Contribution Rate Stability Initial Consideration

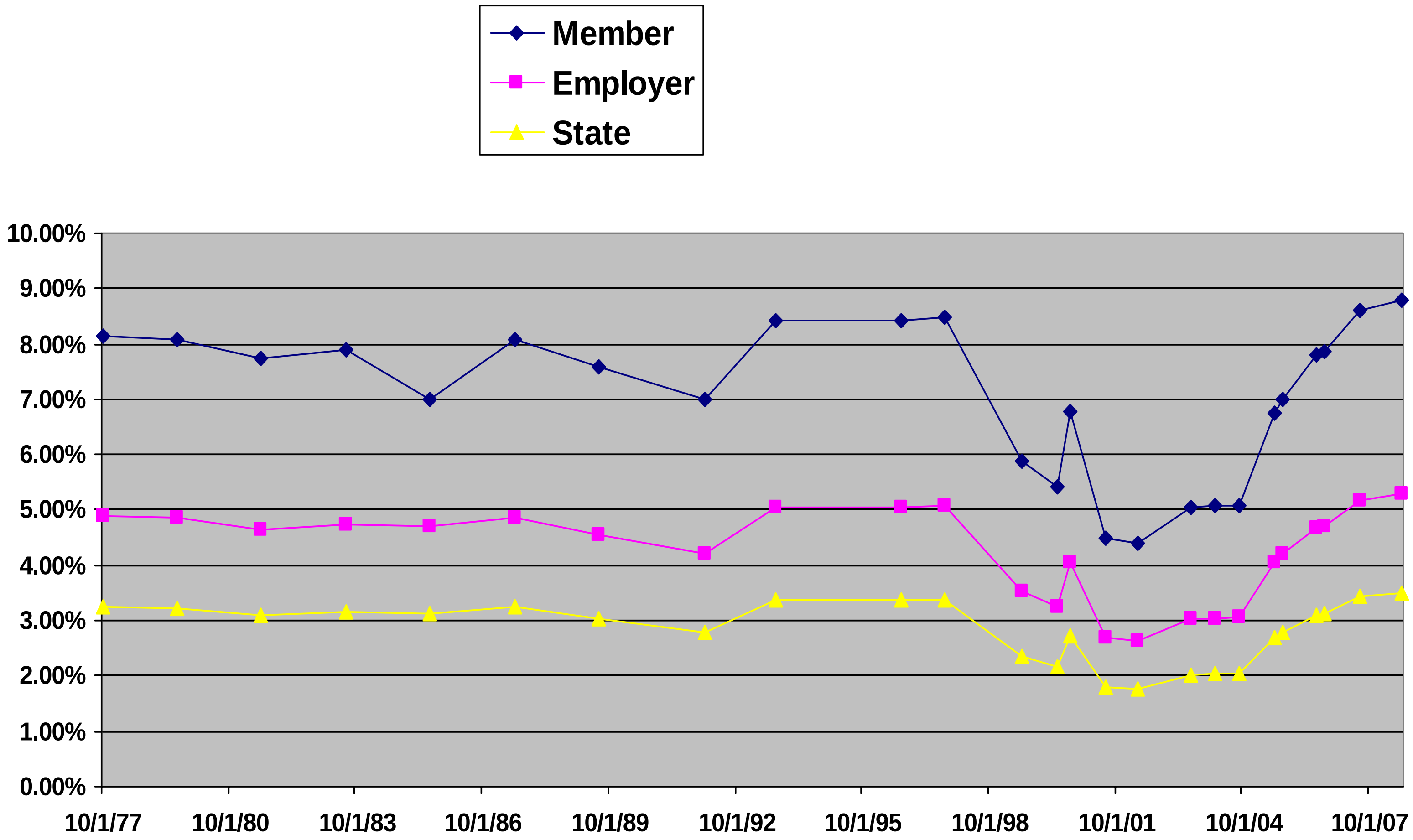
LEOFF Plan 2 Retirement Board

June 19, 2007

Brief Summary

- Historical Rates
- 2004 Board Adopted 4-Year Rate Schedule
- Ongoing Rate Stability
- Influences on Rates
- Policy Issues

Historical Rates



2004 Board Adopted 4-Year Rate Schedule

Effective Date	Member	Employer	State
07/01/2005	6.75%	4.05%	2.70%
09/01/2005*	6.99%	4.20%	2.79%
07/01/2006	7.79%	4.68%	3.11%
09/01/2006*	7.85%	4.72%	3.13%
07/01/2007	8.60%	5.17%	3.43%
07/01/2008	8.79%	5.28%	3.50%

*Supplemental

Ongoing Rate Stability

- Minimum Contribution Rate
  - 90% of the entry age normal cost (EANC = 8.67%)
- 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 will be $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 07/01/2008

- Some Options to Consider
  - Variable rate based on OSA valuation
  - Fixed rate

Contribution Rate Stability

QUESTIONS?

LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS' PLAN 2 RETIREMENT BOARD

Contribution Rate Stability

Initial Consideration

June 19, 2007

1. Issue

The Board's original contribution rate stability plan was a four-year plan that would gradually increase rates until they reached the expected long-term cost of the plan. That four-year plan ends with the July 1, 2008 contribution rate increase. The issue is what are the Board's next steps to maintain contribution rate stability?

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 15,168 active LEOFF Plan 2 members and 481 employers.

4. Current Situation

In December of 2004, the Board adopted a weighted annual increase of contribution rates over a four-year period. This would raise contribution rates to the actuarial long-term cost of providing the existing benefits by July 1, 2008. In addition to the annual increases, any new benefit enhancements with costs would be added. Appendix A includes a table of the rate increases as originally proposed by the Board and a copy of the actual contribution rate increases as they have occurred, including benefit enhancements.

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. By July, the Board heard an Initial Consideration on the subject and was followed up with a Preliminary Report in September 2004 with three options for short-term rate smoothing. This would allow rates to be "stepped up" to the expected long-term costs of the plan based on current benefits. The contribution rate for LEOFF Plan 2 as of September 2004 was 5.09% member, 3.06% employer, and 2.03% state. This represented about 60% of the long-term actuarial cost of the plan.

One option was to continue to use the current funding method (as adopted at the September 2004 meeting) which would have rates jump up dramatically (member 7.20%, employer 4.32%, and state 2.88%). The second option was to use an equivalent annual increase which would have a lower initial rate increase, but much larger at the end of the four-year period. The final option was to use a weighted annual increase, which would have a slightly higher initial rate increase but a lower rate at the end of the period (see Appendix C for a complete comparison).

At the December 9, 2004 meeting, the Board adopted the weighted average annual increase option to raise rates to the levels they need to be to fund current benefits by July 1, 2008.

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 is 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.

Policy Issues

The policy issue needingto be addressed is what is the Board going to do for contribution rate setting after July 1, 2008? Should the Board adopt rates periodically based on the Office of the State Actuary's evaluation or should rates be fixed?

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. Supporting Information

Appendix A – Board Contribution Rate Schedules

Appendix B – Historical Contribution Rate Schedule

Appendix C – 2004 Contribution Rate Options

Appendix A – Board Contribution Rate Schedules

Proposed Contribution Rate Increases

Effective Date	Member	Employer	State
7/1/05	6.75%	4.05%	2.70%
7/1/06	7.55%	4.53%	3.02%
7/1/07	8.30%	4.98%	3.32%
7/1/08	8.49%	5.09%	3.39%

Actual/Future Contribution Rate Increases

Effective Date	Member	Employer	State
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%
7/1/08	8.79%	5.28%	3.50%

***Supplemental Rate**

Appendix B – 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%

Appendix C – 2004 Contribution Rate Options

Option 1: Current Funding Method and Polices

The current statutory funding methods for LEOFF Plan 2 result in projected contribution rate increases over the next four years as follows:

	Member	Employer	State
July 1, 2005	7.20%	4.32%	2.88%
July 1, 2006	7.20%	4.32%	2.88%
July 1, 2007*	8.34%	5.00%	3.34%
July 1, 2008*	8.34%	5.00%	3.34%

*The rates for 2007 and 2008 were projections and are subject to change

Option 2: Equivalent Annual Increases:

One option that has been discussed as a means of phasing in the projected contribution rate increases would be to establish annual contribution rate increases of equal amounts over the next four years. This method would result in a higher cost at the end because the rates charged in the 2004-05 fiscal year would be lower than the rates necessary to fund the system as determined by the State Actuary in the 2003 Actuarial Valuation. The rates that would result from this method are as follows:

	Member	Employer	State
July 1, 2005	6.17%	3.69%	2.47%
July 1, 2006	7.24%	4.34%	2.90%
July 1, 2007	8.32%	4.98%	3.33%
July 1, 2008	9.39%	5.63%	3.75%

Option 3: Weighted Annual Increases

The “overshoot” effect that results from equivalent annual increases could be softened if contribution rate increases for the next four years were weighted so that the increases would result in a projected rate for 2008-09 that is equivalent to the expected long-term cost of the plan. The rates that would result from this method are as follows:

	Member	Employer	State
July 1, 2005	6.75%	4.05%	2.70%
July 1, 2006	7.55%	4.53%	3.02%
July 1, 2007	8.30%	4.98%	3.32%
July 1, 2008	8.49%	5.09%	3.39%