

BOARD MEETING AGENDA

June 24, 2015 - 9:30 AM



LOCATION

STATE INVESTMENT BOARD
Large Conference Room, STE 100
2100 Evergreen Park Drive S.W.
Olympia, WA 98502
Phone: 360.586.2320
Fax: 360.586.2329
recep@leoff.wa.gov

- | | |
|---------------------------------------------|----------|
| 1. Approval of Minutes | 9:30 AM |
| Steve Nelsen, Executive Director | |
| 2. Supplemental Rate Adoption | 9:35 AM |
| Ryan Frost, Research Analyst | |
| 3. Experience Study Timing | 10:00 AM |
| Lisa Won, Deputy State Actuary | |
| 4. Retiree Purchase of Annuity | 10:30 AM |
| Ryan Frost, Research Analyst | |
| 5. Income Leveling Options | 11:00 AM |
| Ryan Frost, Research Analyst | |
| 6. Increasing Retirement Age | 11:30 AM |
| Ryan Frost, Research Analyst | |
| 7. Disaster Response Coverage | 12:00 PM |
| Ryan Frost, Research Analyst | |
| 8. Final Legislative Update | 12:30 PM |
| Ryan Frost, Research Analyst | |
| 9. Administrative Update | |
| • Outreach Activities | 1:00 PM |
| Steve Nelsen, Executive Director | |
| 10. Agenda Items for Future Meetings | 1:30 PM |
| Steve Nelsen, Executive Director | |

Lunch is served as an integral part of the meeting.

In accordance with RCW 42.30.110, the Board may call an Executive Session for the purpose of deliberating such matters as provided by law. Final actions contemplated by the Board in Executive Session will be taken in open session. The Board may elect to take action on any item appearing on this agenda.



Supplemental Rate Adoption

Report Type:

Final Proposal

Date Presented:

6/24/2015

Presenter Name and Title:

Ryan Frost, Research Analyst

Summary:

The Board must decide whether it is necessary to increase contribution rates due to the passage of Substitute House Bill 1194, providing surviving spouses of members of the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) and Washington State Patrol Retirement System (WSPRS) monthly survivor benefits regardless of remarriage.

Strategic Linkage:

This item supports the following Strategic Priority Goals:

Enhance the benefits for the members., Provide the stakeholders with a voice in plan governance., Maintain the financial integrity of the plan., Inform the stakeholders.

ATTACHMENTS:

Description	Type
📎 Supplemental Rate Adoption Report	Report
📎 Supplemental Rate Adoption Presentation	Presentation



June 24, 2015

Supplemental Rate Adoption

FINAL PROPOSAL

By Ryan Frost

Research Analyst

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ryan.frost@leoff.wa.gov

ISSUE STATEMENT

The Board must decide whether it is necessary to increase contribution rates due to the passage of Substitute House Bill 1194, providing surviving spouses of members of the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) and Washington State Patrol Retirement System (WSPRS) monthly survivor benefits regardless of remarriage.

OVERVIEW

Based on the preliminary actuarial data as of May 18, 2015, there were 16,773 active LEOFF Plan 2 members. Adopting supplemental contribution rates impacts all active LEOFF Plan 2 members, employers, and the state.

One of the Board's strategic goals is to ensure the financial integrity of the plan. In order to maintain that goal, it may be necessary for the Board to pay for benefit improvements. Not all benefit improvements will have costs necessitating an increase in contribution rates, but if they do, the Board has the option of adopting a supplemental rate increase. Changes are usually effective September 1 following the effective date of the legislation.

BACKGROUND & POLICY ISSUES

The Office of the State Actuary (OSA) provided a fiscal note on March 2, 2015 indicating the cost of this benefit enhancement would require a contribution rate increase of four basis points for the member (0.04%), three basis points for the employer (0.03%), and one basis point for the state (0.01%). The House and Senate have funded this bill in their preliminary budgets.

Just last year, the Board decided to leave contribution rates at their current levels for the upcoming biennium. With this new bill, there is potentially a larger gap between actual rates and what the normal cost of the plan is projected to be.

However, the vast majority of the costs of this bill are related to the assumptions of remarriage among current widows. With limited information and experience about this matter, it may be the Board's decision to let experience play out before assuming changes to the normal cost of

the plan. The actuary's fiscal note and assumptions are currently under audit by an outside actuary, with the results of that audit to come soon.

The Board will be studying its funding policy this interim. Adopting a rate change now when the Board may be adopting a new funding policy that could also involve a rate change, may lead to rate volatility in the short term. The Board could discuss its funding policy first, then come back later in the interim to review supplemental rate adoption.

Lastly, the Board could decide to adopt the full entry age normal cost (EANC) of the plan now. The majority of the rate increases were tied to mortality improvements among the population. Previously, the Board elected to leave rates at their current levels through the 2015-2017 biennium, then adopt the full normal cost rates for the 2017-2019 biennium.

POLICY OPTIONS

Option 1: Do not adopt a supplemental rate

Under this option, the Board would recommend no increase in contribution rates. This would leave rates at:

Member	8.41%
Employer	5.05%
State	3.36%

Option 2: Adopt OSA's recommended supplemental rates

Under this option, the Board would recommend to adopt an increase in contribution rates of 0.04% for members, 0.03% for employers, and 0.01% for the state. Rates would increase to:

Member	8.45%
Employer	5.08%
State	3.37%

Option 3: Adopt the full normal cost

Under the option, the Board would adopt the full normal cost of the plan as presented by OSA last interim, including the cost of the new benefit. This would increase rates to:

Member	8.89%
Employer	5.34%
State	3.55%



Supplemental Rate Adoption

Final Report
June 24, 2015

Issue

A supplemental rate change may be necessary due to the passage of SHB 1194.

Overview

- Impacts
 - Member
 - Employee
 - State
- Ensuring Actuarial Soundness

Background

- Rate Adoption History
- Full Normal Cost of the Plan

Options

Option 1: Do not adopt a supplemental rate

The Board would leave rates at:

Member	8.41%
Employer	5.05%
State	3.36%

Options

Option 2: Adopt OSA's recommended supplemental rates

The Board would adopt an increase in contribution rates of 0.04% for members, 0.03% for employers, and 0.01% for the state. Rates would increase to:

Member	8.45%
Employer	5.08%
State	3.37%

Options

Option 3: Adopt the full normal cost

The Board would adopt the full normal cost of the plan as presented by OSA last interim, including the cost of the new benefit. This would increase rates to:

Member	8.89%
Employer	5.34%
State	3.55%

Options

	Option 1 – Do not adopt a supplemental rate	Option 2- Adopt OSA's recommended supplemental rates	Option 3- Adopt the full normal cost, including the new benefit
Member	8.41%	8.45%	8.89%
Employer	5.05%	5.08%	5.34%
State	3.36%	3.37%	3.55%

Questions?

Contact:

Ryan Frost

Research Analyst

(360) 586-2325

ryan.frost@leoff.wa.gov



Retiree Purchase of Annuity

Report Type:

Initial Consideration

Date Presented:

6/24/2015

Presenter Name and Title:

Ryan Frost, Research Analyst

Summary:


Following passage of the annuity purchase legislation in 2014, retirees inquired whether they could roll over and purchase an annuity after retirement from the LEOFF 2 trust. Staff has determined retiree annuity purchase is permissible under the internal revenue code if the LEOFF Plan 2 act were amended to allow it.

Strategic Linkage:

This item supports the following Strategic Priority Goals:

Enhance the benefits for the members., Inform the stakeholders.

ATTACHMENTS:

Description		Type
 Retiree Annuity Purchase Report		Report
 Appendix A		Appendix
 Retiree Annuity Purchase Presentation		Presentation



June 24, 2015

Retiree Annuity Purchase

INITIAL CONSIDERATION

By Ryan Frost

Research Analyst

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ISSUE STATEMENT

The Legislature enacted the Board's 2013 proposal allowing retiring LEOFF Plan 2 members to roll over tax deferred savings into LEOFF Plan 2 to purchase an annuity, RCW 41.26.463. Current state law limits roll overs to the time of retirement.

OVERVIEW

Following passage of the law, retirees inquired whether they could roll over and purchase an annuity after retirement. Staff has determined retiree annuity purchase is permissible under the internal revenue code if the LEOFF Plan 2 act were amended to allow it.

At the time of retirement, members can roll their retirement savings from a tax qualified plan into LEOFF Plan 2. The Department of Retirement Systems (DRS) will convert this rollover into a monthly life annuity. Because members are rolling over from a tax qualified savings plan, they do not have to pay taxes at the time the annuity is purchased. Instead, the money will be included in their taxable income as they receive it.

Members receive their pension dollars as well as this annuity in one monthly check from DRS. If they were to pass away before receiving the initial cost to purchase the annuity, the designated beneficiary receives the balance.

BACKGROUND & POLICY ISSUES

Other annuities

Many private annuity companies offer their own versions of this benefit. However, LEOFF's higher interest rate assumption (7.5% - compared to around 4% for a private annuity company) translates into a larger annuity from the same lump sum. Additionally, administrative cost to the member are much lower.

Analysis supporting the Board's 2013 annuity purchase proposal is included in the December 18, 2013 final proposal to the Board attached as exhibit A.

Retirees may purchase an annuity

A 2012 IRS revenue ruling¹ allowed pension plan member to roll money from a deferred compensation account into the member's defined benefit plan to purchase an annuity if authorized by the plan document (i.e. the LEOFF Plan 2 statutes). The original revenue ruling did not discuss whether retirees could also be given that opportunity.

The bill proposed by the Board and passed by the Legislature limits roll over and annuity purchases to the time of retirement. Following questions raised by retirees, staff has determined that federal tax law allows retirees to take that same action if authorized in statute.

SUPPORTING INFORMATION

Appendix A: Promoting Individual Savings for Retirement – Final Proposal, December 18, 2013

¹ Internal Revenue Bulletin 2012-8; issued February 21, 2012.



DECEMBER 18, 2013

PROMOTING INDIVIDUAL SAVINGS FOR RETIREMENT

FINAL PROPOSAL

By Paul Neal
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ISSUE

Members are not able to take advantage of a recent IRS ruling which provides new options for managing savings in retirement.

PROPOSAL SUMMARY¹

At the November 20th meeting the Board directed staff to prepare proposals on:

- Option 1: Authorize LEOFF Plan 2 to annuitize roll-overs of tax deferred savings;
- Option 3: Require LEOFF Employers to Offer DRS's Deferred Compensation Program to LEOFF Members; and
- Option 4: Encourage DRS to offer a Roth option as part of its 457 deferred compensation plan.

Those options are being presented for Board action at the December 18th meeting.

MEMBERS IMPACTED

New options encouraging member's retirement savings as part of LEOFF Plan 2 would be available to all 16,720 active LEOFF Plan 2 members².

OVERVIEW

The LEOFF Plan 2 defined benefit Plan, the first leg of the three-legged retirement stool, provides a defined lifetime payout that does not vary with investment return. Retirees must devise their own distribution strategy for the second leg of the stool, individual retirement savings. Members can reduce the risk of outliving their assets if they convert at least some of those assets into a lifetime annuity.

¹ The Board initially considered this issue at the August 28, 2013 Board meeting. At the September follow-up the Board looked at three options and requested additional information on: Annuitization of additional amounts rolled over into LEOFF Plan 2; and requiring LEOFF employers to participate in DRS's 457 plan. Staff also researched authorized "Roth" accumulations in governmental 457 plans.

² Membership number as of June 30, 2012; Office of the State Actuary 2011 LEOFF Plan 2 Valuation Report.

LEOFF Plan 2 members may purchase an additional monthly benefit through the LEOFF Plan 2 trust fund by buying up to 5 years of additional service credit at the time retirement. Under current law, only Plan 3 members (TRS, PERS & SERS³) can convert contributions to an annuity from their retirement system.

Leveraging the existing LEOFF Plan 2 infrastructure to authorize accumulation of savings and/or converting that account to a monthly benefit through the LEOFF Plan 2 trust fund would provide a cost-effective mechanism to encourage retirement savings. This can be particularly important for LEOFF Plan 2 members since many do not participate in social security through their employer.

This report examines federal laws encouraging retirement savings, the costs of savings for retirement, different mechanisms for annuitizing retirement savings, a recent IRS ruling authorizing annuitizing retirement savings through LEOFF Plan 2, and provides options for further action.

BACKGROUND INFORMATION & POLICY ISSUES

The LEOFF Plan 2 Retirement Board began studying ways to encourage increased retirement savings during the 2004 Interim. The Board recommended legislation allowing purchase of up to five years of service credit at retirement. The Legislature passed that recommendation in 2005 (HB 1269).

That same year the Department of Retirement Systems (DRS) began offering annuities through the Plan 3 programs. The Purchase of Annuity topic was studied by the Board during the 2006, 2007, 2008 and 2009 Interims reaching the Final Proposal stage in 2006, 2008 and 2009, but no legislation was recommended. The topic was deferred for joint consideration with the Select Committee on Pension Policy (SCPP) for the 2009 Interim. No further action was taken.

The paradox is that investors recognize that their retirement savings will need to last longer than ever before but they aren't making plans to ensure they will actually have the money they need. There tends to be a false sense of security when it comes to Planning for retirement. We hope that the money will somehow be there when we need it but we're not taking the action required to ensure it is. This is a serious problem, and addressing it must become an urgent priority.

Noel Archard, Head of BlackRock
Canada. July 2013

SAVING FOR RETIREMENT

Federal Law Encouraging Retirement Savings

³ Teachers' Retirement System (TRS); Public Employees' Retirement System (PERS); School Employees' Retirement System (SERS).

The federal tax code encourages individuals to save for, and invest in, retirement:

- Qualified deferred compensation plans, such as the IRS §457 plan offered through the Department of Retirement Systems (DRS) deferred compensation program, permit an individual to authorize pre-tax salary deductions for deposit into a personal investment account. Many LEOFF Plan 2 employers offer these types of plans to employees. Upon separation from employment a member may leave the funds invested or select a distribution option.
- Members may transfer funds between government defined benefit pension Plans like LEOFF Plan 2 and deferred compensation accounts such as 457, 403(b), and 401(k) Plans. This helps members manage retirement savings as they change employers.
- Purchase of up to five years of service credit or “air-time” was authorized in the Federal Pension Protection Act.
- A recent IRS revenue ruling⁴ allows members with funds in a deferred compensation account maintained by an employer to roll the funds over into their defined benefit plan and convert those funds to an annuity from the defined benefit Plan.
- The Small Business Jobs act of 2010 authorized governmental 457 plans to include a Roth option.

Using these federal provisions, some state and local government pension plans allow member fund transfers, including funds from tax-deferred accounts, into the primary defined benefit plans to purchase additional service credit or an annuity.

THE COST OF SAVING - DEFERRED COMPENSATION FEES

DRS operates a deferred compensation program under 26 U.S.C. §457, commonly called a "457 Plan". Washington's political subdivisions may participate in DRS's 457 Plan, or use another administrator, such as ICMA-RC. Administrative fees vary significantly. Comparing private administrator fees to DRS's annual .13% fee can be challenging since private administrators tend to use variable fee schedules rather than the flat fee charged by DRS, as demonstrated by the fee comparison table included as Appendix A.

The average net annual fee of the private 457 plan administrators examined in Appendix A is 1.29%, nearly 10 times the .13% charged by DRS. DRS's lower fees facilitate a larger accumulation from the same member contributions⁵:

⁴ Internal Revenue Bulletin 2012-8; issued February 21, 2012.

⁵ The comparison assumes \$3,602 per year contribution for 15 years, earning interest at LEOFF PLAN 2's assumed rate of 7.5%, less annual fees.

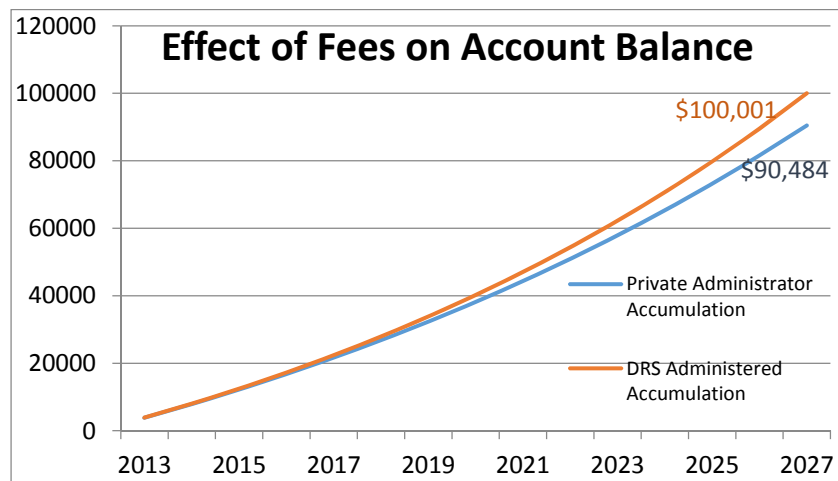


Figure 1

ANNUITIZING ASSETS

Annuities can convert retirement savings into a guaranteed monthly income (this process is called annuitization) for a specified period of time. A life annuity provides that income for the member's lifespan in exchange for a lump-sum dollar amount paid up front. Deferred compensation plans do not normally allow for the distribution of assets in the form of an annuity directly from the fund. LEOFF Plan 2 members wishing to annuitize their retirement savings must purchase the annuity through an insurance company.

The price/value of the annuity depends in part upon the features selected by the purchaser. The terms and conditions of an annuity contract specify features such as whether the annuity will be for a single life or a joint annuity (like a survivor benefit feature), the payment frequency, adjustments for cost of living, and death provisions. Different methods for annuitizing assets are listed below, though not all are currently available to LEOFF Plan 2 members.

Trust Fund Annuity Purchase

TRS Plan 3, SERS Plan 3, and PERS Plan 3 members and survivors may convert some or all of the funds from their Plan 3 member account to a life annuity, RCW 41.50.088. The features and options of the Plan 3 annuities administered by DRS are detailed in Appendix B. This option is not available to LEOFF Plan 2 members.

DRS calculates the annuity that can be purchased for a given lump sum using an age based actuarial table to compute the monthly benefit per \$1.00 of accumulation for defined benefits. There is no limit on the amount of funds in the member account that can be converted to an annuity.

RCW 41.32.067 also allows TRS Plan 1, 2 and 3 members to purchase additional benefits through a member reserve contribution which is actuarially converted to a monthly benefit at the time of retirement. The statute was passed to provide teachers with out-of-state service credit a mechanism for transferring contributions from a prior system into TRS⁶.

Service Credit Purchase

LEOFF Plan 2 members can annuitize retirement savings by purchasing up to five years of additional service credit at the time of retirement. To purchase service credit under this option the member pays the actuarial present value of the resulting increase in the member's benefit. A member may pay all or part of the cost of the additional service credit with an eligible transfer from a qualified retirement plan. For more information on the history and methodology for calculating service credit purchases, see Appendix C.

The federal 5-year “air time” limit works out to a maximum of \$86,484 that could be converted to a monthly benefit by the average LEOFF Plan 2 member⁷, see Appendix C. This is a key difference between a Plan 3 annuity conversion and a service credit purchase: the Plan 3 conversion does not have a maximum amount limit.

Commercial Market Annuity

Retirement savings can be annuitized by purchasing an annuity policy through insurance agents, financial planners, banks and life insurance carriers. However, only life insurance companies issue policies. Generally, commercial market annuities do not offer all the same features as the Plan 3 trust fund annuity and do not provide as favorable a payout. A primary reason for the payout difference is the different interest rate used to calculate the value of the annuity. Private insurers use a lower interest rate, due in part to the inclusion of a reasonable profit:

[A] private insurer will provide the annuity based on an interest rate of about 4 percent, whereas DRS will provide the annuity based on an interest rate of about 8%.⁸.

The interest rate differential drives a significant difference in payout amounts between private annuity contracts and contributions annuitized through the trust fund. Five different insurance companies quoted the monthly annuity with a 3% annual COLA they would provide the average LEOFF Plan 2 retiree⁶ for \$100,000:

⁶ See Laws of 1991 c 278 § 2.]

⁷ Age 56 with 17 years of service credit and a final average salary of \$5000 per month.

⁸ 2010 State Actuary 2010 fiscal note on the Board’s purchase of annuity proposal.

Insurance Company	Quote
American General	\$389
Aviva	\$402
Fidelity & Guaranty Life	\$421
Genworth Life Insurance	\$406
Integrity Life Insurance	\$400
Average	\$404

If that same average LEOFF Plan 2 member were able to leverage the institutional advantages of the retirement system by annuitizing \$100,000 within the LEOFF Plan 2 system, the payout would be \$578.14⁹. That's a 43% increase over the average commercial quote, or \$174 more per month for life.

The chart below uses the 15 year accumulations calculated in figure 1 and estimates the annuity those accumulations would purchase from either an insurance company or the LEOFF Plan 2 trust fund.

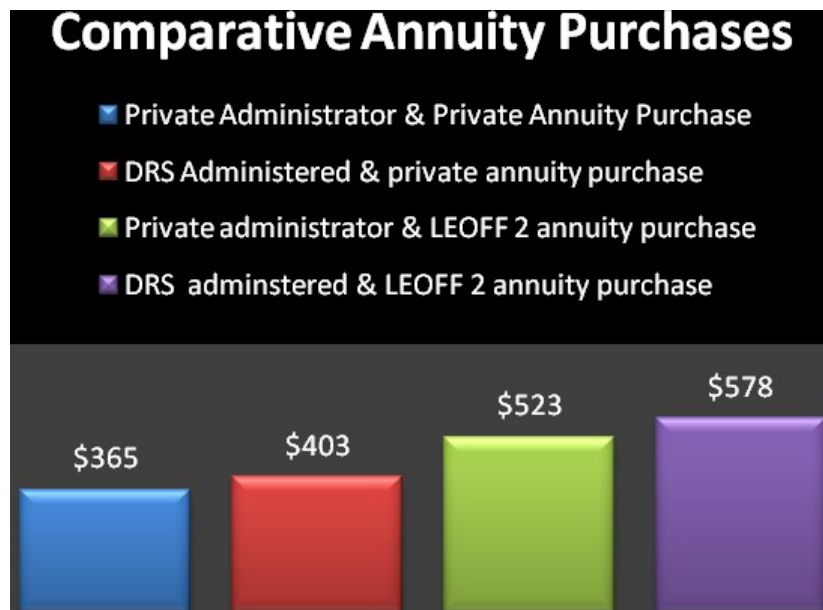


Figure 2

Current state law does not allow annuitization of retirement savings through the LEOFF Plan 2 trust fund. A recent IRS ruling gives the green light to such a program.

⁹ \$100,000 x .0057814 (conversion factor from DRS table for 56 year-old LEOFF member) = \$578.14 monthly life annuity

NEWLY AVAILABLE ALTERNATIVES:

Annuitization through 401(a) plan

Federal tax law allows public defined benefit plans to add a member savings account within the plan, sometimes referred to as a companion account or “sidecar”. Contributions to the employee savings account may be made by the employer or the employee and may be either pre-tax or after tax depending on plan design.

Under the recent IRS ruling cited above, a retirement savings account can be annuitized within the 401(a) defined benefit plan to obtain an additional monthly benefit paid through the trust fund. This can be done either through a employee savings account administered within the 401(a) plan or by rolling over retirement savings from another plan such as a 457 plan.

A “sidecar” plan administered through LEOFF Plan 2 could leverage the institutional advantages available to active members as participants in an existing state-administered Plan. Those advantages include the lower fees charged by DRS to administer the savings plan, and the more favorable annuity payout when purchased through the existing LEOFF Plan 2 trust fund.

Potential Risks

The purchase of an annuity through the LEOFF Plan 2 trust fund would not have a cost to the system¹⁰ under current actuarial assumptions. There is, however, a potential risk to the fund if those assumptions change or actual experience falls below assumed levels. When an annuity is purchased, the member locks in the actuarial assumptions in place at that time. A subsequent change in assumptions may knock the annuity out of actuarial equivalency.

For instance, the Actuary’s 2010 fiscal note assumed a trust fund annuity would be calculated using the fund’s 8% interest assumption. The Board has since reduced that assumption to 7.5%. An annuity locked in with an 8% interest assumption would be “too high” under a 7.5% assumption, causing a \$12,980 actuarial loss to the fund⁹.

Roth Contributions

The original 457 plan design allows employees to deduct contributions from their salary pre-tax. The amounts are taxed at the time of distribution. A Roth¹¹ plan reverses that system by taxing contributions, but then disbursing contributions and earnings tax free after retirement.

Governmental 457 plans were not originally allowed to offer a Roth option. The Small Business Jobs Act of 2010 authorizes government sponsored 457 plans to offer designated Roth accounts. Federal law now allows governmental 457 plans to permit participants to:

¹⁰ See OSA fiscal note on 2010 annuity purchase proposal, Appendix C.

¹¹ Named after Senator William Roth of Delaware, the chief legislative sponsor of the original legislation in the Taxpayer Relief Act of 1997 (Public Law 105-34).

- Designate a Roth elective deferral account within the plan; and/or
- Convert conventional pre-tax contributions into Roth contributions within the same plan. Participants wishing to convert existing contributions would have to pay taxes on amounts converted at the time of conversion.

Participants in DRS's 457(b) plans cannot take advantage of in-plan conversions/rollovers to designated Roth accounts unless DRS formally adopts those options in their plan document. DRS has the authority to do this under current law, though they are not required to.

POLICY OPTIONS

The specifics of options available to the Board are in many ways a function of federal tax laws. DRS has received some guidance from the law firm of Ice Miller as of this writing. The LEOFF Plan 2 Board staff had additional questions which are still pending at this time. The options presented below, while accurate in broad strokes, may have to be modified in subsequent presentations depending on future tax law guidance. Additionally, option 1 could be combined with either option 2 or option 3.

Option 1: Propose Legislation authorizing LEOFF Plan 2 to accept roll-overs of tax deferred savings and annuitize those amounts through the plan upon retirement.

Under this option the Board would direct staff to develop legislation authorizing DRS to accept roll-overs from LEOFF Plan 2 members for annuitization at the time of retirement. Further guidance is required to determine what types of roll-overs are allowable under federal tax laws and what limitations, if any, there are on annuitization of rolled over amounts.

Option 2: Propose Legislation establishing a 410(a) savings plan within LEOFF 2 to accept contributions from LEOFF Plan 2 members.

Under this option the Board would direct staff to develop legislation establishing a "sidecar" savings plan within LEOFF Plan 2 that could accept member contributions for distribution following retirement. Preliminary research indicates that this vehicle would be less flexible than a 457 plan such as that administered by DRS's Deferred Compensation Program. Member contributions may be required to follow the same rules as Plan 3 contributions. A member could be required to select a rate upon enrollment. Like the Plan 3 contribution rates, once selected the rate could not be changed except upon change of employment. Voluntary member contributions, which could apparently fluctuate, would be after-tax.

Option 3: Require LEOFF Employers to Offer DRS's Deferred Compensation Program to LEOFF Members.

This option provides a more flexible plan than the 401(a) option. The Board would propose legislation requiring all LEOFF Plan 2 employers to offer the state administered 457 plan. This would ensure that LEOFF Plan 2 members can avail themselves of a plan with the lowest possible administrative fees.

SUPPLEMENTAL POLICY OPTION INFORMATION

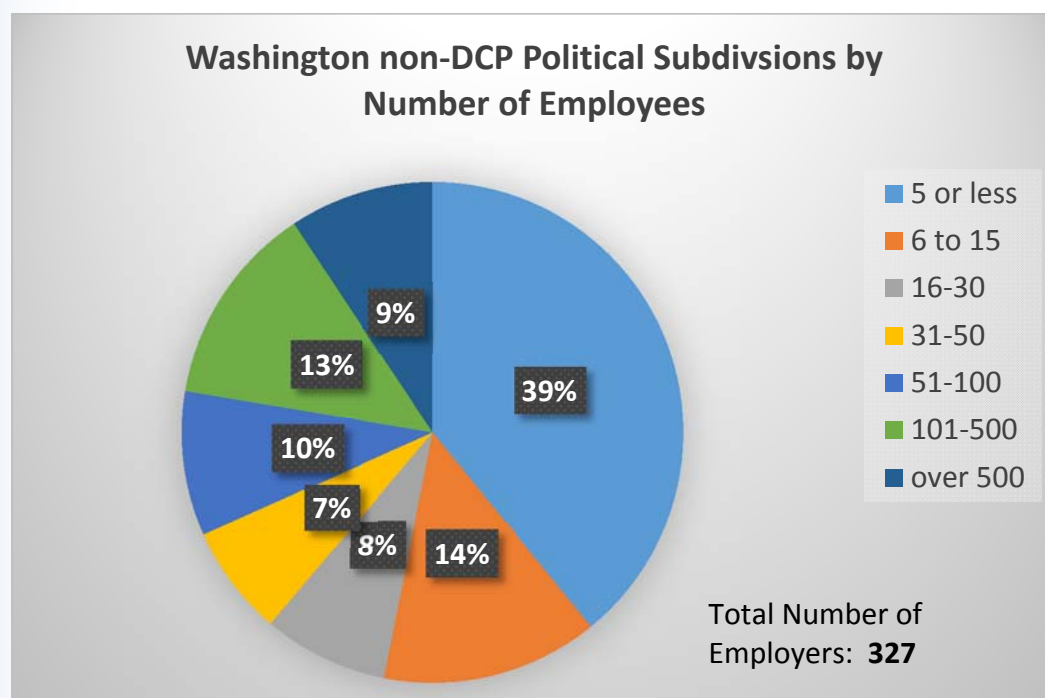
The Board requested additional consideration of options 1 and 3. A fourth option has been developed based on the additional information about Roth plans.

Option 1:

Staff has confirmed that the IRS will permit rollovers from any authorized tax-deferred savings plan (457, 403(b), 401(a)) into LEOFF 2 for purposes of purchasing an annuity. Further, there are no IRS limits on the amount that may be rolled over and annuitized, except that the total payout cannot exceed the IRS's section 415 limits on maximum allowable benefit.

Option 3:

Staff has drafted proposed legislation that is currently being reviewed by DRS for comments. DRS Director Marcy Frost has asked the Select Committee on Pension Policy to consider a similar directive for all Washington Public Employers. Additional data from DRS identifies Washington political subdivision that do not offer the State administered 457 plan:



Option 4: Roth Contributions to Governmental 457 plan.

The Board may wish to take action on the Roth option:

Option 4(a): Amend Deferred Compensation Statute to Require Roth Option.

Submit legislation requiring DRS to develop a Roth option as part of its deferred compensation plan. The Board may want to direct staff to work with DRS on bill language.

Option 4(b): Ask DRS to Offer a Roth Option

If the Board wished DRS to develop a Roth option without a bill, it may be sufficient to send a letter from the Board to DRS requesting them to take action.

Option 4(c): Take No Action at this Time

The Board could decline to take any action on the Roth option at this time.

SUPPORTING INFORMATION

Appendix A: Deferred Compensation Fee Comparison

Appendix B: Plan 3 annuity purchase option features

Appendix C: Service Credit Purchase history and example

Appendix D: OSA draft fiscal note - 2009

Appendix E: Bill Draft re: annuitization of savings

Appendix F: Bill Draft re: Required participation in DRS 457 plan

Appendix G: Letter to DRS re: offering Roth option

Appendix H: OSA draft fiscal note -2013



Retiree Annuity Purchase

Initial Consideration

June 24, 2015

Issue

Current state law limits roll overs to the time of retirement, preventing retirees from taking advantage of the benefit.

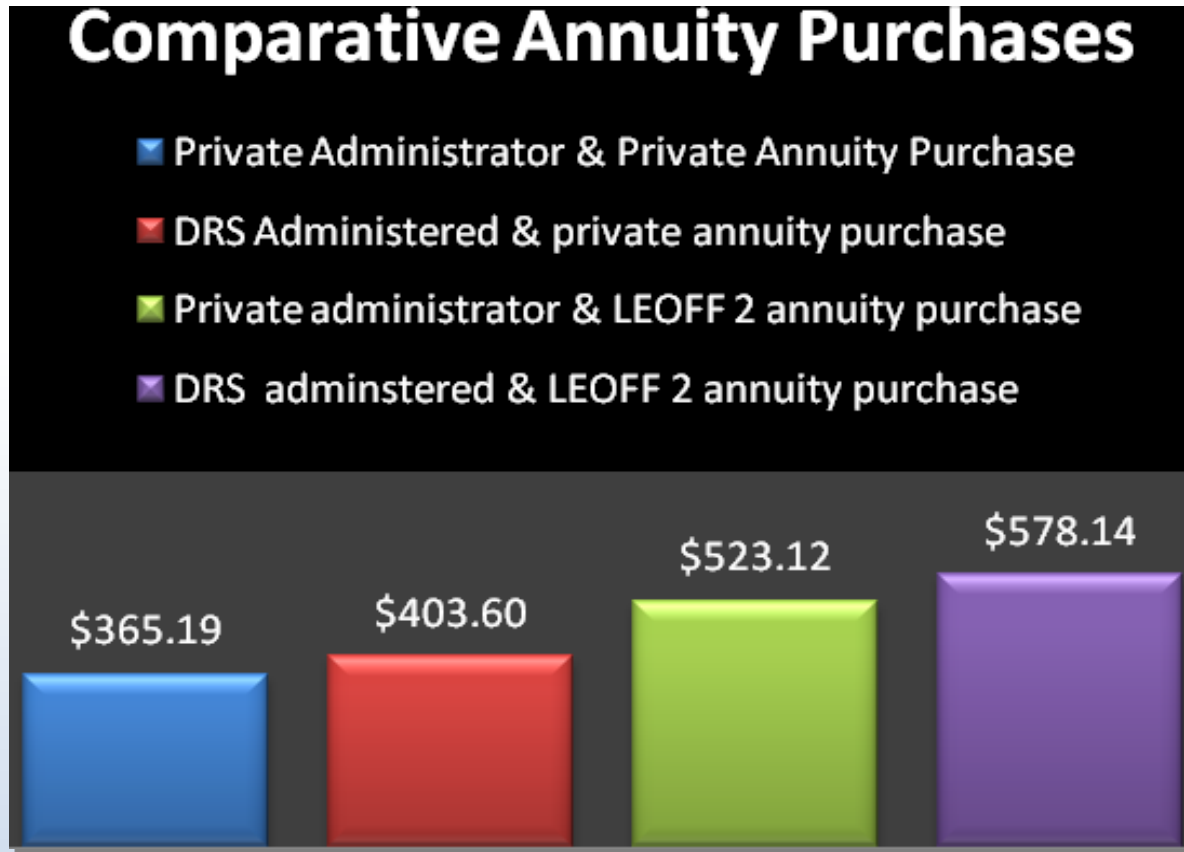
Background

Retiring members can purchase an annuity from LEOFF Plan 2 on more favorable terms than private annuities:

“[A] private insurer will provide the annuity based on an interest rate of about 4 percent, whereas DRS will provide the annuity based on an interest rate of about 8%” -- *OSA fiscal note on Board's 2010 purchase of annuity proposal*

Note: LEOFF Plan 2 uses 7.5%

Advantage: LEOFF 2



Assuming member deferral of \$3602 per year for 15 years at 7.5% rate of return.

Retirees Can Be Included

RCW 41.26.463 allows retiring LEOFF Plan 2 members to roll over funds to purchase an annuity.

- LEOFF retirees asked to be included
- Federal tax law allows benefit to be offered to retirees
- Requires legislation

Next Steps

1. Direct staff to continue to research and report on this issue
2. Defer to another interim
3. Dismiss the issue for now

Questions?

Contact:

Ryan Frost

Research Analyst

(360) 586-2325

ryan.frost@leoff.wa.gov



Income Leveling Options

Report Type:

Initial Consideration

Date Presented:

6/24/2015

Presenter Name and Title:

Ryan Frost, Research Analyst

Summary:

The Board is continually looking for ways to add benefits to the members at little to no cost to the plan. Income Leveling options are designed to provide members who retire between ages 53 and 67 with a consistent total income before and after receiving either Medicare or Social Security benefits.

Strategic Linkage:

This item supports the following Strategic Priority Goals:

Enhance the benefits for the members., Inform the stakeholders.

ATTACHMENTS:

Description	Type
 Income Leveling Options Report	Report
 Income Leveling Options Presentation	Presentation



June 24, 2015

Income Leveling Options

INITIAL CONSIDERATION

By Ryan Frost

Research Analyst

360-586-2325

ryan.frost@leoff.wa.gov

ISSUE STATEMENT

The Board is continually looking for ways to add benefits to the members at little to no cost to the plan. Income Leveling options are designed to provide members who retire between ages 53 and 67 with a consistent total income before and after receiving either Medicare or Social Security benefits.

OVERVIEW

There are two options the Board could decide to move forward with:

1. The Social Security leveling option is available for members who retire before Social Security Full Retirement Age (SSFRA). It provides an increased allowance before SSFRA and a reduced allowance after SSFRA. It is payable to a member for their lifetime only. SSFRA is age 65 for those people born before 1938. For those born later, SSFRA is between ages 65 and 67. Any member who is paying into Social Security, 58.5% of law enforcement officers and 6.5%¹ of fire fighters, would be impacted by implementing this option.
2. The Medicare Leveling option is an irrevocable election made at retirement to temporarily increase the amount of the monthly retirement benefit from LEOFF 2 if a member is under the age of 65. This increase is intended to help pay health insurance premiums until reaching the eligibility age for Medicare. However, there will be a permanent decrease in a member's monthly benefit amount to repay this pre-Medicare increase. In some cases, the permanent decrease in the benefit amount will be greater than the temporary initial increase. In essence, members are taking a loan against future benefits to fund this temporary increase and will pay it back in the form of a permanent decrease in benefits upon reaching Medicare eligibility. All members would be impacted by implementing this option.

BACKGROUND & POLICY ISSUES

¹http://leoff.wa.gov/boardmtgs/2005/BrdMtg_09.28.05/092805.9_LEOFF%20Plan%202%20Employer%20Benefit%20Survey%20Results.pdf

Social Security Leveling

Benefit payments are calculated using a Social Security estimate, which a member would normally receive at full retirement age. Members will need to provide a Personal Earnings & Benefit Estimate Statement (PEBES) from the SSA based on the date that they will be terminating LEOFF 2 employment. When a quote is requested, they would specify the date they plan to retire from their LEOFF 2 job. Then, they would ask for an estimate for full retirement (between ages 65 and 67). It's important to specify that this estimate includes "zero future earnings" for after LEOFF 2 employment is stopped.

If "no future earnings" is not specified, Social Security will assume that members are continuing to work to full retirement age and the quote will reflect that assumption. (The annual statement received from SSA cannot be used to calculate a benefit.) The amount LEOFF 2 will pay as an "acceleration" is based on the member's age and the number of years they're away from the SSFRA. It is important to know once the LEOFF 2 accelerated amount is determined from a Social Security estimate, it will not change (except for cost-of-living adjustments) even if the Social Security benefit turns out to be different from the member's original estimate.

If they retire from active service before eligible to collect Social Security benefits, at age 65, and is eligible to receive benefits from the Pension Plan, they would be able to elect the Social Security Leveling Option at the time of retirement. With this option, the monthly pension benefit payment is temporarily increased by the amount estimated the Social Security benefit will be when they hit their SSFRA. Starting the second month after reaching the SSFRA, the pension benefit is permanently decreased by the amount of this previously estimated Social Security benefit.

There is no actuarial difference in the total amount the member would receive if they choose this option, or if it's elected to receive the pension before the SSFRA without "leveling." However, this option may provide members with the flexibility and financial resources to retire earlier than they might be able to otherwise.

A modification of this option in Idaho allows for a retiree to set a 50% or 100% survivor benefit, which would continue the stream of payments throughout the designated survivors' lifetime.

Medicare Leveling

The member's regular retirement benefit will be calculated based on the retirement option that is selected: 0% survivor benefit, 50% survivor benefit, or 100% survivor benefit. If the Medicare leveling option is selected, the pre-Medicare increase will be added to the regular retirement benefit. Beginning in the month following their 65th birthday, their benefit will be permanently reduced to an amount less than the original retirement benefit to begin repaying the pre-Medicare increase.

The total benefits payable to the member over a lifetime will remain essentially the same, on average, and the calculation of the benefit must be actuarially equivalent to what they would receive had they elected a normal pension with no leveling. The option must be chosen at retirement, and such election is irrevocable.

The Medicare Leveling option expires upon the death of the member. Their election of the option will not affect the amount of benefits payable to the joint annuitant under the survivor option selected at retirement. A surviving spouse or joint annuitant's benefit will be based on the member's regular retirement benefit, including all cost of living adjustments after their retirement date. He or she will receive the amount as if the Medicare Leveling option had not been selected.



Income Leveling Options

Initial Consideration

June 24, 2015

Issue

- The Board is continually looking for ways to add benefits to the members at little to no cost to the plan
- Income Leveling options are designed to provide members who retire between ages 53 and 67 with a consistent total income before and after receiving Medicare or Social Security benefits

Overview

There are two options to consider:

- Social Security Leveling
- Medicare Leveling

Overview

Social Security Leveling

- Designed to provide members who retire between ages 53 and 67 with a consistent total income throughout their lives
- Provides an increased allowance from trust fund before SSFRA, and a reduced allowance after SSFRA
- Any member who is paying into Social Security, 58.5% of law enforcement officers and 6.5% of fire fighters, would be impacted by implementing this option

Overview

Medicare Leveling

- This increase is intended to help pay health insurance premiums until you become eligible for Medicare
- However, there will be a permanent decrease in your monthly benefit amount to repay this pre-Medicare increase

Background

Actuarial Equivalence

- There is no actuarial difference in the total amount received with or without either leveling option
- May provide you with the flexibility and financial resources to retire earlier than you might be able to otherwise

Example

Basic calculation with leveling option

- \$2000 per month pension benefit at 53
- \$1000 per month Social Security/Medicare benefit

Age	Pension	Social Security /Medicare	Total \$
53	\$2500	\$0	\$2500
65	\$1500	\$1000	\$2500

How Does it Work?

Social Security

- Benefit payments are calculated using your Social Security estimate, normally received at full retirement age
- The amount the LEOFF trust pays as an “acceleration” is based on your age and the number of years you are away from your SSFRA (Social Security Full Retirement Age)

How Does it Work?

Medicare

- Your regular retirement benefit will be calculated based on the survivor option you select: 0%, 50%, or 100%
- The pre-Medicare increase will be added to your regular retirement benefit
- Beginning in the month following your 65th birthday, your benefit will be permanently reduced to an amount less than your original retirement benefit to begin repaying the pre-Medicare increase

Survivor Options

Social Security

- 50%, more money to the retiree
- 100%, more money to the survivor
- Payments guaranteed throughout the designated survivors' lifetime

Survivor Options

Medicare

- Expires upon the death of the member
- The surviving spouse or joint annuitant's benefit will be based on your regular retirement benefit, including all cost of living adjustments after your retirement date
- He or she will receive the amount as if you had not made this election

Advantages

More money up front

- Either leveling option can allow you to retire earlier if your standard benefit isn't enough to live on

Simplicity

- Can also greatly simplify retirement financial planning, as your income will remain consistent throughout retirement

Disadvantages

Post-retirement employment

- The impact of post-retirement employment, even part-time, has a drastic effect on Social Security
- If the retiree continues to work in retirement, they will lose \$1 for every \$2 they earn above about \$14,000 a year

Benefit drop after reaching eligibility age

- Your pension benefit will drop after reaching eligibility age
- Often, retirees forget the reduction will occur and are unprepared when it happens

Next Steps

1. Direct staff to continue to research and report on this issue
2. Defer to another interim
3. Dismiss the issue for now

Questions?

Contact:

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Research Analyst

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Increasing Retirement Age

Report Type:

Initial Consideration

Date Presented:

6/24/2015

Presenter Name and Title:

Ryan Frost, Research Analyst

Summary:

The sponsor of a bill introduced in the 2015 session as SB 5982, believed that due to the increase in life expectancy, the retirement age of members should increase to reflect that extra cost.

Strategic Linkage:

This item supports the following Strategic Priority Goals:

Provide the stakeholders with a voice in plan governance., Maintain the financial integrity of the plan., Inform the stakeholders.

ATTACHMENTS:

Description		Type
 Increasing Retirement Age Presentation		Presentation
 Increasing Retirement Age Report		Report



June 24, 2015

Increasing Retirement Age

EDUCATIONAL BRIEFING

By Ryan Frost

Research Analyst

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ISSUE STATEMENT

The normal retirement age (NRA) for LEOFF 2 members are each increased by two years for persons who first become members of the retirement plan on or after July 1, 2015.

OVERVIEW

The NRA for a defined benefit retirement plan is generally the age at which a member can begin receiving an unreduced retirement allowance. For LEOFF 2 members, NRA is age 53. Most state retirement plans, including Washington's, permit members to retire early and receive a reduced retirement allowance.

The LEOFF 2 early retirement age is 50 for members with 20 or more years of service. Reductions are based on the difference between the member's age at retirement and age 53.

In 2012 the Society of Actuaries published the Mortality Improvement Scale BB Report, an updated table of annual mortality improvement rates. The new table documents increases in average life spans and includes projections for future additional increases. The updated table was used by the State Actuary in conducting the 2013 actuarial valuations for the state retirement plans.

BACKGROUND & POLICY ISSUES

NRA for all Washington Plan 2's were set in 1977 and LEOFF 2 was set at age 58. Since then, that age was modified twice with two different pieces of legislation:

- ESHB 1294 passed in 1993 to lower the NRA from 58 to 55. The purpose of the bill was three fold:
 1. To provide full retirement benefits to law enforcement officers and fire fighters at an appropriate age, which recognizes the unique nature and physical demands of their work.
 2. To provide a reasonable value from the retirement system for members who leave before retirement.
 3. Increase flexibility for members to make transitions into other public or private sector employment.

- ESSB 6530 passed in 2000, which provided two additional benefits to LEOFF 2 members:
 1. NRA was reduced to age 53.
 2. Members who are at least 50 years old and with at least 20 years of service, may receive a benefit reduced by 3 percent for each year the member is less than NRA.

Mortality Improvement

Since the original retirement ages were set in 1977, life expectancy has increased by over 5 years. The sponsor of a bill introduced in the 2015 session as SB 5982, believed that due to the increase in life expectancy, the retirement age of members should increase to reflect that extra cost. The concern was that the pension liability costs are outpacing the growth of other budgetary costs to the state.

Member Impacts

The bill would not affect anyone hired before the effective date of the bill. If the retirement age is raised, with the goal of paying out benefits for a shorter period of time, the cost of the benefits comes down. Contribution rates would lower for all current Plan 2 members, therefore current members would receive a savings of sort. The savings of the bill is split 50/50 between the employee and the employer. This bill was not vetted by the Select Committee on Pension Policy (SCPP) before it was introduced in the Senate.

State Impacts

The State Actuaries' Office (OSA) predicted an employer savings of \$3.0 billion over a 25 year period if the retirement ages of all plans was raised by 2 years. Changes to assumed retirement behavior also impact the results of this bill. If it's assumed there is no retirement behavior change, the total employer savings would be \$3.6 billion over the 25-year period instead of OSA's best estimate savings of \$3.0 billion. Conversely, if new members are expected to work longer than OSA's best estimate, the total employer savings would be \$2.5 billion over the 25-year period.



Increasing Retirement Age

Educational Briefing
June 24, 2015

Issue

The normal retirement age (NRA) for LEOFF 2 members are each increased by two years for persons who first become members of the retirement plan on or after July 1, 2015

Overview

- The NRA for a defined benefit retirement plan is generally the age at which a member can begin receiving an unreduced retirement allowance
- NRA for LEOFF 2 members is age 53

Overview

- NRA for all Washington's Plan 2's were set in 1977, and LEOFF 2 was set at age 58
- That age was modified twice with two different pieces of legislation

Legislative History

- ESHB 1294 passed in 1993 to lower the NRA from 58 to 55. The purpose of the bill was three fold:
 1. To provide full retirement benefits to law enforcement officers and fire fighters at an appropriate age, which recognizes the unique nature and physical demands of their work
 2. To provide a reasonable value from the retirement system for members who leave before retirement
 3. Increase flexibility for members to make transitions into other public or private sector employment

Legislative History

- ESSB 6530 passed in 2000, which provided two additional benefits to LEOFF 2 members:
 1. NRA was reduced to age 53
 2. Members who are at least 50 years old and with at least 20 years of service, may receive a benefit reduced by 3 percent for each year the member is less than NRA

Background

Mortality Improvement

- The sponsor of SB 5982 believed that due to the increase in life expectancy, the retirement age of members should increase to reflect that extra cost
- Since the retirement ages were set in 1977, life expectancy has increased by over 5 years
- The concern was that the pension liability costs are outpacing the growth of other budgetary costs to the state

Background

Member Impacts

- Will decrease the expected cost of benefits for new members
- Members will retire later and receive fewer pension payments than under current law
 - This is where the largest portion of the savings comes from
- Savings are split 50/50 between employer and current members

Background

State Impacts

- OSA's best estimate shows a savings of \$3.0 billion over a 25-year period
- If it's assumed there is no retirement behavior change, the total employer savings would be \$3.6 billion over the 25-year period
- If new members are expected to work longer than OSA's best estimate, the total employer savings would be \$2.5 billion over the 25-year period

Next Steps

1. Direct staff to continue to research and report on this issue
2. Defer to another interim
3. Dismiss the issue for now

Questions?

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Disaster Response Coverage

Report Type:

Initial Consideration

Date Presented:

6/24/2015

Presenter Name and Title:

Ryan Frost, Research Analyst

Summary:

LEOFF 2 members who are called up to federal service to respond to natural disasters such as the Chelan wildfires or the Oso mudslide have different, and often less, pension protections than those called into service for military reserves or the National Guard.

Strategic Linkage:

This item supports the following Strategic Priority Goals:

Enhance the benefits for the members., Inform the stakeholders.

ATTACHMENTS:

Description		Type
	Disaster Response Report	Report
	Disaster Response Presentation	Presentation



June 24, 2015

Disaster Response Coverage

Initial Consideration

By Ryan Frost

Research Analyst

360-586-2325

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ISSUE STATEMENT

LEOFF 2 members who are called up to federal service to respond to natural disasters such as the Chelan wildfires or the Oso mudslide have different, and often less, pension protections than those called into service for military reserves or the National Guard.

OVERVIEW

This paper will do the following:

- Explain current Washington State benefits
- Provide a history of legislation that has affected these benefits
- Deliver information about Federal Military benefits
- Discuss policy issues

BACKGROUND & POLICY ISSUES

Washington State Benefits

A member who dies before retirement is entitled to a standard death benefit ranging from a refund of contributions, up to an actuarially reduced monthly benefit paid to a surviving spouse or minor child. The monthly benefit received by the survivor is determined by the number of years the member has in the system at the time of death.

In addition to the monthly benefit, if a member dies in the line of duty, as of July 1, 2015 a \$236,443 death benefit will be paid to their designated beneficiary.

Legislative History

The Select Committee on Pension Policy (SCPP) and LEOFF Plan 2 Retirement Board passed joint legislation to the 2009 Legislature which provides an unreduced survivor annuity to qualifying survivors of members of all systems and plans who leave public employment due to service in the National Guard or Military Reserves and die while service honorable during a *period of war*.

The “period of war” language creates a gap where members who are called by the National Guard or Military to respond to natural disasters are not covered by that 2009 bill. Additional

legislation with language tying natural disaster responders to the unreduced survivor annuity would be required.

Federal Benefits Available to Survivors of Military Service Members

Department of Defense (DoD) benefits for survivors of deceased members of the armed forces vary significantly in purpose and structure. Benefits such as the death gratuity provide immediate cash payments to assist these survivors in meeting their financial needs during the period immediately following a member's death. Similarly, the Service Members' Group Life Insurance (SGLI) provides the life insurance policy value in a lump sum payment following the service member's death. Other benefits such as the Veteran's Administration Dependency and Indemnity Compensation (DIC) and the Survivor Benefit Plan (SBP) are designed to provide long-term monthly income. Additional death benefits provided by the DoD for survivors and dependents include housing assistance, health care, commissary and exchange benefits, educational assistance, and burial, funeral, and related benefits. Survivors may also receive death benefits from Social Security.

Policy Issues

There are two key issues related to the military death benefit: (1) consideration by the pension plan for military service and (2) adequacy of benefits provided to survivors of members killed in military service.

Currently, no considerations are made for members who are called to military service to respond to natural disasters, and are killed during that service. The survivor of a member killed in military service responding to natural disasters is treated the same, and has benefits computed the same as the survivor of a member who left employment for other reasons. Thus, a primary policy question is whether survivors of members who die while called to respond to natural disasters should receive the same benefits as members who die while serving in the military during a period of war.

If special consideration is provided to survivors of these members, then what level of benefit should be provided? The current benefit only provides a refund of accumulated contributions. Should this rise to the level of a line of duty death providing full earned benefits or does it only merit an enhanced survivor benefit that is more adequate than a lump sum refund of contributions. Further, is a lump sum payment the form the benefit should take, as most of the Federal benefits are, or is an annuity a more adequate?



Disaster Response Coverage

Initial Consideration
June 24, 2015

Issue

- **LEOFF 2 members who are called up to federal service to respond to natural disasters such as the Chelan wildfires or the Oso mudslide have different, and often less, pension protections than those called into service for military reserves or the National Guard**

Current Benefits

- **Members who die before retirement are entitled to a standard death benefit**
- **The benefit is determined by the number of years the member has in the system at the time of death**
- **For duty-related deaths, designated beneficiaries are paid a state death benefit of \$236,443 (effective July 1, 2015).**

Previous Legislation

- **The Select Committee on Pension Policy (SCPP) and LEOFF Plan 2 Retirement Board passed joint legislation to the 2009 Legislature**
 - The bill provides an unreduced survivor annuity to qualifying survivors of members of all systems and plans who leave public employment due to service in the National Guard or Military Reserves and die while in honorable service during a *period of war*.

Coverage Gap

- **The “period of war” language creates a gap where members who are called by the National Guard or Military to respond to natural disasters are not covered by that 2009 bill.**
- **Additional legislation with language tying natural disasters to the unreduced survivor annuity would be required.**

Key Issues

- **Two key issues related to the military death benefit:**
 - Consideration by the pension plan for military service
 - Adequacy of benefits provided to survivors of members killed in military service
- **Currently, no special considerations are made for members who are called to military service to respond to natural disasters, and are killed during that service.**

Key Issues

- **Survivors of a member killed in military service for responding to natural disasters is treated the same, and has benefits computed the same as the survivor of a member who left employment for other reasons**
- **A primary policy question is whether survivors of members who die while called to respond to natural disasters should receive the same benefits as members who die while serving in the military during a period of war.**

Next Steps

- 1. Direct staff to continue to research and report on this issue**
- 2. Defer to another interim**
- 3. Dismiss the issue for now**

Questions?

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Final Legislative Update

Report Type:

Educational Briefing

Date Presented:

6/24/2015

Presenter Name and Title:

Ryan Frost, Research Analyst

Summary:

Provides an overview of the most recent legislative changes as it concerns to contribution rates and the Benefit Improvement Account.

Strategic Linkage:

This item supports the following Strategic Priority Goals:
Inform the stakeholders.

ATTACHMENTS:

Description	Type
 Legislative Update Presentation	Presentation



2015 Legislative Update

June 24, 2015

Overview

- **Contribution Rates**
- **Benefit Improvement Account**

Rates

Budget Bill

Final budget not yet passed; Governor, House, and Senate each have proposed budgets

- Contribution Rates fully funded in all 3 proposed budgets.

Benefit Improvement Account

- Account Payment
 - Governor proposes \$10 million
 - House proposes cancelling 2015 payment
 - Senate proposes cancelling 2015 payment
 - Also, intent of the Senate is to suspend the payment in 2017 as it investigates whether this benefit should continue, be modified, or be terminated.

Questions?

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2015 AGENDA ITEMS CALENDAR

MEETING DATE	AGENDA ITEMS
January 28, 2015	2015 Legislative Update
February 25, 2015	2015 Legislative Update
March 25, 2015	2015 Legislative Update
April 22, 2015	2015 Legislative Update
May 27, 2015	2015 Legislative Review 2015 Interim Planning Supplemental Rate Adoption
June 24, 2015	Supplemental Rate Adoption Experience Study Timing – Lisa Won, OSA Retiree Purchase of Annuity Income Leveling Option Increasing Retirement Age Disaster Response Coverage Final Legislative Update
July 22, 2015	PEBB Access - Mary Fliss, HCA DRS Update, CEM Benchmarking – Mark Feldhausen, DRS Annual Attorney General Training – Dawn Cortez, AAG Experience Study Overview – OSA Administrative Factors - OSA Garnishment Forfeiture Health Savings Accounts
August 26, 2015	
September 23, 2015	
October 28, 2015	
November 18, 2015	
December 16, 2015	