same pre-retirement survivor annuity for inactive members as for active members in the Public Employees' Retirement System (PERS) Plan 1.

Staff Contact

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Survivors of PERS 1 Inactives

In Brief

ISSUE

PERS 1 provides different pre-retirement death benefits for inactive members than for active members. PERS 1 is the only Washington State plan with service-based survivor benefits that makes such a distinction.

Survivor annuities are provided for PERS 1 members who die prior to retirement while in active service. Once a member leaves active service, however, the only benefit available to the survivor is a refund of accumulated contributions – even if the member was eligible to collect a retirement pension at the time of death.

MEMBER IMPACT

There are 2,675 PERS 1 terminated vested members. Of these, at least 200 are eligible for immediate retirement.

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Current Situation

The pre-retirement death benefits provided for Public Employees' Retirement System Plan 1 (PERS 1) members differ depending on whether the member was active or inactive at the time of death.

Survivors of active PERS 1 members who die prior to retirement may generally choose between a refund of the member's accumulated contributions or a survivor annuity. To qualify for the survivor annuity, the member must have been eligible for retirement or had ten or more years of service at the time of death. The survivor annuity is calculated as if the member chose to retire and elected a joint and 100 percent survivorship option. The annuity is actuarially reduced for the difference between the age when the member would have qualified for a service retirement and the age of death.

In contrast, survivors of PERS 1 members who die after leaving service but prior to retirement only receive a refund of the member's accumulated contributions.* The survivor is not allowed to receive a continuing survivor benefit – even if the member was eligible for retirement at the time of death.

**Accumulated contributions include interest.*

Example

Example 1: Short career, long absence

A PERS 1 member leaves service after ten years. The member does not withdraw their contributions and becomes a terminated vested member. Twenty years later the member dies.

Example 2: Full career, short absence

A PERS 1 member leaves service after thirty years. The member is eligible to retire, but chooses to defer retirement for tax purposes. Three months

after separating from service, and before applying for retirement, the member dies.

A survivor annuity is often more valuable than a return of contributions.

In both cases, the survivor only receives a refund of the member's accumulated contributions. Had the member been in active service at the time of death, the survivor would have been allowed to receive a survivor annuity based on the member's earned pension. In the case of the member who was retirement eligible at the time of death, the survivor annuity would be worth far more than the refund of the member's contributions.

Policy Analysis

The current policy for pre-retirement death benefits in PERS 1 takes different views of death prior to retirement based on the employment status of the member. Members who die while in service are viewed as early retirements while members who die after leaving service are viewed as withdrawals from membership. Being treated as a withdrawn member means the employer-funded portion of the member's retirement benefit is forfeited. Such a policy runs counter to the basic earned benefit design of the PERS system. Under an earned benefit design, a member receives the value of the benefit they have accrued or "earned" based on the service rendered. Under current policy, members who leave employment and become vested after long careers lose much of the value of the service they have rendered if they die prior to retirement.

Active members who die are viewed as early retirements while inactive members are viewed as withdrawals.

Providing lesser benefits for members who leave active service may be seen as a way to encourage members to remain active in the system until retirement. This is more of a "golden-handcuffs" approach to pension plan design that places less emphasis on member flexibility in changing careers.

The practice of providing different pre-retirement death benefits to members who die in active service as opposed to members who die after leaving service is inconsistent with the practice in other Washington plans that provide service-based survivor benefits.

Reasons For Differences

The PERS 1 differences in pre-retirement death benefits for active and inactive members may be the result of an oversight or a deliberate policy decision.

Differences may be an oversight or a deliberate policy decision.

When PERS 1 was first created, it did not provide a vested retirement benefit to members who separated from service prior to retirement. When the vested benefit was later added, the survivor benefit for vested members may have been overlooked.

Policy reasons for providing different and less generous benefits for members who leave active service include:

- Encouraging members to stay active in the plan until retirement.
- Reducing costs.
- Lack of a perceived need to provide survivor benefits on behalf of members who left the system.

Other Washington State Plans

Other plans provide the same benefits for both active and inactive members.

PERS 1 is unique among Washington plans providing service-based survivor benefits in that it differentiates between active and inactive members for purposes of pre-retirement death benefits. In contrast, the Plans 2/3 and the Teachers' Retirement System Plan 1 (TRS 1) do not differentiate between active and inactive members. These plans provide the same pre-retirement death benefits for active and inactive members: Survivors of eligible members in these plans, whether active or inactive at time of death, may choose between a survivor annuity or a refund of the member's accumulated contributions.

Comparative Systems*

The comparative systems are split on the policy of differentiating between active and inactive members.

Washington's comparative systems are split on the policy of differentiating between active and inactive members for pre-retirement death benefits. Among the systems covering general government employees, six distinguish between active and inactive members for the purpose of providing pre-retirement death benefits and five do not. Oregon, Wisconsin, Ohio, Florida, Colorado, and California provide different pre-retirement death benefits for inactive

members than for active members. Generally, these systems provide a refund of member contributions for inactive members while providing a survivor annuity or an additional employer match of member contributions for active members. Seattle, Minnesota, Missouri, Idaho, and Iowa provide the same pre-retirement death benefits for both active and inactive members. California and Ohio treat members who have separated within a specified timeframe as active for purposes of receiving the pre-retirement death benefits: four months in California, and thirty months in Ohio.

**Information on comparative systems is based on research conducted in August of 2007.*

Policy Questions

Policy makers may wish to consider the following questions when deliberating on this issue:

- Should the same pre-retirement death benefits be provided for inactive PERS 1 members that are provided for active PERS 1 members (choice of annuity or refund of contributions)?
- Should the same eligibility criteria for a survivor annuity apply to both inactive members and active members (retirement eligible or ten or more years of service at time of death)?

Implications Of Changes To Current Policy

Providing the same pre-retirement death benefits for active and inactive members is consistent with the approach in other Washington plans.

Providing the same pre-retirement death benefits and eligibility for inactive members as for active members is consistent with the earned benefit design and with the approach taken in the Plans 2/3 and TRS 1.

Providing different eligibility criteria for inactive members may lower costs and could be used to target the improvement to those survivors most adversely affected by the current policy. For example, the survivor annuity could be limited to inactive members who were retirement eligible at the time of death or who had worked substantial careers before leaving service. These members generally lose the most by not having an annuity option available. However, any time a line is drawn, some members will fall outside of it. This may lead to calls for additional

expansions later (i.e., an inactive member dies one day prior to retirement eligibility).

Benefit improvements are unlikely to be fully funded over the working lives of members.

Changing current policy regarding pre-retirement death benefits in PERS 1 may have funding policy implications as well. Since PERS 1 is a closed plan and most members are near the end of their working careers, any benefit improvements are unlikely to be funded over the working lifetime of the current members. This is inconsistent with the current statutory funding policy goal of intergenerational equity. Intergenerational equity calls for benefit improvements to be funded over the working lives of the members receiving the benefits so that the costs of those benefits are paid for by the taxpayers who receive the benefit of the members' services.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 Session to provide the same pre-retirement survivor annuity for inactive members as is provided for active members (HB 3006/SB 6652). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways & Means.

The Committee held a public hearing and took executive action on this issue in May of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 Session.

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

Provide the same pre-retirement survivor annuity for inactive members as for active members in the Public Employees' Retirement System (PERS) Plan 1. Recommended May 13, 2008.

Bill Draft

A Code Reviser bill draft implementing the SCPP recommendation is attached (Z-0069.1/09).

Draft Fiscal Note

Attached.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0069.1/09

ATTY/TYPIST: LL:cro

BRIEF DESCRIPTION: Extending the survivor annuity option for preretirement death in plan 1 of the public employees' retirement system to members who die after leaving active service.

AN ACT Relating to extending the survivor annuity option for preretirement death in plan 1 of the public employees' retirement system to members who die after leaving active service; and amending RCW 41.40.270.

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

Sec. 1. RCW 41.40.270 and 2003 c 155 s 6 are each amended to read as follows:

(1) Except as specified in subsection (4) of this section, should a member die before the date of retirement the amount of the accumulated contributions standing to the member's credit in the employees' savings fund, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, at the time of death:

(a) Shall be paid to the member's estate, or such person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there be no such designated person or persons still living at the time of the member's death, or if a member fails to file a new beneficiary designation subsequent to marriage, remarriage, dissolution

of marriage, divorce, or reestablishment of membership following termination by withdrawal or retirement, such accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the surviving spouse as if in fact such spouse had been nominated by written designation as aforesaid, or if there be no such surviving spouse, then to the member's legal representatives.

(2) Upon the death ((~~in service, or while on authorized leave of absence for a period not to exceed one hundred and twenty days from the date of payroll separation,~~)) of any member who is qualified but has not applied for a service retirement allowance or has completed ten years of service at the time of death, the designated beneficiary, or the surviving spouse as provided in subsection (1) of this section, may elect to waive the payment provided by subsection (1) of this section. Upon such an election, a joint and one hundred percent survivor option under RCW 41.40.188, calculated under the retirement allowance described in RCW 41.40.185 or 41.40.190, whichever is greater, actuarially reduced, except under subsection (5) of this section, by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 shall automatically be given effect as if selected for the benefit of the designated beneficiary. If the member is not then qualified for a service retirement allowance, such benefit shall be based upon the actuarial equivalent of the sum necessary to pay the accrued regular retirement allowance commencing when the deceased member would have first qualified for a service retirement allowance.

(3) Subsection (1) of this section, unless elected, shall not apply to any member who has applied for service retirement in RCW 41.40.180, as now or hereafter amended, and thereafter dies between the date of separation from service and the member's effective retirement date, where the member has selected a survivorship option under RCW 41.40.188. In those cases the beneficiary named in the member's final application for service retirement may elect to receive either a cash refund, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed

under RCW 41.50.670, or monthly payments according to the option selected by the member.

(4) If a member dies within sixty days following application for disability retirement under RCW 41.40.230, the beneficiary named in the application may elect to receive the benefit provided by:

(a) This section; or

(b) RCW 41.40.235, according to the option chosen under RCW 41.40.188 in the disability application.

(5) The retirement allowance of a member who is killed in the course of employment, as determined by the director of the department of labor and industries, is not subject to an actuarial reduction. The member's retirement allowance is computed under RCW 41.40.185.

--- END ---

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ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/31/08**	**Z-0069.1 / Z-0403.1**

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 throughout the 2008 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 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 impacts the Public Employees' Retirement System (PERS) Plan 1 by providing an optional survivor annuity for certain inactive members who die prior to retirement.

Impact on Pension Liability

(Dollars in Millions)	Current	Increase	Total
Today's Value of All Future Pensions	$14,061	$0.6	$14,062
Earned Pensions Not Covered by Today's Assets	$3,609	$0.6	$3,609

Impact on Contribution Rates: (Effective 09/01/2009)

2009-2011 State Budget	PERS	SERS	PSERS
Employee (Plan 2)	0.00%	0.00%	0.00%
Employer:			
Current Annual Cost	0.00%	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%	0.00%
Total	0.00%	0.00%	0.00%

Budget Impacts

(Dollars in Millions)	2009-2011	2011-2013	25-Year
General Fund-State	$0.0	$0.0	$0.2
Total Employer	$0.0	$0.1	$1.1

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

WHAT IS THE PROPOSED CHANGE?

Summary of Benefit Improvement

This bill impacts the PERS Plan 1 by providing the same optional survivor annuity for inactive members who die prior to retirement as is provided for active members who die prior to retirement.

Effective Date: 90 days after end of session.

What Is The Current Situation?

Survivors of active PERS 1 members who die prior to retirement may be eligible to choose between a refund of the member's accumulated contributions with interest or a survivor annuity. To qualify for the survivor annuity, the member must have been eligible for retirement or had ten or more years of service at the time of death. The survivor annuity is calculated as if the member chose to retire and elected a joint and 100 percent survivorship option. The annuity is actuarially reduced for the difference between the age when the member would have qualified for a service retirement and the age of death.

In contrast, survivors of inactive PERS 1 members who die after leaving service but prior to retirement only receive a refund of the member's accumulated contributions with interest.

Who Is Impacted And How?

PERS Plan 1 currently has 2,656 terminated and vested members. Of those, 1,753 have at least ten years of membership service. We would expect to see about seven deaths in the first year among those 1,753 members. The assumed ratio of members with survivors who collect annuities varies by age, but we estimate that approximately four survivors per year would receive an annuity in place of the current return of member contributions.

Additionally, 12,975 PERS Plan 1 active members could be impacted in the future. An active member who terminates with at least ten years of service sometime in the future could also die and leave a beneficiary to collect a monthly annuity under this proposal.

This proposal will not affect member contribution rates in Plan 1 since they are fixed in statute.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

Currently, the average inactive member with ten or more years of service has an accumulated account balance of about $65,000. Under this proposal, a beneficiary could receive a monthly annuity payment instead of an account refund. In most cases, the annuity will be more valuable.

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Who Will Pay For These Costs?

All PERS, School Employees' Retirement System, and Public Safety Employees' Retirement System employers will pay for the cost of this proposal through increased contribution rates due to the change in the unfunded actuarial accrued liability. PERS Plan 1 employees do not pay for the cost of this benefit improvement since their contribution rate remains a constant 6 percent.

HOW WE VALUED THESE COSTS

Assumptions We Made

We used the same assumed ratio of survivors selecting annuities as was used in determining the costs for annuities resulting from active deaths.

Otherwise, we developed these costs using the same assumptions as disclosed in the 2007 Actuarial Valuation Report (AVR).

How We Applied These Assumptions

To estimate the cost of this benefit improvement, we measured the difference in cost between refunding account balances for all terminated vested deaths and paying annuities to those members assumed to have spouses that would elect to receive an annuity. To these survivors, we paid a joint and 100 percent benefit, actuarially reduced from the member's normal retirement age.

Normal retirement age for terminated and vested members in PERS 1 varies depending on qualifications. Members who terminate after December 31, 2001, who are at least age 50 upon termination, and who have at least 20 years of service, may retire without an actuarial reduction at age 60. All other terminated vested members have a normal retirement age of 65, regardless of service.

Members who die with less than 10 years of service, or members whose survivors do *not* select an annuity, continue to receive a refund of member contributions.

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

Special Data Needed

We developed these costs using the same assets and data as disclosed in the AVR.

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ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of PERS 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)*			
PERS 1	**$4,061**	**$0.6**	**$14,062**
Unfunded Actuarial Accrued Liability *(The Portion of the Plan 1 Liability that is Amortized to 2024)*			
PERS 1	**$3,609**	**$0.6**	**$3,609**
Unfunded PUC Liability *(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)*			
PERS 1	**$3,990**	**$0.6**	**$3,990**

Note: Totals may not agree due to rounding.

How Contribution Rates Changed

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01 percent, therefore the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate increase to measure the fiscal budget changes in future biennia.

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Impact on Contribution Rates: (Effective 09/01/2009)			
System/Plan	**PERS**	**SERS**	**PSERS**
Current Members			
Employee (Plan 2)	0.000%	0.000%	0.000%
Employer:			
Normal Cost	0.000%	0.000%	0.000%
Plan 1 UAAL	0.000%	0.000%	0.000%
Total	0.000%	0.000%	0.000%
New Entrants*			
Employee (Plan 2)	0.000%	0.000%	0.000%
Employer:			
Normal Cost	0.000%	0.000%	0.000%
Plan 1 UAAL	0.000%	0.000%	0.000%
Total	0.000%	0.000%	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)	**PERS**	**SERS**	**PSERS**	**Total**
2009-2011				
General Fund	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2011-2013				
General Fund	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**	**0.0**
Local Government	0.1	0.0	0.0	0.1
Total Employer	**0.1**	**0.0**	**0.0**	**0.1**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2009-2034				
General Fund	$0.1	$0.1	$0.0	$0.2
Non-General Fund	0.2	0.0	0.0	0.2
Total State	**0.4**	**0.1**	**0.0**	**0.4**
Local Government	0.6	0.1	0.0	0.7
Total Employer	**0.9**	**0.2**	**0.0**	**1.1**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**

Note: Totals may not agree due to rounding.

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The analysis of this proposal does not consider any other proposed changes to the system. The combined effect of several changes to the system 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

In determining the cost of this bill, we used the same assumed ratio of survivors selecting annuities that we use in estimating the cost of annuities for survivors of active deaths. If instead, we assumed a higher ratio of terminated vested members who die will leave survivors taking annuities, the cost of this bill would be higher.

To set an upper bound on the price of this benefit improvement, we assumed all terminated vested members eligible for the proposed benefit would leave survivors selecting annuities. That is, for all inactive members with at least ten years of service, we assumed 100 percent of those who died would leave survivors electing to receive annuities, regardless of the member's age.

Using this assumption, the increase in the UAAL changed from around $600,000 to about $1,000,000, and the UAAL contribution rate increase went from 0.0005 percent to 0.0009 percent.

If, on the other hand, we assumed that fewer eligible inactive members leave survivors who select an annuity, then we would expect a cost even closer to zero than our best estimate cost of $600,000.

In any case, the cost of this proposal is insufficient to result in a supplemental contribution rate increase in the first biennium. Any subsequent costs would be realized with actual experience.

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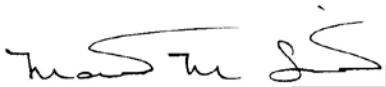
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost 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. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
6. This draft fiscal note has been prepared, and opinions given, 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.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. 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

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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.

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Issues Considered With No Recommendation

Office of the State Actuary

"Securing tomorrow's pensions today."

Plan 1 COLA Proposals

Description Of Issue

The SCPP revisited the Uniform Cost of Living Adjustment (COLA) in PERS and TRS Plan 1. Stakeholders seeking improvements to the COLA have proposed two possible changes. This issue raises three basic policy questions:

- Is the current COLA sufficient?
- Who most needs an improved COLA?
- What form should a new COLA take?

Policy Highlights

- The Uniform COLA helps maintain the value of pensions—though not equally for all members.
- The Uniform COLA and the Plans 2/3 COLA were designed to meet different policy objectives—direct comparisons may be misleading.
- The SCPP has adopted a policy on inflation protection (SCPP Goal #4).
- Benefit improvements for past service increase the Plans 1 UAAL and generally run counter to the principle of intergenerational equity.
- There are a variety of ways to target, implement, and design COLAs.

Stakeholder Proposals:

Stakeholders submitted two proposals to the SCPP regarding the Plan 1 COLA. The stakeholders later asked the Committee to consider revisions to their proposals. See the full report for details on the original stakeholder proposals.

- **Revised Short-Term Option: Grant Additional Increases To The Uniform COLA Based On Year Of Retirement.**
  - Provides larger increases to members retired the longest.
  - Does not precisely recover purchasing power.
  - Impacts minimum benefits.

- **Revised Long-Term Option: Provide The Better Of The Uniform COLA Or A CPI-Based COLA Similar To The Plans 2/3 COLA.**
  - Generally prevents the further loss of purchasing power.
  - Does not diminish benefits.
  - Provides similar value for the CPI-based COLA, but a better overall COLA in the Plans 1 than the Plans 2/3.
  - Raises questions about contractual rights.

Committee Activity

Staff briefed the Committee on this issue in September and November. The Committee held a public hearing in December.

Recommendation To 2009 Legislature

None.

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Plan 1 COLA Proposals

In Brief

ISSUE

The SCPP revisited the COLA provided in PERS and TRS Plans 1. Stakeholders seeking improvements to the COLA have proposed two possible changes. The first modifies the design of the existing COLA by granting additional increases based on the year of retirement. The second establishes a new COLA policy of providing inflation-based increases.

MEMBER IMPACT

These proposals would affect very different member groups. The first would impact nearly 33,000 PERS and TRS Plan 1 members who retired prior to 1991. The second would impact over 114,000* PERS and TRS Plan 1 active, terminated vested, and retired plan members.*

**As of June 30, 2007.*

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Introduction

The SCPP revisited the post-retirement Cost-Of-Living-Adjustment (COLA) provided in Plan 1 of the Public Employees' Retirement System (PERS) and the Teachers' Retirement System (TRS). (The term "Plans 1" will be used throughout to refer to PERS and TRS Plan 1.) Stakeholders seeking improvements to the COLA have proposed possible changes.

This issue raises three basic policy questions:

- Is the current COLA sufficient?
- Who most needs an improved COLA?
- What form should a new COLA take?

This paper will explore the policy considerations around these questions and the challenges faced by policy makers when trying to retrofit a COLA into a plan that was not originally designed for one.

Current Situation

The primary COLA provided in the Plans 1 is the Uniform COLA. The Uniform COLA is a service-based COLA payable the first calendar year in which the recipient turns age 66 and has been retired for one year. The Uniform COLA is a fixed dollar amount multiplied by the member's total years of service. The dollar amount of the Uniform COLA increases by 3 percent every year on July 1. As of July 1, 2008, the Uniform COLA was $1.73 per month/per year of service. This amounts to an annual increase of $623 for a recipient with 30 years of service. Statute specifies that future increases to the Uniform COLA are not a contractual right.

An optional Consumer Price Index (CPI)-based automatic COLA is also available to the Plans 1 members who elect it at retirement. The Auto-COLA* provides an annual percentage increase in the retirement allowance. The increase is based on changes in the CPI** up to a maximum of 3 percent per year (essentially the same COLA as provided in the Plans 2/3). The Auto-COLA begins one year

after retirement—regardless of age or service—and is in addition to any other COLAs received. Members who elect the Auto-COLA receive an actuarially reduced retirement allowance to offset the cost.

COLAs address how well a pension maintains its value, while minimum benefits address the adequacy of a pension.

The Plans 1 also provide minimum retirement benefits in addition to the COLAs discussed above. While COLAs address how well a pension maintains its value over time, minimum benefits address the adequacy of a pension and serve as a safety net. Minimum benefits increase every year—effectively providing a COLA to those at the minimum benefit level. Two minimums are provided: the Basic and the Alternative.

The Basic Minimum is $38.92*** per month multiplied by the member's total years of service. The Alternate Minimum is $1,092.73*** a month for recipients who:

a) Have at least 25 years of service and have been retired at least 20 years.

b) Have at least 20 years of service and have been retired at least 25 years.

The Basic Minimum increases every year by the dollar amount of the Uniform COLA. (For example, the Basic Minimum increased from $37.19 to $38.92 in 2008. The $1.73 increase was the amount of the Uniform COLA for that year.) The Alternate Minimum is not tied to the Uniform COLA and increases by 3 percent each year.

**First available in 1990.*
***Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) for Seattle-Tacoma-Bremerton (STB).*
****As of July 1, 2008.*

Example

Figure 1 illustrates the impact of the Uniform COLA on three retirees with 30 years of service and different monthly pensions. In this example, Retiree 3 receives the Basic Minimum benefit—which increases by the Uniform COLA amount each year.

Figure 1

Uniform COLA Example: 30 Years of Service				
	Pension Before COLA	2008 Uniform COLA ($1.73*30)=51.90	Pension After COLA	Percent Increase
Retiree 1	$1,500.00	$51.90	$1,551.90	3.46%
Retiree 2	$3,000.00	$51.90	$3,051.90	1.73%
Retiree 3	$1,115.70 (Basic Minimum)	$51.90	$1,167.60 (Basic Minimum)	4.65%

The Uniform COLA provides proportionately higher increases for annuitants with smaller pensions.

This example shows how the Uniform COLA provides proportionately higher increases (and greater purchasing power protection) for annuitants with smaller pensions. This is because the Uniform COLA is a fixed dollar amount and not based on a percentage of the pension.

History

To understand where today's COLA policy came from, it is helpful to look at the history of COLA policy from different perspectives. The broader perspective is how COLA policy has changed within the context of plan design. A more narrow focus is how the Legislature has addressed COLAs within the Plans 1.

COLA Policy Has Changed Over Time

When the Plans 1 were first created over 60 years ago, they did not provide for post-retirement COLAs. COLAs may not have been provided for a variety of reasons:

The Plans 1 were not originally designed to provide a COLA.

- Inflation was relatively low from 1940 until the early 1970s.
- Members were not expected to live many years in retirement.
- The plans were intended to provide more of a reward for service than replacement income.

Eventually, changing times began to challenge this design. Periods of high inflation, increasing life spans, and increasing expectations for retirement all called into question the adequacy of the Plans 1 design. These challenges led to a rethinking of the basic purpose of retirement plans.

The Plans 2 were designed from the onset to provide a COLA.

Responding to challenges with the Plans 1 design, the Plans 2 were created in 1977. The Plans 2 were designed from the onset to be income replacement plans and to provide a post-retirement COLA. Part of this design was the establishment of a normal retirement age of 65—substantially higher than the retirement ages in Plans 1. The higher retirement age made the COLA more affordable and increased the likelihood the COLA would reasonably protect the value of the pension over the recipient's life.

The Plans 2 income replacement and COLA policy was carried forward into the design of the Plans 3 when those plans were created in the late1990s.

Benefits For Plans 1 Retirees Have Increased Over Time

COLA policy also changed within the Plan 1 design to a more limited extent. Responding to concerns about the adequacy of benefits and the impact of inflation, policy makers made several efforts over the years to increase benefits for retirees in the Plans 1. These efforts continued even after they closed.

The Legislature has employed a variety of different approaches in their efforts to increase retiree benefits:

Various approaches have been used to increase retiree benefits.

- Establishing minimum benefits and periodically increasing them to reflect changes in the cost-of-living.
- Granting various ad-hoc benefit increases.
- Granting increases based on earnings realized by plan assets.
- Providing an optional, CPI-based COLA from retirement paid for by members.
- Providing automatic COLAs (including Uniform).

Appendix A provides a history of post-retirement benefit increases in the Plans 1. Some highlights from this history are provided in **Figure 2,** below.

Figure 2

Key Post-Retirement Benefit Adjustments in The Plans 1	
Year	Increase
1961	Minimum benefit established.
1970-1986	Various ad-hoc COLAs (3% - 6%) and Minimum benefit increases.
1987	3% automatic annual increase in Minimum benefit.
1989	CPI-based automatic COLA (up to 3%) for retirees whose purchasing power at age 65 drops more than 40%.
1995	Uniform COLA replaces CPI-based COLA.
1998	Gain-sharing established. Provided possible even-year increases in the Uniform COLA depending on investment earnings.
2008	Gain-sharing ended. Replaced by one-time increase to Uniform COLA.

SCPP Action Taken On Plans 1 COLA Policy

The SCPP studied the issue of purchasing power for Plans 1 retirees in 2003 and 2004, and received an update on the issue in 2005.

The SCPP has made several recommendations on COLAs in the Plans 1 that have been adopted by the Legislature.

The SCPP has made several recommendations on COLAs in the Plans 1.

2003*

- $1,000 Alternative Minimum benefit for members with 25+ years of service and retired 20+ years.

2004*

- $1,000 Alternative Minimum benefit for members with 20+ years of service and retired 25+ years.
- Increase the amount of the Alternative Minimum by 3 percent each year.
- One-time increase in the Uniform COLA.
- Provide the Uniform COLA to members who will turn age 66 during the calendar year.

Indicates year first recommended. Some proposals were recommended in more than one year. See **Appendix A for year enacted.*

Policy Analysis

Other Washington Plans

The Plans 2/3 provide a CPI-based COLA.

Washington's Plans 2/3 provide a CPI-based COLA. This COLA is designed to maintain the purchasing power of retiree benefits and is consistent with the underlying income replacement design of the plan. The Plans 2/3 COLA is an annual percentage increase in the retirement allowance beginning one year after retirement. The increase is based on changes in the CPI* up to a maximum of 3 percent per year.

As discussed in the **History** section, the Plans 2/3 COLA is tied to a normal retirement age of 65 (or 62 with 30 years of service). Members who retire prior to the normal retirement age still receive the COLA after one year—but on an actuarially reduced benefit.

**Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) for Seattle-Tacoma-Bremerton (STB).*

Peer Systems

Washington's peer systems provide automatic CPI-based or fixed-percent COLAs.

All of Washington's peer systems provide an automatic post-retirement COLA in their open plans (see **Figure 3**). Five of those systems provide COLAs that are CPI-based with varying caps from 2 to 6 percent. The remaining systems provide fixed percent increases ranging from 1.5 to 3.0 percent. Systems where members are not covered by Social Security tend to provide larger COLAs. Most COLAs begin after one year of retirement; Florida and Idaho provide prorated COLAs for those retired less than one year.

Several of the peer systems provide protection against specific losses of purchasing power. Benefits in the California systems cannot fall below a minimum percent (75 or 80 percent) of the original benefit's purchasing power. Benefits in the Seattle system cannot fall below 60 percent of their original purchasing power. This is similar to a 1992 COLA provision that protected Plans 1 members from the loss of more than 40 percent of their age 65 benefits' purchasing power.

Figure 3

COLA Provisions by Select Retirement Systems*	
System	**COLA**
Cal PERS	CPI based, 2% max (75% purchasing power min.)
Cal STRS	2% simple (80% purchasing power min.)
Colorado PERA**	CPI up to 3%
Florida (FRS)	3%
Idaho (PERSI)	CPI based, 1% min, 6% max,
Iowa (IPERS)	Simple, 3% max, tied to investment surplus
Minnesota (MSRS)	CPI based, 2.5% max + investment surplus
Missouri (MOSERS)**	80% of change in the CPI, 5% max
Ohio (OPERS)**	CPI based, 3% max
Oregon PERS**	CPI based, 2% max
Seattle (SCERS)	1.5% (60% purchasing power min.)

**For new hires. Source: Member handbooks published on system administrators' websites as of 8/28/2008.*

***Not covered by Social Security.*

Some state plans only provide ad-hoc COLAs.

While all of Washington's peer systems provide automatic CPI-based or fixed percent COLAs, some states do not. According to the 2007 Public Fund Survey (a national survey of 126 retirement plans representing all 50 states), 26 state plans provide COLAs only on an ad-hoc basis. Also, 15 state plans provide COLAs that are in some part based on investment earnings. The remaining plans (nearly two-thirds) generally provide automatic CPI-based or fixed-percent COLAS.

Providing Adequate Benefits And Protecting Purchasing Power Are Different Policy Objectives

COLA policy has largely been driven by adequacy of benefits and purchasing power concerns.

COLA policy in the Plans 1 has largely been driven by the twin concerns of adequacy of benefits and purchasing power protection. Though there is some overlap, the two are very distinct concepts from a plan-design perspective and have different policy implications.

Adequacy of benefits relates to how well a pension *meets expectations* around a standard of living. In contrast, purchasing power protection relates to how well a pension *retains value* over time. To illustrate the difference: the pension of a highly-paid retiree might lose considerable value over time and still be considered "adequate," while

the pension of a low-paid retiree might retain its full value over time but be considered "inadequate."

Purchasing power protection is addressed through COLAs.

Adequacy of benefits may be addressed through a variety of means including changing benefit formulas or establishing minimum benefits. Purchasing power protection is addressed through COLAs. The remainder of this paper will focus on policies around purchasing power protection.

The Uniform COLA And Plans 2/3 COLA Were Designed To Meet Different Objectives

Discussions of COLA policy in the Plans 1 often involve comparisons between the Uniform and the Plans 2/3 COLA. These COLAs were designed to meet different policy objectives. Direct comparisons between them can be misleading.

The Uniform COLA is designed to meet four primary policy objectives within fiscal constraints:

The Uniform COLA provides more purchasing power protection to members with lower salaries.

- Provide a larger dollar increase to members with more service.
- Provide more purchasing power protection to members who retire with lower salaries.
- Provide a COLA at the same age that Plans 2/3 members qualify for an unreduced COLA.
- Provide legislators a simple mechanism to grant ad-hoc COLAs.

These objectives are consistent with the reward-for-service design of the Plans 1 and reflect trade-offs between adequacy of benefits and purchasing power protection. Tying the Uniform COLA to the Plans 2/3 unreduced retirement age may reflect a desire to maintain consistency between the plans in the starting age for unreduced COLAs. The design of the Uniform COLA also provides a simple mechanism for legislators to grant ad-hoc COLAs—the most recent example being the 40 cent (per month/per year of service) increase granted in 2008.

In contrast to the Uniform COLA, the Plans 2/3 COLA is designed to maintain the value of members' pensions in an environment of moderate inflation. The Plans 2/3 COLA

The Plans 2/3 COLA is designed to maintain purchasing power for all retirees.

does not favor any one group of retirees. Retirees with relatively high salaries and high benefits receive the same protection from inflation as lower-salary, lower-benefit retirees. This is consistent with the underlying income-replacement design of the plan.

The Uniform and the Plans 2/3 COLA both provide inflation protection consistent with their respective plan designs. While the Plans 2/3 COLA generally does a better job of maintaining the value of the pension than the Uniform COLA, there are exceptions. Some Plans 1 retirees may receive proportionately larger increases under the Uniform COLA than they would under the Plans 2/3 COLA. These would tend to be recipients of minimum benefits or low-wage, high-service retirees.

Existing Policies Impact This Issue

There are three key policies that are relevant to a discussion of this issue:

- Inflation protection.
- Intergenerational equity.
- Amortization of Plan 1 unfunded liabilities.

The SCPP adopted a policy goal directly related to inflation protection.

The SCPP adopted a policy goal directly related to inflation protection. The goal is: "to increase and maintain the purchasing power of retiree benefits in the Plans 1 of PERS and TRS, to the extent feasible, while providing long-term benefit security to retirees." The Legislature has taken actions that support this goal by providing various automatic COLAs not included in the original design of the Plans 1. This includes the Uniform COLA and automatic increases in minimum benefits.

A desire that retiree benefits should have some form and degree of protection from inflation is also evident in the creation of the Plans 2/3. These plans included a CPI-based automatic COLA in the original plan design.

Intergenerational equity requires benefits to be funded over the working lifetime of the member.

Another policy that impacts this issue is the Legislature's funding policy based on the concept of intergenerational equity. The policy is to fund, to the extent feasible, benefit increases for Plans 1 members over the working lives of those members so that the cost of those benefits are paid by the taxpayers who receive the benefit of those members' service [RCW 41.45.010 (4)].

Benefit increases granted to retired members are inconsistent with the concept of intergenerational equity. Why? None of the cost can be funded over their working lifetimes since they are already retired. Instead, the cost is generally born by taxpayers who never received services from the members.

Providing benefit improvements for active Plans 1 members consistent with intergenerational equity presents policy makers a challenge as well. Active members in the Plans 1 are generally close to retirement. This leaves limited opportunity to fund the cost of improved benefits over the remainder of their working lifetimes. Therefore, the source of contributions to fund benefit improvements increasingly becomes taxpayers who never received services from these members.

The cost of Plans 1 benefit improvements not funded over the members' working lifetimes is passed along to Plans 2/3 employers. All Plans 2/3 employers are required to make additional contributions to pay for these Plans 1 benefits.

Benefit improvements for past service increase the Plans 1 UAAL.

Benefit improvements for past service increase the Unfunded Actuarial Accrued Liability (UAAL) for the Plans 1. The UAAL exists because benefits already earned by Plans 1 members have not been fully paid for. Current funding policy requires that the UAAL in the Plans 1 be fully paid by June 30, 2024 [RCW 41.45.010(2)]. The level of benefit improvements that can be financed over the remaining amortization period may serve to constrain policy options.

COLA Policy May Impact Human Resource Policies

COLA policy in the Plans 1 may have an impact on human resource policies around post-retirement employment and retention.

The lack of a COLA for Plans 1 members prior to age 66 may encourage post-retirement employment. Returning to work after retirement may seem an attractive option for those who wish to accumulate additional assets to offset future inflation and other post-retirement expenses. This may lead to greater pressure for expanded post-retirement employment opportunities. In 2001, the Legislature expanded the post-retirement employment program for the Plans 1. The expansion allows Plans 1 retirees to work

significantly more hours than Plans 2/3 retirees without having their pensions suspended.

On the flip side, providing a COLA in the Plans 1 prior to age 66 may encourage more Plans 1 members to retire at earlier ages. Such an outcome may conflict with employers' desire to retain their most experienced workers.

Several Factors May Impact Purchasing Power

Policy makers seeking to answer questions about the need for an improved COLA in the Plans 1 may also turn to an economic approach. An economic approach to COLA policy considers the impact of inflation on the purchasing power of retiree pensions. When balanced with the overall policy considerations, an economic analysis may provide additional focus for further policy discussion.

Purchasing power is a measure of how well a pension retains its value over time.

Purchasing power is a measure of how well a pension retains its value over time. Purchasing power is measured by comparing the change in the member's pension over time with the amount of inflation over the same time period. Purchasing power is impacted by three factors:

- Inflation after retirement.
- Length of retirement.
- Post-retirement COLAs.

Inflation is the driving force behind the decline in the relative value of a pension over time. Members who retire during periods of high inflation will generally lose more purchasing power than members who retire during periods of relatively low inflation. See **Appendix B** for a history of inflation.

Likewise, members who are retired for a longer period of time are likely to lose more purchasing power due to post-retirement inflation than members who are retired for shorter periods. Earlier retirement ages and increasing life spans are significant factors in the loss of purchasing power experienced by some members.

Post-retirement COLAs help maintain purchasing power.

Post-retirement COLAs offset the effects of inflation and help maintain purchasing power. The Legislature has provided numerous COLAs in the Plans 1 (see **Appendix A**). Members who receive less in COLAs will generally lose

more purchasing power over time than members who receive more in COLAs.

Figures 4 and 5 show the purchasing power for PERS and TRS Plans 1 service retirees by year of retirement. The Original Benefit line shows the purchasing power had no COLAs been provided. The Current Benefit line shows the purchasing power after factoring in all COLAs. The differences in purchasing power between the systems reflect the impact of COLAs received.

Figure 4
Purchasing Power of PERS 1 Service Benefits in 2008

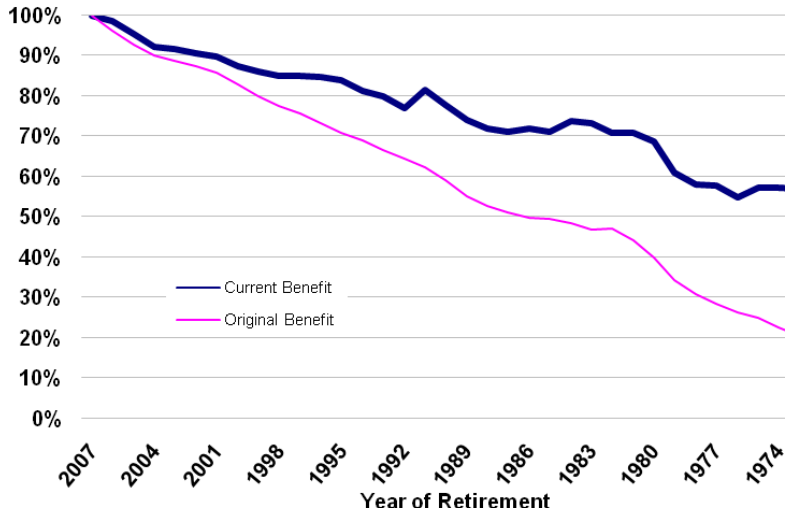
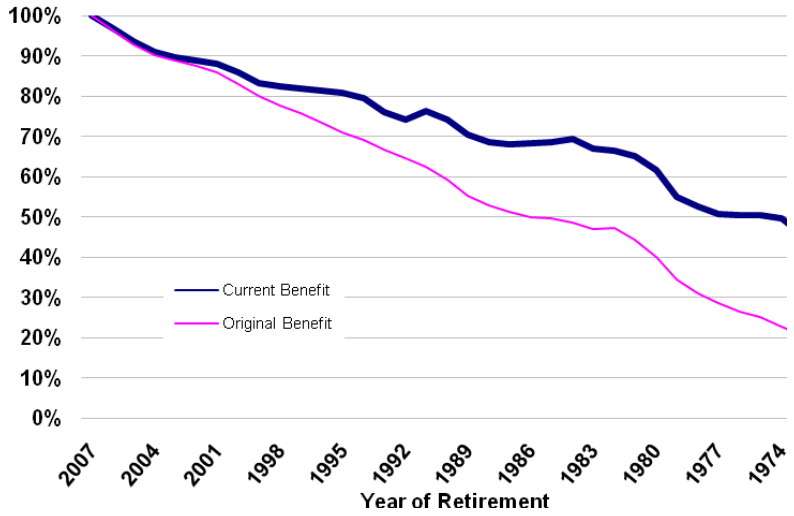


Figure 5
Purchasing Power of TRS 1 Service Benefits in 2008



Purchasing power for Plans 1 members who retired at the same time may vary widely from the group average due to post-retirement increases. The Plans 1 have provided numerous post-retirement benefit increases that were not designed to uniformly recover purchasing power. These include increases to minimum benefits, certain ad-hoc COLAs, and Uniform COLA increases. These increases impact members within the same group differently. Generally, the increases have served to recover more purchasing power for retirees with lower pensions.

The Uniform COLA Helps Maintain The Value Of Pensions

Some Uniform COLA recipients will continue to lose purchasing power.

A closer look at how the current Uniform COLA impacts purchasing power is relevant to a discussion of purchasing power within the Plans 1. The Uniform COLA helps maintain the value of a recipient's pension from age 65. Because the Uniform COLA is a dollar amount per year of service, it provides the greatest inflation protection for members who retired with the smallest salaries (This includes members who worked lower-paying jobs, and members who retired many years ago when wages were generally lower.) Members who retire prior to age 65 may lose a significant amount of purchasing power in their pension before they receive their first Uniform COLA increase. Once they receive the Uniform COLA, the impact on purchasing power will vary. Some recipients (lower-salaried) may maintain or even recover lost purchasing power during some years, while others (higher-salaried) will face a continued erosion of purchasing power.

COLA Policy Is A Balance

COLA policy reflects a balance between various concerns.

As discussed earlier in this paper, current COLA policy in the Plans 1 reflects a balance between various concerns:

- Inflation protection.
- Adequacy of benefits.
- Intergenerational equity.
- Funding.
- Human resources.

Policy makers may wish to consider whether or not the current balance is appropriate when evaluating the sufficiency of the Plans 1 COLA.

Key Questions In Shaping New COLA Policy

The first part of this paper has explored the question of whether or not the current COLA in the Plans 1 is sufficient. If policy makers feel the COLA needs improvement, they may next consider who most needs an improved COLA and what form the COLA should take. Answers to these key questions will help shape any new COLA policy.

COLAs Can Be Targeted

COLAs may be directed to individuals with the greatest perceived need.

It is likely that substantial improvements to the Plans 1 COLA will face fiscal constraints. Policy makers may then choose to direct limited COLA dollars to those individuals who they perceive as having the greatest need for a COLA. COLAs can be targeted to recipients based on loss of purchasing power, years retired, years of service, or size of benefit. If policy makers desire to maintain purchasing power they will likely target COLAs based on purchasing power or years retired. If the desire is to reward long careers, then COLAs will likely be targeted to members with many years of service. If the concern is adequacy of benefits, then COLAs will likely be targeted to members with the lowest pensions.

Besides directing dollars to recipients with the most need, targeting COLAs may serve other policy needs such as controlling costs or maintaining equity across the plans.

COLAs May Be Implemented Many Different Ways

COLAs may be ad-hoc or automatic.

The form that an improved COLA takes depends on the goals of policy makers. COLAs may be implemented in a variety of ways to achieve specific policy objectives. COLAs may be implemented on a one-time or ongoing basis, and the payment may take many forms.

Ad-hoc COLAs are one-time increases given to retirees. Ad-hoc COLAs can be very effective at making up for past inflation, but usually do little to address future inflation. Ad-hoc COLAs can give policy makers the most flexibility in

reacting to specific situations and in controlling costs. When COLAs are ad-hoc, there is often little or no pre-funding—effectively making them pay-as-you-go benefit improvements.

In contrast, automatic COLAs are ongoing increases and usually benefit both active and retired members. Automatic COLAs can be very effective at protecting benefits against future inflation, but may do little to address lost purchasing power due to past inflation. Automatic COLAs may be preferred from the member viewpoint since they are ongoing and don't require continual action by policy makers. However, for the same reasons, it may be more difficult to fine-tune an automatic COLA for a specific situation. Because automatic COLAs are ongoing and more forward-looking, they offer greater opportunities for pre-funding. Pre-funding reduces the contributions required for a benefit improvement since more of the cost of the improvement is paid for by future investment returns.

COLA payments may take many forms. Some of these include:

COLA payments may take many forms.

- Percentage based on a CPI.
- Fixed percentage.
- Flat dollar amount.
- Dollar amount per year of service.

CPI-based COLAs are the most direct way to protect a benefit against inflation since the COLA is based on actual, measured inflation. CPI-based COLAs provide the same inflation protection to all recipients regardless of the size of their pension. CPI-based COLAs often have an annual cap to control costs. However, an annual cap means that recipients will lose purchasing power when inflation exceeds the cap.

Fixed percentage COLAs (i.e., 2 or 3 percent) protect against a set amount of inflation while controlling costs. They provide the same amount of inflation protection to all recipients regardless of the size of their pension. However, recipients will lose purchasing power when inflation exceeds the fixed percent.

Flat dollar amount COLAs (i.e., $100/month) provide proportionally greater increases to recipients with smaller pensions. While they may do little to protect purchasing

power for retirees with larger pensions, flat dollar amount COLAs are an effective way to address adequacy of benefit concerns.

Dollar amount per year of service COLAs (i.e., $10/month/year of service) provide larger increases to members with more service and proportionally larger increases to members who retired with lower salaries. This type of COLA is a blend between adequacy of benefits and reward for service policies. It may do little to protect the purchasing power of high-salaried retirees. The Uniform COLA is an example of this type of COLA in the Plans 1.

COLAs might be impacted by IRS requirements.

Any of the COLA designs mentioned above might be impacted by Internal Revenue Service (IRS) requirements. Some designs might result in COLAs that do not conform to IRS requirements for tax-qualified plans or must be administratively reduced to comply with IRS requirements. This is more likely to be an issue with COLAs designed to make up for long periods of past inflation. Policy makers may wish to consult tax counsel before making significant changes in COLA policy.

Policy Makers Have Flexibility In Crafting COLA Policy

Policy makers have a great deal of flexibility in crafting new COLA policy for the Plans 1. Policy makers may target, implement, and design COLAs in a variety of ways to support their policy objectives. Any new COLA policy may be constrained by fiscal and IRS considerations.

Conclusion

The issue of COLAs in the Plans 1 raises three basic questions for policy makers.

- Is the current COLA sufficient?
- Who most needs an improved COLA?
- What form should a new COLA take?

In considering these questions, policy makers will likely balance a wide variety of concerns including inflation protection, adequacy of benefits, intergenerational equity, funding, and human resources. The current Plans 1 Uniform COLA reflects trade-offs between these various concerns.

Any change to the Uniform COLA will likely involve further trade-offs. Given likely fiscal constraints, policy makers may choose to direct limited COLA dollars to recipients with the greatest perceived need.

Stakeholder Proposals

Stakeholders proposed both a short-term and long-term option. They later revised both options.

Stakeholders are seeking improvements in the COLAs provided to PERS and TRS Plan 1 retirees. The stakeholders have proposed both a short-term and a long-term option. The short-term option modifies the design of the existing Uniform COLA by granting additional increases based on the year of retirement. The long-term option establishes a new COLA policy by providing a CPI-based COLA.

Following the initial Committee briefing on this issue, stakeholders submitted revised COLA proposals to the Committee for consideration. Both the original and revised proposals are discussed below.

Original Stakeholder Proposals

The original short-term option modified the design of the existing Uniform COLA by granting additional increases based on the year of retirement. The original long-term option replaced the Uniform COLA with a CPI-based COLA similar to the Plans 2/3 COLA.

Preliminary pricing of the original proposals was provided at the September meeting.

Proposal 1: Original Short-Term Option

Increase the 2009 Uniform COLA by the following additional amounts based on year of retirement:

Year Retired	Increase Amount *($ per month/per year of service)*
1985-1990	$0.75
1980-1984	$1.00
1979 and earlier	$1.50

This option has several broad policy implications that are discussed in more detail below. These include:

- Modifies existing COLA policy.
- Provides larger increases to members retired the longest.
- Does not precisely replace purchasing power.
- Impacts minimum benefits.

Modifies Existing COLA Policy.

This option is consistent with the reward-for-service design.

This option would establish a new policy objective within the existing Uniform COLA design. The new policy would grant different COLAs based on year of retirement. This differs from the current Uniform COLA design of granting the same increase to all members with the same service. However, it is consistent with the reward-for-service design of the Plans 1 since the COLA amount is still based on years of service—within each group. No additional increases are provided for members who retired after 1990. However, policy makers may feel less need to provide an additional COLA to these members since they had the option of purchasing the CPI-based Auto-COLA at retirement.

Provides Larger Increases To Members Retired Longest.

Some members who have been retired longer have not necessarily lost more purchasing power.

This option grants larger COLA increases to members who have been retired longer. Some members who have been retired longer have not necessarily lost more purchasing power after past COLAs are factored in. To more precisely replace lost purchasing power would require measuring purchasing power on an individual basis—which may be more complex to administer.

Does Not Precisely Recover Purchasing Power.

Targeting COLAs on a group basis does not precisely recover an individual's lost purchasing power. The purchasing power of individuals within the group varies due to past COLAs. This means that some members will benefit more than others in any group approach. The large differences between the steps of the increases further increase this discrepancy for some members. As an

extreme example, a member who retired in 1979 will receive a COLA that is 50 percent larger than a member who retired in 1980—even though inflation was only 16.1 percent between 1979 and 1980. While this approach does not precisely recover purchasing power for an individual, it is relatively easy to administer and does provide larger increases to groups that have lost more purchasing power.

Impacts Minimum Benefits.

Some may view this as effectively creating four different Basic Minimum benefits.

This proposal has implications for minimum benefit policy because the Basic Minimum is tied to the Uniform COLA amount. The proposal would result in recipients of the Basic Minimum receiving different total benefit amounts based on the year they retired. Some policy makers may view this as effectively creating four different Basic Minimum benefits based on year of retirement. Others may view this as providing an additional COLA for those who have been retired longer, on top of the Basic Minimum. However this is viewed, it raises certain policy questions.

Minimum benefits are intended to provide an adequate standard of living for recipients. Policy makers may question whether it is appropriate to effectively establish different standards of living based solely on length of retirement. For example, does someone retired for 30 years require a larger pension to maintain an adequate standard of living than someone retired for only five years? The Legislature set a precedent for providing higher minimum benefits based on years retired when it established the Alternate Minimum benefit in 2004. Policy makers exploring this option may wish to consider if the Basic Minimum should continue to be linked to the Uniform COLA or if a different increase mechanism would be preferable.

Proposal 2: Original Long-Term Option

Replace the Uniform COLA with a CPI-based COLA similar to the Plan 2/3 COLA:

- CPI up to 3 percent maximum a year.
- Starts one year after retirement.
- Retroactive or prospective.

This option has several broad policy implications which are discussed in more detail below. These include:

- Establishes a new COLA policy.
- Generally prevents the further loss of purchasing power.
- Diminishes benefits for some members.
- Provides a better COLA in the Plans 1 than in the Plans 2/3.

Establishes A New COLA Policy.

This option is more consistent with an income replacement design.

This option would establish a new* COLA policy for the Plans 1 of basing COLAs on actual inflation—regardless of service or salary. This policy is more consistent with an income replacement plan design such as the Plans 2/3. It is also a departure from the current policy to provide more inflation protection to members who retired with lower salaries.

*****A CPI-based COLA was provided from 1989-1994. The COLA began after a member lost more than 40 percent of purchasing power from age 65.*

Generally Prevents Further Loss Of Purchasing Power.

Fully retroactive increases might have implications for plan qualification.

Providing this COLA on a prospective basis will generally prevent the further erosion of purchasing power for current and future retirees—as long as long-term inflation averages less than 3 percent. Making it retroactive will enable retirees to recover lost purchasing power, but will be more expensive. Providing COLA increases retroactive to retirement will likely result in relatively large increases for some retirees (i.e. doubling the pension) and might have implications for plan qualification under IRS requirements.

Diminishes Benefits For Some Members.

Diminishing benefits raises questions around contractual rights.

The Uniform COLA will provide larger increases for some retirees—whether the new CPI-based COLA is applied prospectively or retroactively. Members who would likely benefit more under the Uniform COLA design include those who retired with relatively low salaries or who are receiving the Basic Minimum benefit. Diminishing benefits raises questions around contractual rights protections. Statute

specifies that future increases to the Uniform COLA are not a contractual right. However, this kind of statutory language is currently subject to litigation.

Provides Larger Lifetime COLAs In The Plans 1.

This proposal has implications for equity between the plans. It would provide larger lifetime COLAs to some Plan 1 members than is available to Plan 2/3 members. Plan 1 members would receive an unreduced COLA regardless of age. In contrast, Plan 2/3 members who retire prior to age 65 (or age 62 with 30 years of service) receive a COLA on an actuarially reduced benefit—effectively reducing the COLA they receive. This would result in many Plan 1 members receiving more generous lifetime benefits than similarly situated Plan 2/3 members.

Revised Stakeholder Proposals

The revised short-term option modifies the design of the existing Uniform COLA by granting additional increases based on the year of retirement. The revised long-term option provides the better of the Uniform COLA or a CPI-based COLA similar to the Plans 2/3 COLA.

Preliminary pricing of the revised short-term option was provided at the November meeting.

Proposal 1: Revised Short-Term Option

Increase the 2009 Uniform COLA by the following additional amounts based on year of retirement:

Year Retired	Increase Amount *($ per month/per year of service)*
1985-1990	$0.35
1980-1984	$0.50
1979 and earlier	$0.75

This option has several broad policy implications that are discussed in more detail below. These include:

- Modifies existing COLA policy.
- Provides larger increases to members retired the longest.
- Does not precisely replace purchasing power.
- Impacts minimum benefits.

Modifies Existing COLA Policy

This option is consistent with the reward-for-service design.

This option would establish a new policy objective within the existing Uniform COLA design. The new policy would grant different COLAs based on year of retirement. This differs from the current Uniform COLA design of granting the same increase to all members with the same service. However, it is consistent with the reward-for-service design of the Plans 1 since the COLA amount is still based on years of service—within each group. No additional increases are provided for members who retired after 1990. However, policy makers may feel less need to provide an additional COLA to these members since they had the option of purchasing the CPI-based Auto-COLA at retirement.

Provides Larger Increases To Members Retired Longest

Some members who have been retired longer have not necessarily lost more purchasing power.

This option grants larger COLA increases to members who have been retired longer. Some members who have been retired longer have not necessarily lost more purchasing power after factoring in past COLAs. To more precisely replace lost purchasing power would require measuring purchasing power on an individual basis—which may be more complex to administer.

Does Not Precisely Recover Purchasing Power

Targeting COLAs on a group basis does not precisely recover an individual's lost purchasing power. The purchasing power of individuals within the group varies due to past COLAs. This means that some members will benefit more than others in any group approach. The large differences between the steps of the increases further increase this discrepancy for some members. As an extreme example, a member who retired in 1979 will receive a COLA that is 50 percent larger than a member who retired in 1980—even though inflation was only 16.1

percent between 1979 and 1980. While this approach does not precisely recover purchasing power for an individual, it is relatively easy to administer and does provide larger increases to groups that have lost more purchasing power.

Impacts Minimum Benefits

Some may view this as effectively creating four different Basic Minimum benefits.

This proposal has implications for minimum benefit policy because the Basic Minimum is tied to the Uniform COLA amount. The proposal would result in recipients of the Basic Minimum receiving different total benefit amounts based on the year they retired. Some policy makers may view this as effectively creating four different Basic Minimum benefits based on year of retirement. Others may view this as providing an additional COLA for those who have been retired longer, on top of the Basic Minimum. However this is viewed, it raises certain policy questions.

Minimum benefits are intended to provide an adequate standard of living for recipients. Policy makers may question whether it is appropriate to effectively establish different standards of living based solely on length of retirement. For example, does someone retired for 30 years require a larger pension to maintain an adequate standard of living than someone retired for only five years? The Legislature set a precedent for providing higher minimum benefits based on years retired when it established the Alternate Minimum benefit in 2004. Policy makers exploring this option may wish to consider if the Basic Minimum should continue to be linked to the Uniform COLA or if a different increase mechanism would be preferable.

Proposal 2: Revised Long-Term Option

Provide the better of the Uniform COLA or a CPI-based COLA similar to the Plan 2/3 COLA:

- CPI from retirement up to 3 percent maximum a year.
- Starts the year the retiree turns age 66.
- Prospective only.

This option has several broad policy implications that are discussed in more detail below. These include:

- Establishes a new COLA policy.
- Generally prevents further loss of purchasing power.
- Does not diminish benefits.
- Provides a CPI-based COLA with similar value to the Plans 2/3 COLA.
- Provides a better overall COLA in the Plans 1 than in the Plans 2/3.
- Raises questions about contractual rights.

This option is more consistent with an income replacement design.

Establishes A New COLA Policy

This option would establish a new* COLA policy for the Plans 1, basing COLAs on actual inflation—regardless of service or salary. This policy is more consistent with an income replacement plan design such as the Plans 2/3. It is also a departure from the current policy to provide more inflation protection to members who retired with lower salaries.

**A CPI-based COLA was provided from 1989-1994. The COLA began after a member lost more than 40 percent of purchasing power from age 65.*

It will not recover lost purchasing power.

Generally Prevents Further Loss Of Purchasing Power

Providing this COLA on a prospective basis will generally prevent the further erosion of purchasing power for current and future retirees—as long as long-term inflation averages 3 percent or less. It will not recover purchasing power already lost due to inflation.

Does Not Diminish Benefits

Providing the better of the Uniform COLA or the proposed CPI-based COLA ensures that retirement benefits are not diminished for any member. (Some would receive larger increases under the Uniform COLA; others, under the CPI-based COLA.) Policy makers may prefer to <u>not</u> diminish benefits in order to avoid raising issues around contractual rights protections.

Provides A CPI-Based COLA With Similar Value To The Plans 2/3 COLA

The proposed CPI-based COLA would start at age 66—the same age that Plans 2/3 members with less than 30 years of service* qualify for an unreduced COLA. Tying the proposed CPI-based COLA to the Plans 2/3 unreduced retirement age ensures the two COLAs generally provide similar value. This is because Plans 1 and Plans 2/3 members will generally receive the full value of a CPI-based COLA starting at the same age. Starting the proposed CPI-based COLA at age 66 is also consistent with current practice in the Uniform COLA.

**Members with 30 or more years of service qualify at age 62.*

Provides A Better Overall COLA In The Plans 1

This option provides a better overall COLA, going forward, in the Plans 1 than in the Plans 2/3. This is because Plans 1 members would receive the *better* of a COLA similar to the Plans 2/3 COLA or the Uniform COLA. In other words, the Plans 2/3 COLA becomes the new baseline COLA in Plan 1—with some members (Uniform COLA recipients) receiving additional amounts on top of that.

Raises Questions About Contractual Rights

Policy makers may wish to consult legal counsel before designing a benefit linked to non-contractual rights language.

Statute specifies that the Legislature reserves the right to amend or repeal the Uniform COLA, and that future increases to the Uniform COLA are not a contractual right. The option does not specify whether the CPI-Based COLA would have similar language. Policy makers would need to specify whether or not the proposed new benefit is a contractual, or a non-contractual right. The implications of making the proposed new benefit a contractual right while leaving the Uniform COLA a non-contractual right are unclear. Also, non-contractual rights language similar to that used in the Uniform COLA is currently subject to litigation. Policy makers may wish to consult legal counsel before designing a benefit that is linked to non-contractual rights language.

Committee Activity

Staff briefed the full SCPP on this issue, including the original stakeholder proposals, at the September meeting. At the Executive Committee meeting that followed, the stakeholders requested the Committee allow them to revise the proposals under consideration.

Staff briefed the full SCPP on the revised proposals in November. The Executive Committee then recommended that the full SCPP consider the revised short-term option for possible executive action at the December meeting.

The Committee held a public hearing in December and took no further action on this issue.

Stakeholder Input

The following correspondence is on file with the Office of the State Actuary. Items marked with an asterisk are also attached to this paper.

Correspondent	Affiliation	Date
Ester Wilfong Leslie Main Don Carlson	Legislative Committee Chair, WSSRA Legislative Coordinator, WSSRA Lobbyist, WSSRA	03/20/2008
John Kvamme	Consultant, WASA & AWSP	04/15/2008
Not Specified	PEPR	04/15/2008 **06/17/2008*** **10/07/2008***
John E. O'Brien Cassandra de la Rosa	President, RPEC Executive Director, RPEC	05/13/2008
Lindajo Jarboe		06/10/2008 10/01/2008
Matthew D. Zuvich	Chair, PEPR	07/08/2008
Bill Loken		08/17/2008
Hal Phillips		12/10/2008

**Correspondence attached.*

Stakeholder Input

Two items attached and nine other items on file with OSA.

Appendix A

History Of Post-Retirement Adjustments In TRS 1 And PERS 1

Date	TRS 1	PERS 1
3/21/61		Minimum pension $900/year if retired at age 70 with 10 or more years of service $60/month if 15-19 years of service $70/month if 20-24 years of service $80/month if 25-29 years of service $90/month if 30 or more years of service
3/21/67		Minimum benefit increases to: $60/month if 12-15 years of service $90/month if 16-19 years of service $120/month if 20 or more years of service
7/1/67	Pension portion of benefit increased to $5.50/month/year of service if age 65 and not qualified for Social Security.	
3/25/69		Minimum benefit increases to: $75/month if 12-15 years of service $100/month if 16-19 years of service $130/month if 20 or more years of service
7/1/70	Minimum benefit revised to $5.50/month/year of service. Applicable to members retiring before 4/1/69. Applied to the pension portion of the benefit.	The following received for each $1 of pension by year of retirement: '49 - $1.5239 '56 - $1.3687 '63 - $1.2116 '50 - $1.5386 '57 - $1.3485 '64 - $1.1960 '51 - $1.5239 '58 - $1.3031 '65 - $1.1813 '52 - $1.4110 '59 - $1.2601 '64 - $1.1620 '53 - $1.3805 '60 - $1.2501 '65 - $1.1291 '54 - $1.3702 '61 - $1.2116 '66 - $1.0980 '55 - $1.3643 '62 - $1.2255 '67 - $1.0536
7/1/71		5.95% COLA applied to pension portion of the benefit if retired before 12/31/70.
7/1/72	5.9% COLA for all members retired before 7/1/71, plus an additional 5.4% for those retired between 7/1/69 and 6/30/70.	
4/25/73		Minimum benefit of $6.50/month/year of service. 3% permanent increase based on assets in excess of current liabilities.

Date	TRS 1	PERS 1
7/1/73	$3/month/year of service for retirees not eligible for Social Security.	Increase of 1.0609% if the member retired before 1972 and their service retirement allowance was adjusted in section (1) for adjustment made of 4/25/73.
7/1/74	11.9% pension increase for those retired on 6/31/70. 2.9% pension increase for those retired 7/1/70 - 6/30/73. 3% COLA on total allowance for those retired on 12/31/73.	3% COLA for those retired prior to 12/31/73.
7/1/75		3% COLA for those retired prior to 12/31/74.
7/1/76	Minimum pension benefit of $7.50/month/year of service if retired prior to 4/25/73.	3% COLA for those retired prior to 12/31/75.
7/1/77	Minimum pension benefit of $8.00/month/year of service if retired prior to 4/25/73.	3% COLA for those retired prior to 12/31/76.
7/1/78		3% COLA for those retired prior to 12/31/77.
7/1/79	Minimum pension benefit of $10/month/year of service for retirees of 7/1/79. Disability and survivor benefits as of 12/31/78, and service benefits as of 7/1/74 permanently increased by $0.8171 multiplied by the member's years of service.	Minimum pension benefit of $10/month/year of service for retirees of 7/1/79. 3% COLA for those retired prior to 12/31/78.
7/1/80		3% COLA for those retired prior to 12/31/79.
7/1/81		Excess earnings adjustment no longer in effect as employer contribution rate increased above rate on 4/24/73.
7/1/83	$0.74/month/year of service COLA to disability and survivor benefits being received on 12/31/82 and service retirement benefits being received on 7/1/78.	
7/1/86	Minimum benefit increased to $13.00/month/year of service.	
7/1/87	Permanent automatic 3% annual increase to the minimum benefit becomes effective. Minimum pension benefit increased to $13.50/month/year of service.	
7/1/88	Minimum pension benefit increased to $13.82/month/year of service.	
7/1/89	Minimum pension benefit increased by $1 to $14.91/month/year of service and then increased 3% to $15.36/month/year of service. Permanent automatic COLA enacted for retirees whose age 65 purchasing power had been reduced by more than 40%.	
7/1/90	Minimum pension benefit increased 3% to $15.72/month/year of service. 3% COLA for eligible retirees.	

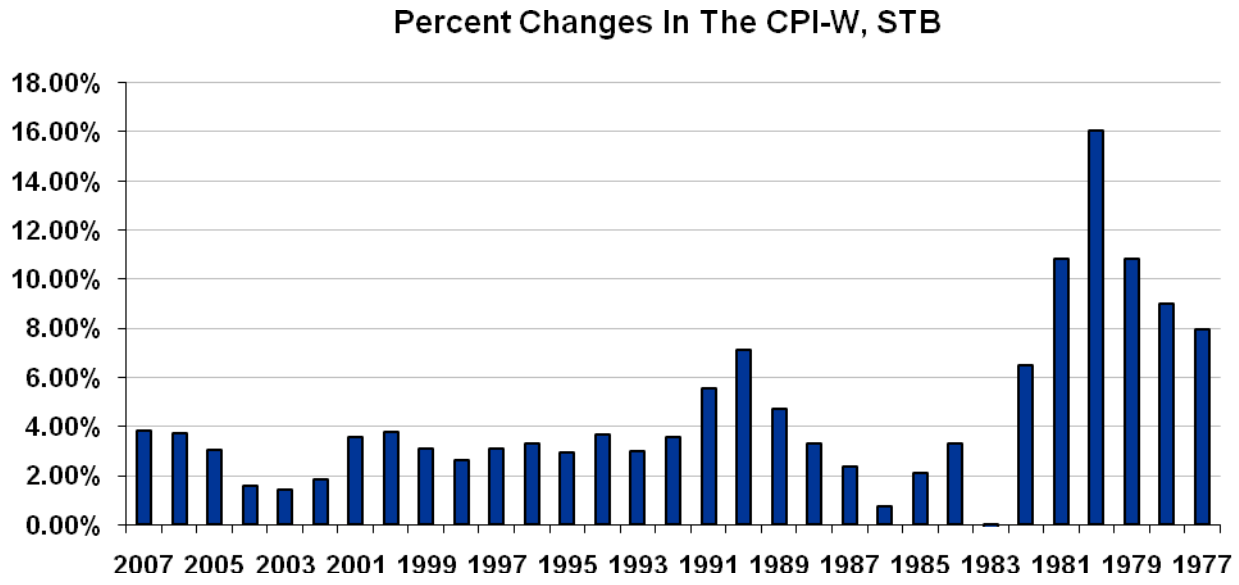
Date	TRS 1 PERS 1
7/1/91	Minimum pension benefit increased 3% to $16.19/month/year of service. 3% COLA for eligible retirees.
2/1/92	The current benefits of those eligible for the COLA adjusted to be equal to 60% of their age 65 retirement allowance.
7/1/92	Minimum pension benefit increased 3% to $16.68/month/year of service. 3% COLA for eligible retirees.
7/1/93	Minimum pension benefit increased 3% to $17.18/month/year of service. 3% COLA for eligible retirees. Continuation of special adjustment effective 2/92. Temporary ad hoc COLA effective through 6/30/94, $3/month/year of service for those retired 5 years, who were 70 years of age, and did not receive a COLA in 1992.
7/1/94	Minimum pension benefit increased 3% to $17.70/month/year of service. 3% COLA for eligible retirees. Special adjustment effective 2/92 made permanent. Temporary ad hoc COLA extended to 6/30/95. Provides $3/month/year of service to eligible retirees.
7/1/95	Uniform Increase established. Initial increase of $0.59/month/year of service to be increased by 3% per year. Retirees are eligible for the Uniform Increase if they have been retired at least one year and are age 66 by 7/1 in the calendar year in which the annual increase is given, or if their retirement allowance is lower than the minimum benefit amount. Minimum benefit increased to $24.22/month/year of service, and to automatically increase each year by the Annual Increase amount. Temporary ad hoc COLA that had been extended to 6/30/95 made permanent.
7/1/98	Gain-sharing established, providing even-year enhancements to the Annual Increase amount based on half the compound average investment returns in TRS 1 and PERS 1 plan assets over the previous four fiscal years that exceed 10%.
7/1/04	$1,000 minimum benefit (before optional benefit payments) established for retirees with 25 years of service and at least 20 years of retirement. Does not include an automatic increase. Effectively sunsets after the regular minimum increases to $40/month/year of service.
7/1/06	$1,000 minimum benefit (before optional benefit payments) extended to retirees with 20 years of service and at least 25 years of retirement. Automatic increase provided for $1,000 minimum of 3% per year.
7/1/07	Uniform COLA eligibility changed to include all retirees who have been retired one year and will have attained age 66 by 12/31 of the calendar year in which the increase is given.
7/22/07	Gain-sharing repealed after 2008 distribution. One-time increase in the Uniform COLA of $0.40*/month/year of service in lieu of future gain-sharing. **Thirty-five cents of the increase payable 1/1/08; five cents payable on 7/1/09.*

Appendix B
Consumer Price Index

Inflation is measured by the Consumer Price Index (CPI). The CPI records changes in the price of a set "market basket" of goods and services at different points in time. The U.S. Department of Labor publishes numerous indexes that measure inflation based on different market baskets and geographic regions. Each CPI produces a slightly different measure of inflation. The CPI most commonly used in Washington State's retirement systems is the Consumer Price Index for Urban Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB).

An individual may experience inflation quite different from that measured by the CPI if the goods and services purchased by the individual do not closely match the market basket used by the CPI.

The following graph shows historical rates of inflation based on annual changes in the CPI-W, STB. Data for the graph is provided on the following page.



Percent Changes In The CPI-W, STB

Year	CPI	Change
2007	623.65	3.79%
2006	600.9	3.73%
2005	579.3	3.02%
2004	562.3	1.57%
2003	553.6	1.41%
2002	545.9	1.81%
2001	536.2	3.55%
2000	517.8	3.75%
1999	499.1	3.10%
1998	484.1	2.63%
1997	471.7	3.10%
1996	457.5	3.30%
1995	442.9	2.90%
1994	430.4	3.66%
1993	415.2	2.98%
1992	403.2	3.54%
1991	389.4	5.53%
1990	369.0	7.11%
1989	344.5	4.68%
1988	329.1	3.30%
1987	318.6	2.35%
1986	311.3	0.71%
1985	309.1	2.08%
1984	302.8	3.27%
1983	293.2	-0.27%
1982	294.0	6.48%
1981	276.1	10.84%
1980	249.1	16.08%
1979	214.6	10.85%
1978	193.6	9.01%
1977	177.6	7.96%

Year	CPI	Changes
1976	164.5	5.58%
1975	155.8	10.11%
1974	141.5	10.98%
1973	127.5	6.52%
1972	119.7	2.84%
1971	116.4	2.11%
1970	114.0	4.40%
1969	109.2	4.90%
1968	104.1	4.10%
1967	100.0	2.99%
1966	97.1	2.75%
1965	94.5	1.18%
1964	93.4	1.41%
1963	92.1	1.66%
1962	90.6	1.46%
1961	89.3	1.59%
1960	87.9	1.27%
1959	86.8	1.88%
1958	85.2	2.28%
1957	83.3	4.13%
1956	80.0	1.27%
1955	79.0	0.51%
1954	78.6	0.00%
1953	78.6	1.29%
1952	77.6	2.51%
1951	75.7	7.68%
1950	70.3	1.44%
1949	69.3	-0.43%
1948	69.6	8.24%
1947	64.3	13.20%
1946	56.8	

Source U.S. Department of Labor, Bureau of Labor Statistics
CPI: Urban Wage Earners and Clerical Workers (Current Series)
Seasonal: Not Seasonally Adjusted
Area: Seattle-Tacoma-Bremerton, Washington
Base: Alternate (base period = 1967)
Item: All Items

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Public Employees for Pension Reform

A coalition of Washington State Public Employee Unions and Retiree Associations serving active and retired state and public employees

TO: Select Committee on Pension Policy (SCPP)

FROM: Public Employees for Pension Reform (PEPR)

DATE: June 17, 2008

RE: Options for Plan 1 COLA Improvement

During the April SCPP meeting, the PEPR coalition requested that the issue of Plan 1 Purchasing Power – COLA Improvement be placed on the Select Committee on Pension Policy's (SCPP) 2008 Interim agenda. At the direction of the Executive Committee, advocates were directed to work with the Office of the State Actuary and legislative fiscal committee staff to explore short and long-term options that address inadequacies of the current Plan 1 COLA.

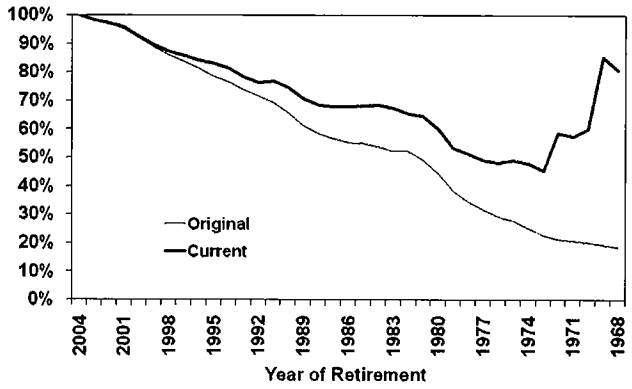
The Uniform Plan 1 COLA is not a true "Cost of Living Adjustment (COLA)" since it is not based on economic indicators such as the Consumer Price Index (CPI), but is "post-retirement adjustment" based on a *dollars/per month/per years of service formula*. The **Annual Increase**:

1. started at $.59 per month per years of service, effective 7/1/95;
2. increases each year by 3% (estimated at $1.73 per month, per year of service as of 7/1/08), and
3. is cumulative upon eligibility.

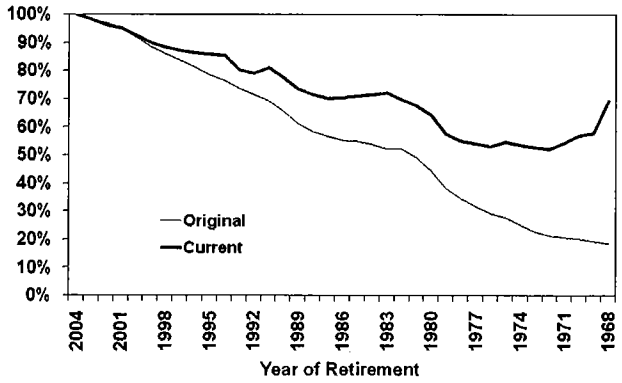
When the Uniform COLA was established in 1995, to help address *inadequacies* of the base annual increase amount and to make the benefit cost neutral with the COLA being replaced, certain **"Adjustments"** to the COLA's *annual increase amount* were granted to retirees based on age. Though these adjustments were of help, long-time retirees continue as those who have experienced the most severe losses of purchasing power.

In June of 2005 the Office of the State Actuary presented a briefing to SCPP members regarding Teachers Retirement System (TRS) and Public Employees Retirement System (PERS) Plan 1 Purchasing Power. The briefing indicated that even with the modest improvements that Gain Sharing provided to the Uniform Plan 1 COLA, erosions in the purchasing power of Plan 1 pension benefits continue. *As the dated charts provided for illustration purposes below indicate,* members of TRS/PERS Plan 1 who retired during the 1970s have lost approximately 50% of their purchasing power.

Purchasing Power of TRS 1 Service Benefits in 2004



Purchasing Power of PERS 1 Service Benefits in 2004



Source: Office of the State Actuary 6/8/05

The charts illustrate the percentage of purchasing power lost relative to the date retired. The line "current benefit" represents receipt of the original pension benefit, plus the Uniform Plan 1 "COLA." An updated briefing on the status of Plan 1 Purchasing Power, especially for long-time retirees would be helpful in providing SCPP members with a better picture of the value of pension benefits to Plan 1 retirees.

Short and long-term options that address inadequacies of the current TRS/PERS Plan 1 COLA that the PEPR coalition requests the SCPP's consideration of include:

Short-Term Plan 1 COLA Improvement

New Supplemental Adjustment to the Uniform COLA's **Annual Increase** granted 7/1/09 based on the year of retirement:

- 1985-90 — $0.75 per month/per years of service (approximate benefit increase of $22.50 per month for a retiree with *30 years of service*)
- 1980-84 — $1.00 per month/per years of service (approximate benefit increase of $30.00 per month for a retiree with *30 years of service*)
- 1979 and earlier* — $1.50 per month/per years of service (approximate benefit increase of $45.00 per month for a retiree with *30 years of service*)

* Also includes current recipients of the Minimum Benefit retired before 1979.

The design of the benefit improvement is a variation of the '95 adjustments to provide a supplemental adjustment to the annual increase of the Uniform Plan 1 COLA based on year of retirement. This option would provide relief to those who have been retired the longest, and have experienced the most severe losses in purchasing power.

Long-Term Plan 1 COLA Improvement

Replace Uniform "COLA" with a true *Cost-of-Living Adjustment* (COLA):

- based on 100% of the Consumer Price Index (CPI) up to 3% (banked)
- CPI: Urban Wage Earners & Clerical Workers, Seattle-Tacoma-Bremerton, WA – All Items
- paid/compounded annually
- beginning 1 year after retirement
- preferably retroactive up to limits provided by the Internal Revenue Service (IRS); but possibly prospective.

This option would bring uniformity to COLA benefit design between systems and plans.

The measure of a defined pension plan's worth is how it retains its value over the retirement years of plan members. The value of TRS/PERS Plan 1 pension benefits needs to be protected from substantial losses in purchasing power which occur due to the design of Plan 1, especially for long-time retirees. The PEPR coalition looks forward to addressing the critical issue of Plan 1 purchasing power with SCPP members this Interim.

PEPR
(Public Employees for Pension Reform)

Washington State Federation of State Employees (WFSE)
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Public Employees for Pension Reform

A coalition of Washington State Public Employee Unions and Retiree Associations serving active and retired state and public employees

TO: Select Committee on Pension Policy (SCPP)

FROM: Public Employees for Pension Reform (PEPR)

DATE: October 7, 2008

RE: Revised Proposals for Plan 1 COLA Improvement

RECEIVED
OCT 7 - 2008
Office of
The State Actuary

Members of the Public Employees for Pension Reform (PEPR) coalition appreciate the Select Committee on Pension Policy's (SCPP) 9/16/08 Work Session on Plan 1 Purchasing Power. The briefing by staff from the Office of the State Actuary (OSA) provided a much-needed update on the current status of Plan 1 pension benefits, as well as important information on policy and cost considerations related to the PEPR coalition's proposals for short and long-term Plan 1 COLA improvement. We also greatly appreciate the authorization by SCPP Executive Committee members for PEPR coalition members to put forth a revised set of proposals that would reduce costs from estimates on the original COLA improvement proposals.

In refection of the updated data regarding lost purchasing power, our continuing goal of broad-based COLA enhancement, and the budget challenges facing employers in the 2009-11 biennium and beyond, members of the PEPR coalition offer the following revised proposals for Plan 1 COLA improvement:

Key changes noted in **bold** print.

Short-Term Plan 1 COLA Improvement

New Supplemental Adjustment to the Uniform COLA's Annual Increase granted 7/1/09 based on the year of retirement:

- 1985-90 ~~$0.75~~ **$0.35** per month/per years of service
  (approximate benefit increase of ~~$22.50~~ $10.50 per month for a retiree with *30 years of service*)
- 1980-84 ~~$1.00~~ **$0.50** per month/per years of service
  (approximate benefit increase of ~~$30.00~~ $15.00 per month for a retiree with *30 years of service*)
- 1979 and earlier* ~~$1.50~~ **$0.75** per month/per years of service
  (approximate benefit increase of ~~$45.00~~ $22.50 per month for a retiree with *30 years of service*)

Based on year of retirement, the design of the proposed benefit improvement is a variation of the '95 age based adjustments to provide a supplemental adjustment to the annual increase of the Uniform Plan 1 COLA. This option would provide a degree of relief to those who have been retired the longest, and have experienced the most severe losses in purchasing power, while acknowledging budget challenges facing employers.

Long-Term Plan 1 COLA Improvement

Replace Uniform "COLA" with a true *Cost-of-Living Adjustment* (COLA):

- based on 100% of the Consumer Price Index (CPI) up to 3% (banked)
- CPI: Urban Wage Earners & Clerical Workers, Seattle-Tacoma-Bremerton, WA – All Items
- prospective only
- paid/compounded annually
- ~~beginning 1 year after retirement~~ **beginning in July the retiree turns age 66** (to coincide more closely with COLA eligibility for Plans 2/3 and the current Uniform Plan 1 COLA)
- **CPI measured from date of retirement** (to coincide with methods of calculating the COLA for Plans 2/3)
- **annual benefit to be the greater of this CPI-based COLA or the Uniform COLA** (to ensure no loss of benefit).

This option would bring uniformity to COLA benefit design between systems and plans and protect the value of Plan 1 pension purchasing power while acknowledging budget challenges facing employers and the desire to contain COLA eligibility policy.

The PEPR coalition looks forward to continuing this dialogue with SCPP members to develop solutions to the critical issue of recovery of Plan 1 purchasing power.

Public Employees for Pension Reform (PEPR)

Washington State Federation of State Employees
Matt Zuvich, Chair – 306-352-7603

American Federation of Teachers of Washington
Washington Public Employees Association
Washington State Council of City & County Employees – Council 2
Retired Public Employees Council of Washington
Association of Washington School Principals
Washington Association of School Administrators
Public School Employees of Washington
Washington Education Association
Washington Education Association – Retired
Washington State School Retirees' Association

Visiting International Faculty

Description Of Issue

Should visiting teachers from other countries be exempt from retirement system membership?

The Visiting International Faculty Program (VIF) is a sponsor under the U.S. Department of State's Exchange Visitor Program. VIF would like to sponsor visiting teachers in Washington, and is requesting an exemption from membership in the Teachers' Retirement System (TRS) Plans 2/3. These teachers would not stay in the state long enough to earn a pension. Exempting them would mean that employer and member contributions would not be collected for these teachers, and refunds of member contributions would not be required when they leave.

Based on experience in other states, the program could grow to about 200-300 teachers statewide.

Policy Highlights

- A similar exemption exists in TRS Plan 1.
- DRS supports the idea of the exemption to alleviate administrative concerns.
- The two peer states that participate in the Exchange Visitor Program provide an exemption.
- An exemption is consistent with federal policies.
- An exemption adds membership complexity.
- An exemption spreads Plan 1 UAAL cost to non-participating employers.
- Impacts would reach beyond the pension system.

Committee Activity

Staff briefed the Committee at its November meeting and the SCPP took no further action.

Recommendation To 2009 Legislature

None.

Staff Contact

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Visiting International Faculty

In Brief

ISSUE

Should the SCPP recommend legislation to exempt visiting teachers from other countries from membership in the Teachers Retirement System Plans 2 and 3 (TRS 2/3)?

MEMBER IMPACT

The proposal would impact TRS 2/3 beginning in the 2010-2011 school year. If legislation were passed, the proponents intend to place approximately 20 visiting international teachers in Washington in the first year, depending on the economy. Based on experience in other states, the program could grow to about 200-300 teachers statewide.

According to the 2007 Actuarial Valuation Report there are approximately 58,600 active members in TRS 2/3.

Laura Harper
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Current Situation

The Director of Government Relations for the Visiting International Faculty Program (VIF) reports that several school districts have asked VIF to bring international teachers to Washington. Also, according to VIF, teachers around the world are expressing interest in working in Washington. Typically VIF seeks to address statutory and regulatory concerns prior to bringing teachers to a specific state. VIF requests a statutory change to the Teachers' Retirement System Plans 2 and 3 (TRS 2/3). The proposal would exempt visiting international teachers from retirement system membership.

Under current TRS 2/3 provisions, visiting teachers who come from other countries to work full time on a temporary basis are required to become contributing members of TRS Plan 2 or 3. When they leave employment they are eligible for a refund of their member contributions.

TRS History

TRS Plan 1 has the following membership exemption: "All teachers employed full-time in the public schools shall be members of the system *except alien teachers who have been granted a temporary permit to teach as exchange teachers*." (Emphasis added.) TRS 1 closed in 1977. The membership exemption was not continued in TRS 2/3. The reason for discontinuing the exemption is unknown, but we do know that many ancillary benefits were discontinued or reduced when Washington closed Plan 1 and opened the Plans 2/3.

What Is The VIF Program?

VIF was founded in 1989 and provides U.S. schools with full-time visiting teachers from fifty nations. Teachers serve for one to three years. The program provides screening, preparation, and support services for visiting teachers.

The VIF Program is a private organization and a designated sponsor in the Exchange Visitor Program under the U.S.

Department of State. The Exchange Visitor Program is carried out under a federal act entitled the Mutual Educational and Cultural Exchange Act of 1961. Its purpose is to foster mutual understanding between the people of the United States and the people of other countries through educational and cultural exchanges.

All exchange visitors are expected to return home upon completion of their program in order to share their U.S. experiences with people in their home country. As stated in federal regulations, these exchanges enable visitors to better understand American culture, society, and teaching practices at the primary and secondary levels. See 22 CFR 62.24(a). They also enhance American knowledge of foreign cultures, customs, and teaching approaches.

Federal regulations set minimum requirements for visitor eligibility. Sponsors such as the VIF Program must adequately screen teacher qualifications, reputation, and character prior to accepting them into the program. Visiting teachers must receive a special visa (known under the regulations as a "J-1" visa) and may participate in the program for a maximum of three years. They also must obtain a Social Security card and pay taxes on salary or wages earned in the U.S., although some are subject to bilateral tax treaties affecting federal taxation. FICA payments are triggered after 180 days, unless they already have a Social Security card from previous work or study in the U.S.

VIF is a sponsor under the U.S. Department of State's Exchange Visitor Program.

VIF is the largest U.S. sponsor for teachers in the State Department's Exchange Visitor Program. The State Department does not recommend or "rate" any of the designated sponsors, however; by virtue of its State Department status, the VIF Program has complied with all applicable regulations for obtaining designation and is in good standing.

There are approximately sixty other sponsors for teachers under the federal program; however, most of these place very few teachers compared to VIF. According the VIF's Director of Government Relations, the second largest sponsor in the U.S. is the Ministry of Education for the Spanish Embassy, which places no more than about 400 teachers per year nationwide. VIF partners with the Ministry in some states to recruit and support teachers from Spain.

Other States

Two peer states, California and Florida, participate in VIF's program. Their visiting teachers are exempt from retirement system membership.

In the fall of 2008 the VIF Program staff discussed its program with OSA staff. At that time it sponsored about 1,500 teachers in 1,000 schools within seven participating states. Once VIF moves into a state, its practice is to allow the program to grow. On average, programs in other participating states have grown to about 200-300 visiting teachers per year.

As of December, 2008 the VIF Program provided teachers in two of Washington's peer states: California and Florida. Both of these states exempt visiting teachers from retirement system membership. Florida requires a temporary visa and has a three-year limit on exempt employment. (These requirements are consistent with federal regulations.) California's membership exemption is much broader and simply excludes "exchange teachers or sojourn teachers from outside of this state" from retirement system membership.

The VIF Program started in North Carolina. In addition to California and Florida, VIF places teachers in Georgia, Maryland, South Carolina, and Virginia. At this time, all participating states have membership exemptions for participants except Maryland. (The VIF Program has not yet asked for an exemption there.)

Policy Analysis

The issue for policy makers is whether to exempt visiting teachers from other countries from membership in TRS 2/3. This section will summarize the impacts on TRS of providing the proposed exemption. It will also discuss the pros and cons of a membership exemption from a policy perspective. Finally, this section identifies questions that reach beyond the pension system, and which may be of interest to other legislative committees and/or groups.

How Would The Proposal Impact TRS?

Currently, visiting teachers from other countries who teach full-time in eligible positions must pay member contributions to the retirement system. Similarly, their employers must pay contributions on their behalf. When their visas expire

Visiting teachers stay for one to three years and do not earn a pension.

and they leave their teaching positions, they can apply for refunds of member contributions. The employer contributions remain with TRS.

Under the proposal, temporary visiting teachers would be exempt from retirement system membership. This means that the Department of Retirement Systems (DRS) would not collect member or employer contributions for these teachers. No service credit would accrue and DRS would have no obligation to provide refunds of member contributions after visiting teachers leave employment.

How many positions would be affected in TRS? Passing the exemption would trigger action by VIF to work with school districts to temporarily fill certain TRS positions with visiting teachers. The proponents have stated that they intend to place approximately twenty visiting teachers in the 2010-2011 school year, depending on the economy.

Within a four- to five-year period VIF would allow the program to grow. Looking at programs in other states, full program capacity would mean a presence of 200-300 temporary visiting teachers within the state. (Note: While there are other designated sponsors under the State Department's Exchange Visitor Program, those sponsors do not bring large numbers of teachers to the U.S. and are not expected to add significantly to the number of visiting teachers in Washington.)

The fiscal impacts of a membership exemption have not been identified for this initial briefing. If the SCPP decides to pursue the proposal, it can direct staff to prepare a bill draft and draft fiscal note.

What Are Some Reasons For A Membership Exemption?

Addresses Administrative Concerns

Visiting international teachers do not remain in the U.S. long enough to become vested in Plan 2 or in the defined benefit portion of Plan 3. Some policy makers may question whether visiting teachers should be processed as members when they are non-citizens and will not stay long enough to earn a pension.

DRS supports the idea of exempting visiting teachers from membership in TRS 2/3.

The Department of Retirement Systems (DRS) supports the idea of exempting visiting teachers from other countries from retirement system membership. Why? Because

visiting teachers would be eligible for refunds upon termination of employment.

DRS has expressed concerns about the administrative impacts of locating individuals who leave the country before requesting to withdraw their member contributions. Tracking people overseas can be difficult, time-consuming, and expensive.

Consistent with Federal Policies

A TRS exemption would be consistent with the federal preference that visiting temporary teachers should not garner assets in this country. The program is designed for visitors, and garnering U.S. assets gives visitors an incentive to remain in the country. This is inconsistent with the premise of the Exchange Visitor Program.

The proposal also supports the federal policies of the U.S. State Department's Exchange Visitor Program by making it easier to attract visiting international teachers. For the teachers themselves, many of whom are required to continue accruing pension benefits in their home country, this approach avoids double pension payments and the complexity of multiple benefits.

Consistent with TRS 1

The membership exemption already exists in TRS 1. An exemption in TRS 2/3 would provide consistency with that Plan.

Visiting Teacher Convenience

The exemption may also be easiest for visiting teachers, as they will not be required to go through an administrative process that is designed for members working toward a pension. The exemption also frees up dollars for teacher expenses while they are in the U.S.

What Are Some Reasons Against The Exemption?

Adds Membership Complexity

The TRS 2/3 membership provisions are inclusive and do not provide special exemptions to other groups of active members working in eligible positions. Adding this exemption adds complexity to the membership provisions.

Currently all teachers who work full time in an "eligible position" must join TRS (unless retired, receiving a disability benefit, or removed from membership for a terminal illness). An eligible position normally requires five or more months of 70 or more hours of compensated employment from September through August. This definition would include visiting teachers under the Exchange Visitor Program.

Exempting visiting teachers spreads UAAL cost to employers who aren't participating in the VIF Program.

Spreads UAAL Cost to Non-Participating Employers

If employer contributions are not collected for visiting teachers because they are exempted from membership, then all TRS employers would experience a small increase in cost for the TRS 1 unfunded actuarial accrued liability, or UAAL. The UAAL is past cost for TRS 1 that is still unpaid. Current funding policy requires that this cost be spread among all TRS employers and collected as a percent of active teacher salaries. If the number of covered teacher salaries decreases by 200-300, the Plan 1 UAAL cost that would have been paid by employers for those teachers must be spread to remaining employers.

Eliminates a Mandatory Savings Plan for Visiting Teachers

Finally, from the perspective of visiting teachers, the membership exemption eliminates a mandatory savings plan that could benefit them they after they leave employment in the U.S. For those who do not accrue pension benefits in their home country while participating in the Exchange Visitor Program, the loss of these savings is more significant.

Impacts Would Reach Beyond The Pension System

Some impacts of this issue reach beyond the pension system. For this reason, it may be desirable for other groups and legislative committees to weigh in on the decision.

The retirement system membership exemption is a factor in VIF's decision to come to a state. Once it initiates the program, a number of positions that are currently filled by U.S. teachers would be filled by teachers from other countries.

The membership exemption helps facilitate the VIF program. The exemption frees up dollars for recruiting, screening, and supporting international teachers - services that most school districts cannot undertake to

independently provide. (Examples include interest-free start-up loans to teachers, leased cars, health insurance coverage, visa services, orientation, and on-going problem solving.) VIF provides these services for a fee that is paid by school districts. The dollars that would have been paid for pension contributions are paid to the sponsor. Because the exemption helps facilitate sponsorship of visiting teachers, those who favor this type of cultural exchange program for Washington's public schools would presumably favor the exemption.

For those who do not wish to see an expanded program for visiting international teachers in Washington, a membership exemption may be objectionable. Some may prefer that as many Washington teacher positions as possible remain available to U.S. teachers. There may be concerns that a membership exemption would encourage the program to grow and therefore should not be pursued, especially in times of economic downturn.

Conclusion

There are pros and cons to exempting visiting teachers from TRS membership. Some reasons to support a membership exemption include: administrative concerns with refunds, consistency with federal policies, consistency with TRS Plan 1 and practices in participating peer states, and visiting teacher convenience. Some reasons against the exemption are: adding membership complexity, spreading Plan 1 UAAL costs to other TRS employers who are not participating in the program, and eliminating a mandatory savings plan for visiting teachers. Policy makers will weigh the significance of these pros and cons.

The impacts of a retirement system membership exclusion for visiting teachers from other countries reach beyond the pension system. It may be desirable for other groups and legislative committees to consider those impacts and weigh in on the decision.

Possible SCPP Strategies

1. **Sponsor.** Move the proposal forward as potential SCPP request legislation.

2. **Endorse.** Move the issue forward as potential SCPP endorsed legislation.
3. **Request further study.** Move the issue forward for further study.
4. **Monitor.** Monitor the issue for possible future action.
5. **No action.** Take no action and treat the matter as information only.

Stakeholder Input

Correspondence attached from:

Mary Donny, Director of Government Relations, VIF, 9/18/2008

Correspondence on file from:

Mary Donny, Director of Government Relations, VIF, 9/22/2008

David Young, CEO, VIF, 11/5/2008

Supporting Information

The attached Fact Sheet was submitted by the VIF Program.

Committee Activity

Staff briefed the Full Committee on VIF's proposal at its November meeting. The SCPP took no further action.

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VISITING INTERNATIONAL FACULTY PROGRAM℠ | Transforming Lives Through International Exchange

Post Office Box 3566 • Chapel Hill, NC 27515 • USA • phone 919.967.5144 • fax 919.967.8224 • www.vifprogram.com

September 18, 2008

The Honorable Mark Schoesler
Chair
The Honorable Steve Conway
Select Committee on Pension Policy
The Office of the State Actuary
P.O. Box 40914
Olympia, WA 98504-0914

Dear Mr. Chair, Mr. Vice Chair and Members of the SCPP,

I am writing on behalf of the Visiting International Faculty Program (VIF) d/b/a the Center for International Education, Inc. currently, the VIF Program is the largest J-1 international teacher exchange program in the United States and is a sponsoring agency as designated by the US Department of State (Exchange Visitor Program P-4-10082).

Since 1989, VIF teachers have transformed the educational experience of American students, invigorating their schools and communities with meaningful encounters. Participating teachers have been highly successful, succeeding at a rate of around 96%. Many have won school-wide, district-wide and statewide awards. The result has been both excellent instruction and daily intercultural interaction for tens of thousands of U.S. students. Last year we hosted over 1650 teachers from 50 different countries and placed them in 7 states including Maryland, Virginia, North Carolina, South Carolina, Georgia, Florida and California.

Before we begin to bring our teachers to a specific state, we work to make sure that there are no regulatory or statutory barriers that would prevent exchange teachers from working in the state. Over the past few years, we have been approached by several school districts requesting VIF to bring our international exchange teachers to Washington. We believe international teachers would find the state of Washington an attractive location to serve as highly qualified educators and cultural ambassadors.

As you may be aware, under the federal J-1 teacher regulations as written in 22 CFR 62.24, there is a subdivision that notes that while the teachers may take a full-time position, they are here on a temporary (non-immigrant) basis. Specifically, the regulations outline the following in 22 CFR 62.24 2 (e) *Teaching position. …The exchange visitor's appointment to a position at a primary or secondary accredited educational institution shall be temporary, even if the teaching position is permanent.* Our government prefers that the teachers not garner assets while they are here in the US. In fact, some of our exchange teachers are granted leave from their home countries and continue to receive pension credits (civil servant status) while they are in the US on our exchange program. At this time, all the states in which we work, except Maryland, exclude exchange teachers from participation in their retirement systems. (We have not yet asked to be excluded from Maryland's system at this time for non-related reasons).

I am therefore writing to request an exemption from the TRS Plans 2 and 3 on behalf of J-1 exchange teachers. We have been touch with the Washington Teachers' Retirement System (Jeff Wickman and Sandra J. Matheson) regarding this issue. They have indicated that while there is an exception to TRS 1 for "alien" teachers, there is no such exemption to TRS Plans 2 and 3 and that a legislative remedy is required.
The TRS Plan 1 language in RCW 41.32.240 states….(1) *All teachers employed full time in the public schools shall be members of the system except alien teachers who have been granted a temporary permit to teach as exchange teachers.* Given that there is precedence for an exemption, we ask your consideration of extending that exemption to TRS Plans 2 and 3.

Thank you for your review of our request. I am happy to address any questions you may have or provide any additional information you may require.

Sincerely,

Mary Donny
Director of Government Relations

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Fact Sheet

The Visiting International Faculty Program is the United States' largest international-exchange program for U.S. schools and teachers worldwide. VIF searches the globe for the finest educators to serve as full-time classroom teachers and cultural ambassadors, providing a new generation with an international education to succeed in the global marketplace.

Designated as an official sponsor in the U.S. State Department's Exchange Visitor Program, VIF carefully selects highly qualified teachers from more than 50 nations, matches them with U.S. schools and provides comprehensive support to help ensure a rewarding experience.

VIF provides teachers the professional-development experience of teaching in the United States for up to 3 years before returning home to serve as goodwill ambassadors for the U.S. Since 1989, more than 8,000 VIF teachers have positively influenced the lives of more than a million students, educators and community members.

Some key facts about VIF:

- VIF is the largest international-exchange program for U.S. schools and teachers worldwide. This school year, VIF is sponsoring 1,500 highly qualified teachers in 1,000 schools.
- Teachers serve with VIF for 1 to 3 years and return home to share their experiences with students and colleagues, contributing to education in their nations and to a better understanding of the U.S. abroad.
- VIF's thorough selection process includes a detailed application with essays, verification of credentials and experience, professional references, criminal-background checks and personal interviews. VIF is highly selective, placing only 7% of applicants in U.S. schools.
- VIF teachers must be proficient in English, hold a university degree or teaching diploma equivalent to a U.S. bachelor's degree in education, and have had teacher training and experience at the elementary or secondary level.
- VIF's comprehensive support helps ensure a rewarding experience. VIF teachers and host principals are highly satisfied, independent surveys show: 98% of VIF alumni would recommend VIF to a fellow teacher, and school districts rate their VIF teachers as a 9 on a 10-point scale.
- Schools in several U.S. states participate with VIF, including North Carolina, Georgia, Virginia, South Carolina and Florida.
- VIF educators teach more than 20 subjects, including elementary education, a variety of languages, English as a second language, math, science, special education and many more.
- VIF teachers represent over 50 nations, including Argentina, Australia, Canada, Colombia, Costa Rica, Denmark, Ecuador, France, Germany, Ireland, Jamaica, Mexico, New Zealand, Peru, the Philippines, South Africa, Spain, the United Kingdom and Venezuela.

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