

Summary of Draft Legislation

Duty Disability Benefits

Background:

A service-connected disability pension benefit may be nontaxable under the Internal Revenue Code if it meets certain requirements. In order to qualify, the benefit cannot be based on a member's age or years of service. If a service-connected disability provision provides a benefit based on age and/or years of service, subject to minimum that is not based on years of service, the minimum benefit can qualify for favorable tax treatment.

A LEOFF Plan 2 member who separates from service as a result of a service-related disability may choose to either withdraw their accumulated contributions and interest or receive a disability pension if they have five years of service. The member is entitled to 150% of their contributions if they have ten or more years of service. Employer contributions are not included in the withdrawal. The disability pension is actuarially reduced based on the member's age if the member has not reached age 53.

Historically, the great majority of disabled members have chosen the withdrawal option.

Legislation:

The bill would provide that all LEOFF 2 members who separate from service as a result of service-related disability would be entitled to withdraw 150% of their accumulated contributions. This benefit would be entirely nontaxable. If the member chooses this benefit, they would not be eligible for a disability pension.

The bill would also provide that all LEOFF 2 members who separate from service as a result of service-related disability would be entitled to receive a minimum disability pension equivalent to ten percent of their average final salary. The minimum benefit would not be actuarially reduced based on the member's age. This minimum benefit would be nontaxable. The member may receive additional pension benefits for each year of service beyond five years. These additional benefits would be subject to actuarial reduction and would be taxable in the same manner as current disability pension benefits.

The bill includes a cap on the additional disability benefits so that the combined minimum benefit and additional benefits could not exceed the disability pension amount provided in current law.

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Copy of Z-0970.1/04 by LL:seg provided on 12/3/03.

Brief Description: Providing benefits to certain disabled members of the law enforcement officers' and fire fighters' retirement system plan 2.

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ELECTRONIC TRANSMITTAL

AN ACT Relating to providing benefits to certain disabled members of the law enforcement officers' and fire fighters' retirement system plan 2; amending RCW 41.26.470; and creating a new section.

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

Sec. 1. RCW 41.26.470 and 2001 c 261 s 2 are each amended to read as follows:

(1) A member of the retirement system who becomes totally incapacitated for continued employment by an employer as determined by the director shall be eligible to receive an allowance under the provisions of RCW 41.26.410 through 41.26.550. Such member shall receive a monthly disability allowance computed as provided for in RCW 41.26.420 and shall have such allowance actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age fifty-three.

(2) Any member who receives an allowance under the provisions of this section shall be subject to such comprehensive medical examinations as required by the department. If such medical examinations reveal that such a member has recovered from the incapacitating disability and the member is no longer entitled to

benefits under Title 51 RCW, the retirement allowance shall be canceled and the member shall be restored to duty in the same civil service rank, if any, held by the member at the time of retirement or, if unable to perform the duties of the rank, then, at the member's request, in such other like or lesser rank as may be or become open and available, the duties of which the member is then able to perform.

In no event shall a member previously drawing a disability allowance be returned or be restored to duty at a salary or rate of pay less than the current salary attached to the rank or position held by the member at the date of the retirement for disability. If the department determines that the member is able to return to service, the member is entitled to notice and a hearing. Both the notice and the hearing shall comply with the requirements of chapter 34.05 RCW, the Administrative Procedure Act.

(3) Those members subject to this chapter who became disabled in the line of duty on or after July 23, 1989, and who receive benefits under RCW 41.04.500 through 41.04.530 or similar benefits under RCW 41.04.535 shall receive or continue to receive service credit subject to the following:

(a) No member may receive more than one month's service credit in a calendar month.

(b) No service credit under this section may be allowed after a member separates or is separated without leave of absence.

(c) Employer contributions shall be paid by the employer at the rate in effect for the period of the service credited.

(d) Employee contributions shall be collected by the employer and paid to the department at the rate in effect for the period of service credited.

(e) State contributions shall be as provided in RCW 41.45.060 and 41.45.067.

(f) Contributions shall be based on the regular compensation which the member would have received had the disability not occurred.

(g) The service and compensation credit under this section shall be granted for a period not to exceed six consecutive months.

(h) Should the legislature revoke the service credit authorized under this section or repeal this section, no affected employee is entitled to receive the credit as a matter of contractual right.

(4)(a) If the recipient of a monthly retirement allowance under this section dies before the total of the retirement allowance paid to

the recipient equals the amount of the accumulated contributions at the date of retirement, then the balance shall be paid to the member's estate, or such person or persons, trust, or organization as the recipient has nominated by written designation duly executed and filed with the director, or, if there is no such designated person or persons still living at the time of the recipient's death, then to the surviving spouse, or, if there is neither such designated person or persons still living at the time of his or her death nor a surviving spouse, then to his or her legal representative.

(b) If a recipient of a monthly retirement allowance under this section died before April 27, 1989, and before the total of the retirement allowance paid to the recipient equaled the amount of his or her accumulated contributions at the date of retirement, then the department shall pay the balance of the accumulated contributions to the member's surviving spouse or, if there is no surviving spouse, then in equal shares to the member's children. If there is no surviving spouse or children, the department shall retain the contributions.

(5) Should the disability retirement allowance of any disability beneficiary be canceled for any cause other than reentrance into service or retirement for service, he or she shall be paid the excess, if any, of the accumulated contributions at the time of retirement over all payments made on his or her behalf under this chapter.

(6) A member who becomes disabled in the line of duty, and who ceases to be an employee of an employer except by service or disability retirement, may request a refund of one hundred fifty percent of the member's accumulated contributions. Any accumulated contributions attributable to restorations made under RCW 41.50.165(2) shall be refunded at one hundred percent. A person in receipt of this benefit is a retiree.

(7) A member who becomes disabled in the line of duty shall be entitled to receive a minimum retirement allowance equal to ten percent of such member's final average salary. The member shall additionally receive a retirement allowance equal to two percent of such member's average final salary for each year of service beyond five, and shall have the allowance actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age fifty-three. An additional benefit shall not result in a total monthly benefit greater than that provided in subsection

(1) of this section.

NEW SECTION. **Sec. 2.** This act applies to all members, subject to section 1 of this act, who become or became disabled in the line of duty on or after January 1, 2001.

FISCAL NOTE - DRAFT

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/15/04	Z-0970.1/04

SUMMARY OF BILL:

This bill impacts the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2 by providing that members disabled in the line of duty may receive a refund of 150% of their contributions (except for contributions made to restore service credit, which are refunded at 100%).

Alternatively, such members may choose a minimum retirement allowance equal to 10 percent of their final average salary, plus an additional allowance of 2% of final average salary for each year of service beyond 5 years subject to an actuarial reduction from age 53. The additional allowance shall not result in a total monthly benefit that exceeds that of a member who has been determined by the director to be totally incapacitated.

Effective Date: 90 days after session, but retroactively applies to members who became disabled in the line of duty on or after January 1, 2001.

CURRENT SITUATION:

Currently disabled members may receive an earned benefit actuarially reduced from age 53 or a refund of contributions.

MEMBERS IMPACTED:

We estimate that all the 14,011 active members of LEOFF 2 would be affected by this bill. Our experience data, however, indicate that few would become disabled in the course of employment and, as a result, few would actually receive this enhanced benefit.

We estimate that duty-related disablements will occur at a rate of 0.085% each year.

ASSUMPTIONS:

We have assumed that duty-related disablements will occur at a rate of 0.085% each year. This assumption is based on the combined duty and non-duty disability rate in the Washington State Patrol Retirement Plan of .1% multiplied by the ratio of duty disabilities to total disabilities of 85% in LEOFF 1.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

Law Enforcement Officers' and Fire Fighters' Retirement System Plan 2			
<i>(Dollars in Millions)</i>			
	Current	Increase	Total
Actuarial Present Value of Projected Benefits (The Value of the Total Commitment to all Current Members)	\$4,042	\$1	\$4,043
Unfunded Actuarial Accrued Liability (The Portion of the Plan 1 Liability that is Amortized at 2024)	NA	NA	NA
Unfunded Liability (PBO) (The Value of the Total Commitment to all Current Members Attributable to Past Service)	\$(709)	\$1	\$(708)
Increase in Contribution Rates:			
Employee		.01%	
Employer		.01%	
State		.00%	

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

Costs (in Millions):

2004-2005

State:

General Fund	\$0.0
Non-General Fund	<u>0.0</u>
Total State	\$0.0
Local Government	\$0.1
Total Employer	\$0.1
Total Employee	\$0.1

2005-2007

State:

General Fund	\$0.0
Non-General Fund	<u>0.0</u>
Total State	\$0.0
Local Government	\$0.2
Total Employer	\$0.2
Total Employee	\$0.2

2004-2029

State:

General Fund	\$0.0
Non-General Fund	<u>0.0</u>
Total State	\$0.0
Local Government	\$6.0
Total Employer	\$6.0
Total Employee	\$6.0

STATEMENT OF DATA AND ASSUMPTIONS USED IN PREPARING THIS FISCAL NOTE:

The costs presented in this fiscal note are based on our understanding of the bill as well as generally accepted actuarial standards of practice including the following:

1. Costs were developed using the same membership data, methods, assets and assumptions as those used in preparing the September 30, 2002 actuarial valuation report of the Law Enforcement Officers' and Fire Fighters' Retirement System Plan 2 (LEOFF 2) .
2. As with the costs developed in the actuarial valuation, the emerging costs of the System will vary from those presented in the valuation report or this fiscal note to the extent that actual experience differs from that projected by the actuarial assumptions.
3. Additional assumptions used to evaluate the cost impact of the bill which were not used or disclosed in the actuarial valuation report or in the body of this fiscal note above not include the following: None.
4. The analysis of this bill 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.
5. This fiscal note is intended for use only during the 2004 Legislative Session.
6. The funding method used for Plan 1 utilizes the Plan 2/3 employer/state rate as the Normal Cost and amortizes the remaining liability (UAAL) by the year 2024. Benefit increases to Plan 2/3 will change the UAAL in Plan 1. The cost of benefit increases to Plan 1 increases the UAAL.
7. Plan 2/3 utilizes the Aggregate Funding Method. The cost of Plan 2/3 is spread over the average working lifetime of the current active Plan 2/3 members.

GLOSSARY OF ACTUARIAL TERMS:

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.)

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.

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.

Unfunded Actuarial Accrued Liability (UAAL): The cost of Plan 1 is divided into two pieces:

- The Normal Cost portion is paid over the working lifetime of the Plan 1 active members. The remaining cost is called the UAAL.
- The UAAL is paid for by employers as a percent of the salaries of all plan 1, 2 and 3 members until the year 2024.

Pension Benefit Obligation (PBO): The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date (past service).

Unfunded Liability (Unfunded PBO): The excess, if any, of the Pension Benefit Obligation over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.