Contribution Rates Preliminary Report

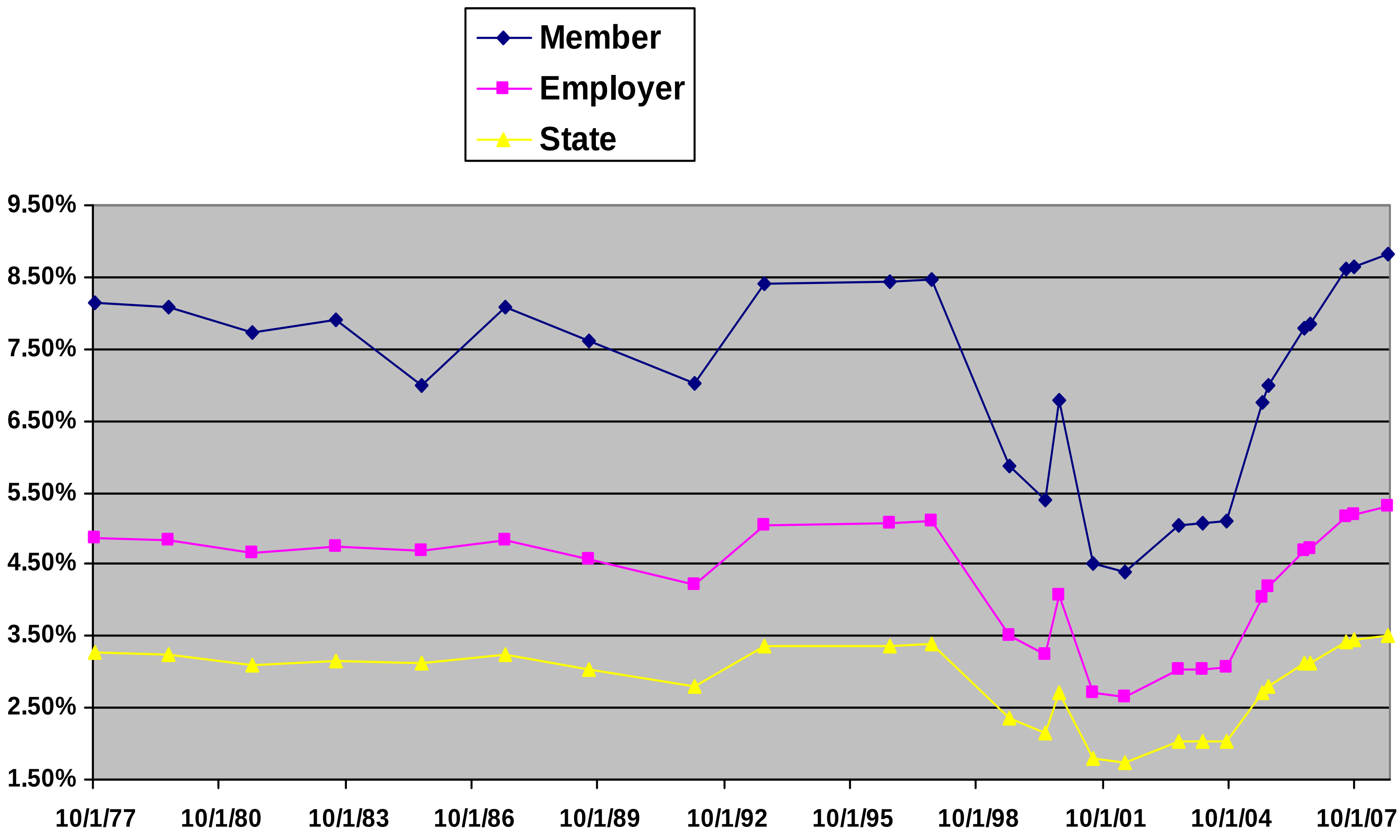
LEOFF Plan 2 Retirement Board

June 18, 2008

Issue

- The Board must adopt member, employer, and state LEOFF Plan 2 contribution rates for the 2009-11 biennium.

Historical Rates



Ongoing Rate Stability

- Minimum Contribution Rate
  - 90% of the expected long-term cost of the plan (8.63% for 2007)
- Corridor Funding
  - Established a minimum and maximum ratio of actuarial to market value of 30%
- Asset Smoothing
  - Allows for excess gains and losses to be recognized over a period of up to 8 years

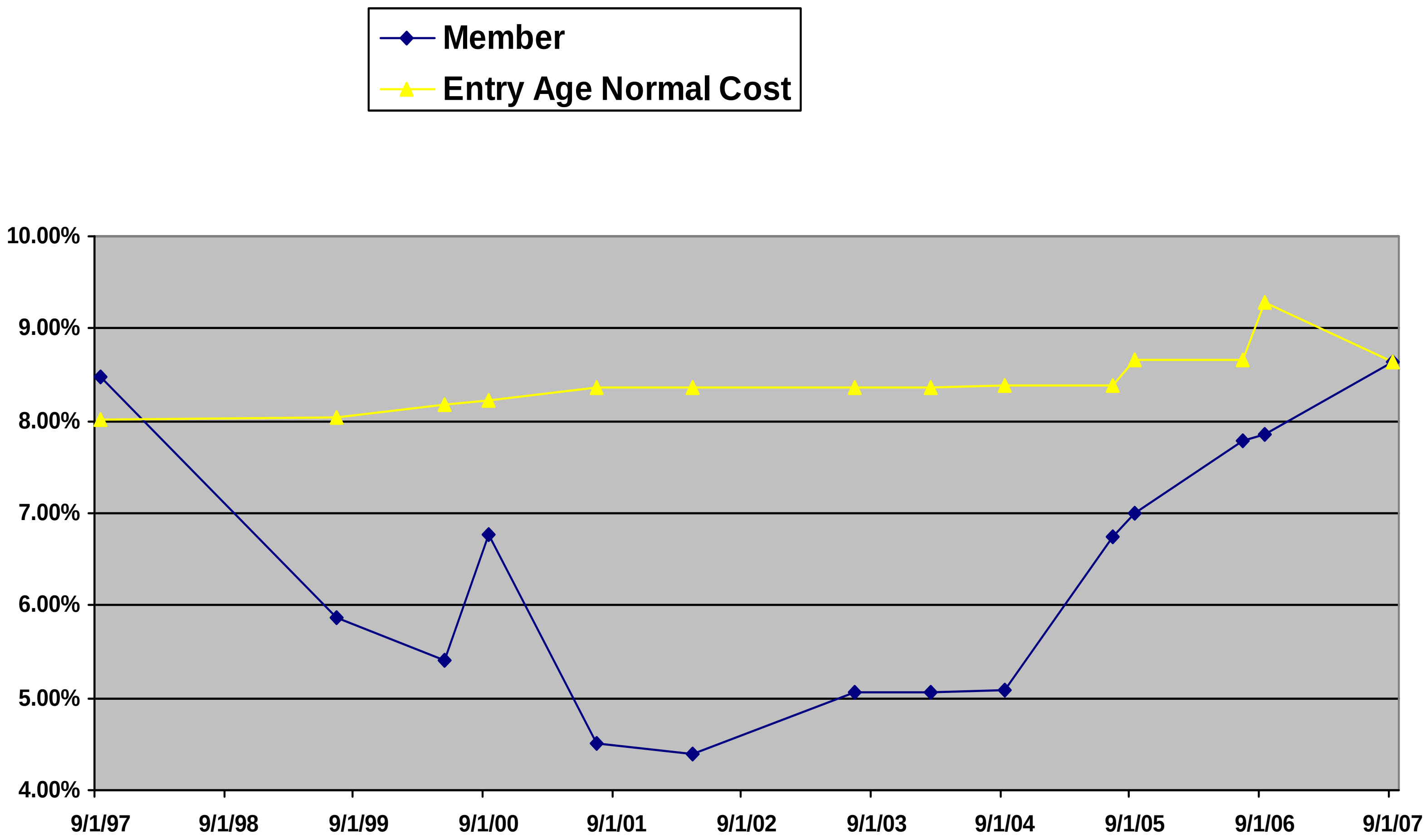
Influences on Contribution Rates

- Future Investment Returns
  - The preliminary deferred investment amount for 2006 was $495 million
- Change in Economic Assumptions
  - Rate of return, inflation, salary growth, growth in system membership
- Experience Study
  - Projected improvements

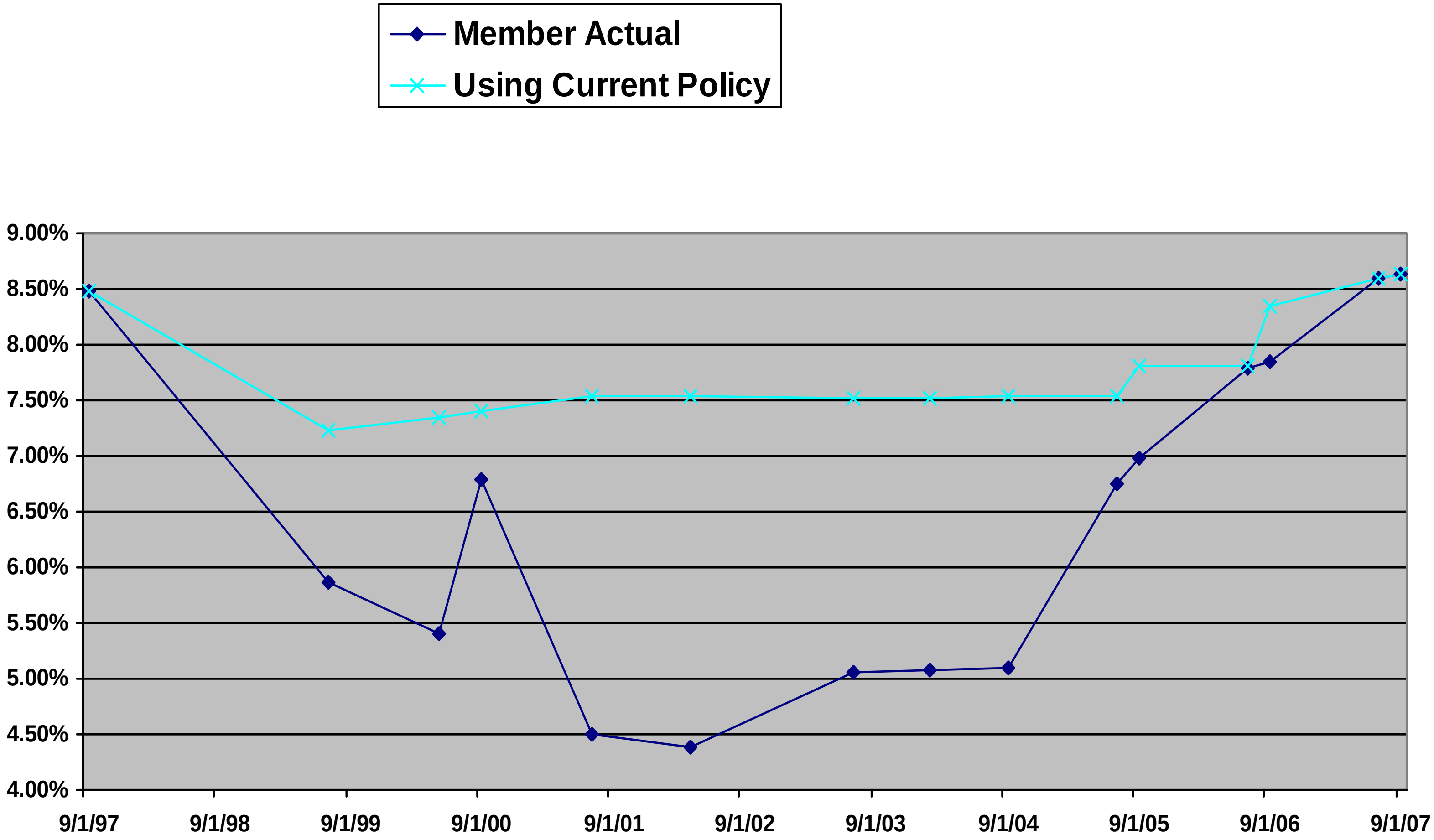
Policy Issues

- Current 4-Year Plan Ends 06/30/2009
- Some Options to Consider
  - Fixed rate
  - Variable rate based on OSA valuation

Option 1: Fixed Contribution Rates



Option 2: Variable Contribution Rates



Contribution Rates

QUESTIONS?

Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board

Contribution Rates

Preliminary Report

June 18, 2008

1. Issue

The Board must adopt member, employer, and state LEOFF Plan 2 contribution rates for the 2009-2011 biennium.

2. Staff

Gregory M. Deam, Senior Research & Policy Manager
(360) 586-2325
Greg.deam@leoff.wa.gov

3. Members Impacted

Any change to the existing LEOFF Plan 2 funding policies would impact all active members and employers. As of the most recent actuarial valuation, there are approximately 15,718 active LEOFF Plan 2 members and 481 employers.

4. Current Situation

In December of 2004, the Board adopted a four-year schedule that raised contribution rates annually beginning July 1, 2005, until they expire on June 30, 2009.

5. Background Information and Policy Issues

Background

Prior to the creation of the Board, contribution rates for LEOFF Plan 2 were adopted by the Pension Funding Council. This is the same process used for all other systems and plans today. However, with the creation of the LEOFF 2 Board in July 1, 2003 under Initiative 790, the Board became responsible for contribution rate adoption.

In June of 2004, the Board identified that contribution rate stability was one of its top priorities. At the December 9, 2004 meeting, the Board adopted a four-year plan of annual increases to raise rates to the levels they need to be to fund current benefits through June 30, 2009.

The Board also adopted two other policies to help stabilize long-term contribution rates. One was adoption of a minimum contribution rate of 90% of the entry age normal cost of the plan. The second was to establish a funding corridor. Under the funding corridor policy a 30% maximum and minimum ratio of actuarial to market asset value was established. This helps ensure rates do not remain artificially too high or low. In addition to these policies and the four-year contribution rate increase policy, the Legislature passed another statutory funding policy in 2003 that allows gains and losses to be “smoothed” over a period of up to eight years, depending on the magnitude of the deviation between actual investment return and the current 8% assumption.

The final contribution rate increase is scheduled for July 1, 2008. There were no bills passed during the 2008 Legislative Session that affect the contribution rates, so no supplemental increase will be due in September.

Policy Issues

The policy issue to be addressed by the Board is for contribution rate setting after June 30, 2009. The Board could adopt rates periodically based on the Office of the State Actuary’s actuarial valuation or they could adopt a fixed rate based on the plan’s expected long-term cost of the plan.

Both methods have pros and cons. With a periodic rate adoption, the contributions might more closely reflect the actual cost of the plan, but the variations could be more difficult from a budgeting standpoint. With a fixed rate, budgeting is easier from the standpoint of projecting costs.

6. Policy Options

Option 1: Use a Fixed Contribution Rate for Four Years
Under this option the Board would approve a fixed rate based on the current expected long-term cost of the plan (8.63% as of the 2007 valuation) for the next four years (July 1, 2009 through June 30, 2013). The rate would increase only if 90% of the expected long-term cost of the plan (the current floor) were to exceed the starting rate during the four-year period.

The advantage of this type of approach is that it makes budgeting for employers and the state much easier. It also makes the administration of collecting contributions easier for both the employers and state as well as for the Department of Retirement Systems.

The disadvantages of this approach is that the benefit fund could be over or under funded depending upon how well or how poor investment performance is during this fixed period. The Board can review the funding status annually and make adjustments as necessary to reduce this concern.

Option 2: Change the Rate Periodically Based on OSA Recommendation/Valuation
Under this option the Board would adopt contribution rates annually, based on the State Actuary's recommendations from their annual valuations. The rate could not go lower than 90% of the expected long-term cost of the plan.

The advantage of this type of approach is that the funding of the benefits is less likely to create large over or under funding as the rates are subject to review annually or biennially.

The disadvantage to this approach is that there are increased administrative costs to accommodate rate changes and the necessary notification process for contribution rate increases.

7. Supporting Information

Appendix A – Historical Contribution Rate Schedule

Appendix B – 2009 Contribution Rate Options

Appendix A – Historical Contribution Rates

Historical Contribution Rates

Effective Date	Member	Employer	State
10/1/77	8.14%	4.88%	3.26%
7/1/79	8.08%	4.85%	3.23%
7/1/81	7.74%	4.65%	3.09%
7/1/83	7.90%	4.74%	3.16%
7/1/85	7.00%	4.70%	3.13%
7/1/87	8.09%	4.85%	3.24%
7/1/89	7.60%	4.56%	3.04%
1/1/92	7.01%	4.21%	2.80%
9/1/93	8.41%	5.05%	3.36%
9/1/96	8.43%	5.06%	3.37%
9/1/97	8.48%	5.09%	3.39%
7/1/99	5.87%	3.52%	2.35%
5/1/00	5.41%	3.25%	2.16%
9/1/00	6.78%	4.07%	2.71%
7/1/01	4.50%	2.70%	1.80%
4/1/02	4.39%	2.64%	1.75%
7/1/03	5.05%	3.03%	2.02%
2/1/04	5.07%	3.04%	2.03%
9/1/04	5.09%	3.06%	2.03%
7/1/05	6.75%	4.05%	2.70%
9/1/05	6.99%	4.20%	2.79%
7/1/06	7.79%	4.68%	3.11%
9/1/06	7.85%	4.72%	3.13%
7/1/07	8.60%	5.17%	3.43%
9/1/07	8.64%	5.19%	3.45%
7/1/08	8.83%	5.30%	3.53%

Appendix B – 2009 Contribution Rate Options

Option 1: Fixed Rate

Under this option the Board would adopt a four-year rate based on one-hundred percent of the most current OSA valuation for the long-term expected cost of the plan. The rates that would result from this method are as follows:

	Member	Employer	State
July 1, 2009	8.63%	5.18%	3.45%
July 1, 2010	8.63%	5.18%	3.45%
July 1, 2011	8.63%	5.18%	3.45%
July 1, 2012	8.63%	5.18%	3.45%

Rates are based on the preliminary 9/30/07 Actuarial Valuation Report

Option 2: Variable Rate

Under this option the Board would adopt rates based on the OSA valuation and use the current smoothing and rate floor policies. The projected contribution rate increases over the next four years are as follows:

	Member	Employer	State
July 1, 2009	7.77%	4.66%	3.11%
July 1, 2010	7.77%	4.66%	3.11%
July 1, 2011*	7.77%	4.66%	3.11%
July 1, 2012*	7.77%	4.66%	3.11%

*The rate(s) for 2011/12 biennium are projected at 90% of the expected long-term cost of the plan, but could increase as a result of the 2009 Actuarial Valuation Report