

SUPPLEMENTAL RATE ADOPTION

LEOFF Plan 2 Retirement Board

July 27, 2011

OVERVIEW

- HB 2070
- Cost of Bill
- Options



HB 2070

- Commonly Referred to as “Furloughs Bill”
- Salary Reductions
 - Reduced work hours
 - Mandatory leave without pay
 - Temporary layoffs
 - Reduction to current pay



COSTS

- Office of the State Actuary
- Audit by Independent Actuary



OPTIONS

- Adopt Supplemental Contribution Rate with September 1, 2011 Implementation Date
 - Current assumptions
- Delay Adoption until December 1, 2011
 - Joint study with Association of Washington Cities (AWC) – August
 - Present data to OSA – September
 - Updated cost presentation to Board – October



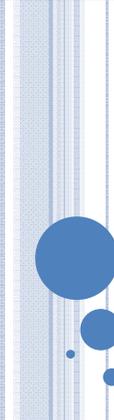
PROS & CONS

- Reliability of Assumptions
- Pre-funding of Costs



QUESTIONS?





SUPPLEMENTAL RATE ADOPTION
LEOFF Plan 2 Retirement Board
July 27, 2011

OVERVIEW

- HB 2070
- Cost of Bill
- Options



HB 2070

- Commonly Referred to as “Furloughs Bill”
- Salary Reductions
 - Reduced work hours
 - Mandatory leave without pay
 - Temporary layoffs
 - Reduction to current pay



COSTS

- Office of the State Actuary
- Audit by Independent Actuary



OPTIONS

- Adopt Supplemental Contribution Rate with September 1, 2011 Implementation Date
 - Current assumptions
- Delay Adoption until December 1, 2011
 - Joint study with Association of Washington Cities (AWC) – August
 - Present data to OSA – September
 - Updated cost presentation to Board – October



PROS & CONS

- Reliability of Assumptions
- Pre-funding of Costs



QUESTIONS?



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

Supplemental Rate Adoption

Final Proposal

July 27, 2011

1. Issue

The Board must decide whether it is necessary to increase contribution rates due to the passage of Substitute House Bill 2070, determining salary for pension purposes.

2. Staff

Greg Deam, Senior Research and Policy Manager
(360) 586-2325
greg.deam@leoff.wa.gov

3. Members Impacted

Based on the actuarial data as of June 30, 2009, there were 16,951 active LEOFF Plan 2 members. Adopting supplemental contribution rates impacts all active LEOFF Plan 2 members, employers and in most cases the state.

4. Current Situation

One of the main goals of the Board is to ensure the actuarial soundness of the plan. In order to maintain that goal, it may be necessary for the Board to pay for any benefit improvements via adoption of a supplemental contribution rate increase.

5. Background Information

One of the primary functions of the Board is to adopt contribution rates. The Board is required to use an accredited actuary using approved actuarial methods to determine the cost of the plan and the cost of any benefit improvements. The statutes covering adoption of supplemental contribution rates for LEOFF Plan 2 include RCW 41.26.720, 41.45.0604 and 41.45.070. These statutes can be found in Appendix A.

Not all benefit improvements will have costs sufficient to increase contribution rates, but if they do, the Board has the task of adopting a supplemental rate increase, usually effective September 1 following the effective date of the legislation.

During the 2011 legislative session, HB 2070 passed that stated a member's pension based on salaries earned during the 2011-13 biennium will not be reduced by compensation due to reduced work hours, mandatory leave without pay, temporary layoff, or reductions to current pay if the measures are an integral part of an employer's expenditure reduction efforts. The Office of the State Actuary (OSA) provided a revised fiscal note on June 14, 2011 indicating the cost of that benefit enhancement would require a contribution rate increase of two basis points for the member (0.02%), one basis point for the employer (0.01%) and one basis point for the state (0.01%).

Policy Issues

The normal process for adopting a supplemental rate increase is for the Board to take action in July for an effective date of September 1, based on the recommendation of OSA and the assumptions used in their fiscal note. However, in this case, it may be appropriate to defer adoption of the supplemental rate until a later date. The estimated cost of this benefit depends on how many members actually have their work hours reduced, have mandatory leave without pay, temporary layoffs or reduced salaries. The Actuary based his costs on the assumption that twenty-five percent of the active members in local government would have a two percent reduction in pay. A larger sample survey of this employer group may provide more reliable data.

The consequence of delaying the adoption of a supplemental rate is the loss of earnings on the contributions that would have been made, if indeed the original assumptions are correct. However, in this case, a delay in the adoption of a supplemental rate will not create a significant risk of underfunding the plan due to the relatively modest cost of the benefit improvement and the relatively delay.

6. Policy Options

Policy Option 1: Adopt Supplemental Rate Effective 9/1/11

Under this option the Board would need to adopt the supplemental contribution rate at the July 27, 2011 Board meeting.

Policy Option 2: Delay Adoption of Supplemental Rate

Under this option, the Board would conduct a joint study with the Association of Washington Cities (AWC) in August 2011 to determine the number of members impacted by this bill. The results of this study would be given to OSA in September 2011 to reevaluate the assumptions used in their prior fiscal note and see if those costs should be revised. OSA would provide a letter/presentation to the Board in October.

7. Appendix A – Contribution Rate Statutes

Appendix B – Letter on Costs from OSA

Appendix C – Letter from Marilyn Oliver, Independent Audit

APPENDIX A – Contribution Rate Statutes

RCW 41.26.720 Board of trustees — Powers — Meeting procedures — Quorum — Judicial review — Budget.

1) The board of trustees have the following powers and duties and shall:

(a) Adopt actuarial tables, assumptions, and cost methodologies in consultation with an enrolled actuary retained by the board. The state actuary shall provide assistance when the board requests. The actuary retained by the board shall utilize the aggregate actuarial cost method, or other recognized actuarial cost method based on a level percentage of payroll, as that term is employed by the American academy of actuaries. The actuary retained by the board shall adjust the actuarial cost method to recognize the actuarial present value of future revenue that will be included in the calculation of the market value of assets pursuant to RCW [41.26.805](#)(2), using the methods and assumptions employed by the state actuary in RCW [41.26.805](#)(9). In determining the reasonableness of actuarial valuations, assumptions, and cost methodologies, the actuary retained by the board shall provide a copy of all such calculations to the state actuary. If the two actuaries concur on the calculations, contributions shall be made as set forth in the report of the board's actuary. If the two actuaries cannot agree, they shall appoint a third, independent, enrolled actuary who shall review the calculations of the actuary retained by the board and the state actuary. Thereafter, contributions shall be based on the methodology most closely following that of the third actuary;

(b)(i) Provide for the design and implementation of increased benefits for members and beneficiaries of the plan, subject to the contribution limitations under RCW [41.26.725](#). An increased benefit may not be approved by the board until an actuarial cost of the benefit has been determined by the actuary and contribution rates adjusted as may be required to maintain the plan on a sound actuarial basis. Increased benefits as approved by the board shall be presented to the legislature on January 1st of each year. The increased benefits as approved by the board shall become effective within ninety days unless a bill is enacted in the next ensuing session of the legislature, by majority vote of each house of the legislature, repealing the action of the board;

(ii) As an alternative to the procedure in (b)(i) of this subsection, recommend to the legislature changes in the benefits for members and beneficiaries, without regard to the cost limitations in RCW [41.26.725](#)(3). Benefits adopted in this manner shall have the same contractual protections as the minimum benefits in the plan. The recommendations of the board shall be presented to the legislature on January 1st of each year. These measures shall take precedence over all other measures in the legislature, except appropriations bills, and shall be either enacted or rejected without change or amendment by the legislature before the end of such regular session;

(c) Retain professional and technical advisors necessary for the accomplishment of its duties. The cost of these services may be withdrawn from the trust;

(d) Consult with the department for the purpose of improving benefit administration and member services;

(e) Provide an annual report to the governor and the legislature setting forth the actuarial funding status of the plan and making recommendations for improvements in those aspects of retirement administration directed by the legislature or administered by the department;

(f) Establish uniform administrative rules and operating policies in the manner prescribed by law;

(g) Engage administrative staff and acquire office space independent of, or in conjunction with, the department. The department shall provide funding from its budget for these purposes;

(h) Publish on an annual basis a schedule of increased benefits together with a summary of the minimum benefits as established by the legislature which shall constitute the official plan document; and

(i) Be the fiduciary of the plan and discharge the board's duties solely in the interest of the members and beneficiaries of the plan.

(2) Meetings of the board of trustees shall be conducted as follows:

(a) All board meetings are open to the public, preceded by timely public notice;

(b) All actions of the board shall be taken in open public session, except for those matters which may be considered in executive session as provided by law;

(c) The board shall retain minutes of each meeting setting forth the names of those board members present and absent, and their voting record on any voted issue; and

(d) The board may establish, with the assistance of the appropriate office of state government, an internet web site providing for interactive communication with state government, members and beneficiaries of the plan, and the public.

(3) A quorum of the board is six board members. All board actions require six concurring votes.

(4) The decisions of the board shall be made in good faith and are final, binding, and conclusive on all parties. The decisions of the board shall be subject to judicial review as provided by law.

(5) A law enforcement officers' and firefighters' retirement system plan 2 expense fund is established for the purpose of defraying the expenses of the board. The board shall cause an annual budget to be prepared consistent with the requirements of chapter [43.88](#) RCW and shall draw the funding for the budget from the investment income of the trust. Board members shall be reimbursed for travel and education expenses as provided in RCW [43.03.050](#) and [43.03.060](#). The board shall make an annual report to the governor, legislature, and state auditor setting forth a summary of the costs and expenditures of the plan for the preceding year. The board shall also retain the services of an independent, certified public accountant who shall annually audit the expenses of the fund and whose report shall be included in the board's annual report.

[2008 c 99 § 5; 2003 c 2 § 5 (Initiative Measure No. 790, approved November 5, 2002).]

Notes:

Findings -- Purpose -- 2008 c 99: See note following RCW [41.26.800](#).

RCW 41.45.0604 Contribution rates — Law enforcement officers' and firefighters' retirement system plan 2.

(1) Not later than July 31, 2008, and every even-numbered year thereafter, the law enforcement officers' and firefighters' plan 2 retirement board shall adopt contribution rates for the law enforcement officers' and firefighters' retirement system plan 2 as provided in RCW [41.26.720](#)(1)(a).

(2) The law enforcement officers' and firefighters' plan 2 retirement board shall immediately notify the directors of the office of financial management and department of retirement systems of the state, employer, and employee rates adopted. Thereafter, the director shall collect those rates adopted by the board. The rates shall be effective for the ensuing biennial period, subject to any legislative modifications.

[2007 c 280 § 3; 2003 c 92 § 4.]

Notes:

Severability -- Effective date -- 2003 c 92: See RCW [41.26.905](#) and [41.26.906](#).

RCW 41.45.070 Supplemental rate.

*** CHANGE IN 2009 *** (SEE [6161-S.SL](#)) ***

(1) In addition to the basic employer contribution rate established in RCW [41.45.060](#) or [*41.45.054](#), the department shall also charge employers of public employees' retirement system, teachers' retirement system, school employees' retirement system, public safety employees' retirement system, or Washington state patrol retirement system members an additional supplemental rate to pay for the cost of additional benefits, if any, granted to members of those systems. Except as provided in subsections (6), (7), and (9) of this section, the supplemental contribution rates required by this section shall be calculated by the state actuary and shall be charged regardless of language to the contrary contained in the statute which authorizes additional benefits.

(2) In addition to the basic member, employer, and state contribution rate established in RCW [41.45.0604](#) for the law enforcement officers' and firefighters' retirement system plan 2, the department shall also establish supplemental rates to pay for the cost of additional benefits, if any, granted to members of the law enforcement officers' and firefighters' retirement system plan 2. Except as provided in subsection (6) of this section, these supplemental rates shall be calculated by the actuary retained by the law enforcement officers' and firefighters' board and the state actuary through the process provided in RCW [41.26.720](#)(1)(a) and the state treasurer shall transfer the additional required contributions regardless of language to the contrary contained in the statute which authorizes the additional benefits.

(3) The supplemental rate charged under this section to fund benefit increases provided to active members of the public employees' retirement system plan 1, the teachers' retirement system plan 1, and Washington state patrol retirement system, shall be calculated as the level percentage of all members' pay needed to fund the cost of the benefit not later than June 30, 2024.

(4) The supplemental rate charged under this section to fund benefit increases provided to active and retired members of the public employees' retirement system plan 2 and plan 3, the teachers' retirement system plan 2 and plan 3, the public safety employees' retirement system plan 2, or the school employees' retirement system plan 2 and plan 3 shall be calculated as the level percentage of all members' pay needed to fund the cost of the benefit, as calculated under RCW [41.45.060](#), [41.45.061](#), or [41.45.067](#).

(5) The supplemental rate charged under this section to fund postretirement adjustments which are provided on a nonautomatic basis to current retirees shall be calculated as the percentage of pay needed to fund the adjustments as they are paid to the retirees. The supplemental rate charged under this section to fund automatic postretirement adjustments for active or retired members of the public employees' retirement system plan 1 and the teachers' retirement system plan 1 shall be calculated as the level percentage of pay needed to fund the cost of the automatic adjustments not later than June 30, 2024.

(6) A supplemental rate shall not be charged to pay for the cost of additional benefits granted to members pursuant to chapter 340, Laws of 1998.

(7) A supplemental rate shall not be charged to pay for the cost of additional benefits granted to members pursuant to ****chapter [41.31A](#) RCW**; section 309, chapter 341, Laws of 1998; or section 701, chapter 341, Laws of 1998.

(8) A supplemental rate shall not be charged to pay for the cost of additional benefits granted to members and survivors pursuant to chapter 94, Laws of 2006.

(9) A supplemental rate shall not be charged to pay for the cost of the additional benefits granted to members of the teachers' retirement system and the school employees' retirement system plans 2 and 3 in sections 2, 4, 6, and 8, chapter 491, Laws of 2007 until September 1, 2008. A supplemental rate shall not be charged to pay for the cost of the additional benefits granted to members of the public employees' retirement system plans 2 and 3 under sections 9 and 10, chapter 491, Laws of 2007 until July 1, 2008.

[2007 c 491 § 12; 2006 c 94 § 3; (2005 c 327 § 10 expired July 1, 2006); 2004 c 242 § 41. Prior: (2003 1st sp.s. c 11 § 3 repealed by 2005 c 327 § 11); 2003 c 92 § 5; prior: 2001 2nd sp.s. c 11 § 16; 2001 2nd sp.s. c 11 § 15; 2000 c 247 § 505; 1998 c 340 § 10; 1995 c 239 § 310; 1990 c 18 § 2; 1989 1st ex.s. c 1 § 1; 1989 c 273 § 7.]

Notes:

Reviser's note: *(1) RCW [41.45.054](#) was decodified by 2005 c 370 § 5, effective September 1, 2005.

** (2) Chapter [41.31A](#) RCW was repealed by 2007 c 491 § 13, effective January 2, 2008, however, RCW [41.31A.020](#) was also amended by 2007 c 491 § 1 and 2007 c 492 § 10. For rule of construction, see RCW [1.12.025](#)(1).

Severability -- Conflict with federal requirements -- 2007 c 491: See notes following RCW [41.32.765](#).

Effective date -- 2006 c 94 § 3: "Section 3 of this act takes effect July 1, 2006." [2006 c 94 § 4.]

Expiration date -- 2005 c 327 § 10: "Section 10 of this act expires July 1, 2006." [2005 c 327 § 13.]

Effective date -- 2004 c 242: See RCW [41.37.901](#).

Effective date -- 2003 1st sp.s. c 11: See note following RCW [41.45.035](#).

Severability -- Effective date -- 2003 c 92: See RCW [41.26.905](#) and [41.26.906](#).

Effective date -- 2001 2nd sp.s. c 11: See note following RCW [41.45.010](#).

Effective date -- 2001 2nd sp.s. c 11: See note following RCW [41.45.030](#).

Effective dates -- Subchapter headings not law -- 2000 c 247: See RCW [41.40.931](#) and [41.40.932](#).

Effective date -- 1998 c 341: See RCW [41.35.901](#).

Effective date -- 1998 c 340: See note following RCW [2.10.146](#).

Intent -- Purpose -- 1995 c 239: See note following RCW [41.32.831](#).

Effective date -- Part and subchapter headings not law -- 1995 c 239: See notes following RCW [41.32.005](#).

Effective date -- 1990 c 18: See note following RCW [41.45.060](#).

Benefits not contractual right until date specified: RCW [41.34.100](#).

APPENDIX B – Letter on Costs from OSA



Office of the State Actuary

"Securing tomorrow's pensions today."

June 14, 2011

Mr. Steve Nelsen
Executive Director
LEOFF Plan 2 Retirement Board
P.O. Box 40918
Olympia, Washington 98504-0918

SUBJECT: 2011 SUPPLEMENTAL CONTRIBUTION RATES

Dear Steve:

As required under RCW 41.45.070, we are forwarding the required supplemental rate increases, effective September 1, 2011, for the following bill that passed during the 2011 Legislative Session.

| LEOFF 2 | Members | Employer | State |
|---------------------|---------|----------|-------|
| HB 2070 (C 5, L 11) | 0.02% | 0.01% | 0.01% |

According to RCW 41.45.070(2), the actuary retained by the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board (the Board) and the state actuary calculate supplemental contribution rates for LEOFF Plan 2 through the process provided in RCW 41.26.720(1)(a). The Board will forward to the Department of Retirement Systems (DRS) any supplemental rate increases required for HB 2070 (C 5, L 11) under separate correspondence.

RCW 41.45.067(2) requires that DRS provide a 30-day notice to affected employers prior to the effective date of any rate change. If the Board adopts supplemental rates by their July Board meeting, that should provide enough time to notify DRS in order for them to meet their statutory deadline.

Please find attached the Actuarial Fiscal Note prepared by our office for HB 2070 to support the supplemental rates listed above.



We have not identified any additional legislation that requires a supplemental rate increase for LEOFF 2 at this time. Please feel free to contact me directly should you have any questions.

Sincerely,

Matthew M. Smith, FCA, EA, MAAA
State Actuary

Attachment

Actuarial Fiscal Note for HB 2070

cc: Marcie Frost, Deputy Director
Department of Retirement Systems
Lisa Won, Actuary
Office of the State Actuary

O:\LEOFF 2 Board\2011\6-15-11\2011_L2_Supplemental_Rates.docx

APPENDIX C – Letter from Marilyn Oliver, Independent Audit

OLIVER CONSULTING

CONSULTING ACTUARIES

104 CALEDONIA STREET, SUITE A
SAUSALITO, CALIFORNIA 94965
415-331-5784, voice
415-331-0559, fax

June 30, 2011

Law Enforcement Officers' & Firefighters' Plan 2 Retirement Board
P.O. Box 40918
Olympia, Washington 98504-0918

Re: Actuarial Review: of Supplemental Contribution Rates for HB 2070 in June 14, 2011 Fiscal Note

Chairman Fox and Members of the Board:

There follow the results of our actuarial review of the above fiscal note.

Background

HB 2070 includes in final average salary for pension purposes any compensation foregone by a member employed by the State or a local government employer during the 7/1/2011-6/30/2013 biennium due to:

- (1) Reduced work hours
- (2) Mandatory leave without pay
- (3) Temporary layoffs, or
- (4) Reductions to current pay (but not elimination of previously agreed upon future salary increases).

The compensation foregone must be an integral part of the employer's expenditure reduction efforts, as certified by the employer.

The estimated increases in contribution rates calculated by the Office of the State Actuary are shown below.

| | |
|--------------|--------------|
| Employee | 0.02% |
| Employer | 0.01% |
| <u>State</u> | <u>0.01%</u> |
| Total | 0.04% |

Results of Review

Assumptions

In order to estimate the cost of this legislation it is necessary to make assumptions regarding the impact of foregone compensation on salary includable in final average. For State employees subject to HB 5620 (State Employees – Compensation Reduction), a 3% reduction is assumed consistent with HB 5620. For LEOFF 2 active members employed by local government a 2% compensation decrease has been assumed for 25% of the membership.

The assumptions for local government are based on judgment, the results of a phone survey of 5 large counties (King, Pierce, Snohomish, Spokane, and Thurston), and a survey conducted by the Association of Washington Cities (AWC). With the exception of Pierce County, which indicated that they started a

voluntary leave program, respondents to the County survey generally did not anticipate compensation reductions covered under the bill in the short term. Weighting by city size, about 12% of the 171 respondents to the AWC survey indicated that they would be reducing hours in 2011, while 7% indicated that they would be implementing salary reductions. Neither of the surveys indicated which employee groups would be affected (for example general, police, or fire) or what level of compensation reductions would be involved. Based on the small amount of data available the assumption used for local government employees does not appear unreasonable.

A more complete survey of cities and counties is being conducted which is designed to gather information specific to HB 2070. This survey may include information related to the likelihood of HB 2070 compensation reductions for LEOFF active employees and estimates of the magnitude of those compensation reductions. This may provide a basis for reviewing the compensation reduction assumptions used for LEOFF 2 members employed by local government.

Calculations

The methodology used was to keep the current salary increase assumptions in place with the following modifications:

- Reduce valuation pay by the compensation reduction assumption
- In two years remove the compensation reduction.

We concur with this methodology.

We independently calculated the supplemental rates and agree with the rates shown on page 1.

Summary

We reviewed the supplemental contribution rate increases shown in the Office of the State Actuary June 14, 2011 Fiscal Note for HB 2070

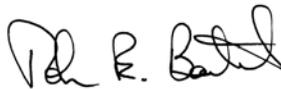
Prediction of the compensation reductions that may be adopted by local government agencies during the 2011/13 biennium is difficult. However, we agree that these supplemental rates represent reasonable estimates of the costs.

The undersigned are members of the American Academy of Actuaries and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

Sincerely,



Marilyn M. Oliver, F.S.A., M.A.A.A.
Actuary and Principal
Oliver Consulting
Contractor



John E. Bartel, A.S.A., M.A.A.A.
President
Bartel Associates, LLC
Peer Review

c. Steve Nelsen, Executive Director
Matthew M. Smith, State Actuary