

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

Actuarial Reductions Preliminary Report

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1. Issue

The term “actuarial reduction” is used to calculate both disability benefits and duty-related death benefits in LEOFF Plan 2, but is undefined in either statute or administrative code.

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3. Members Impacted

Any of the current members of LEOFF Plan 2 could be affected. Similar language is used in the death and disability statutes for PERS 2/3, TRS 2/3, and SERS 2/3.

4. Current Situation

The LEOFF Plan 2 disability statute [RCW 41.26.470] and the LEOFF Plan 2 death benefits statute [RCW 41.26.510] both refer to the application of an “actuarial reduction” with respect to the calculation of benefits under these sections. RCW 41.26.470(1) provides in part that a member’s benefit be “actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age fifty-three.” RCW 41.26.510(4) provides in part that the retirement allowance of a member who is killed in the course of employment “is not subject to an actuarial reduction.” Neither the term “actuarially reduced” nor the term “actuarial reduction” is defined in statute or by agency rule.

The Department of Retirement Systems was recently required to determine in an administrative appeal whether the requirement of an actuarial reduction, with respect to a 2003 duty-related disability retirement of a member aged 50+ with 20+ years of service, meant the full early-retirement actuarial reduction or the subsidized early-retirement actuarial reduction of 3%/year for each year the member is younger than age 53.

5. Background Information and Policy Issues

Disability Benefits:

The LEOFF Plan 2 disability statute [RCW 41.26.470] provides in part:

- (1) A member of the retirement system who becomes totally incapacitated for continued employment by an employer as determined by the director shall be eligible to receive an allowance under the provisions of RCW 41.26.410 through 41.26.550. Such member shall receive a monthly disability allowance computed as provided for in RCW 41.26.420 and shall have such allowance *actuarially reduced* to reflect the difference in the number of years between age at disability and the attainment of age fifty-three, except under subsection (7) of this section (emphasis added)."

The exception under subsection (7) referenced in (1) applies to duty-related disability benefits, which a member is entitled to receive without an actuarial reduction for early retirement since May 13, 2005; the effective date of the Board's Duty Disability legislation in 2005 [chapter 451, laws of 2005]. That legislation did not apply retroactively.

The Department of Retirement Systems determined earlier this year in an administrative appeal that the "actuarial reduction" required by RCW 41.26.470(1) must mean the full early-retirement actuarial reduction and cannot mean the subsidized early-retirement reduction, even though the member in question was aged 50 and had more than 20 years of service. The Board unsuccessfully filed an amicus brief in this matter arguing that the subsidized early-retirement option should have been applied.

A subsidized early retirement actuarial reduction for LEOFF Plan 2 was first enacted in Chapter 247, Laws of 2000, Section 904, codified at RCW 41.26.430. This legislation contained over 60 separate sections and broadly affected the state retirement systems, as well as creating an alternate early-retirement for several retirement plans including LEOFF Plan 2. As might be expected with legislation of such broad scope, the legislative record is equally broad. Thus, there is no specific reference in the written record as to the relationship between the new subsidized early-retirement option for LEOFF Plan 2 in RCW 41.26.430 and the term "actuarial reduction" as used with respect to disability benefits under RCW 41.26.470. In fact, the issue was obscured because the 2000 legislation failed to amend the retirement age reference in RCW 41.26.470 from age 55 to age 53.

The Legislature addressed this discrepancy in retirement age the following year. Legislation to lower the disability retirement age was recommended by the Joint Committee on Pension Policy in 2001 and the bill summary states that the failure to change the disability retirement age in 2000 (from 55 to 53) was inadvertent. However, the 2001 bill did not specifically address the question of whether the subsidized early-retirement option for members aged 50 with 20 years of service was also intended to apply to disability retirements.

Death Benefits:

The Legislature amended the death benefits for PERS, TRS and SERS in 2003 to provide that, “The retirement allowance of a member who is killed in the course of employment, as determined by the director of the department of labor and industries, is not subject to an actuarial reduction” [Chapter 155, Laws of 2003, TRS 1 – RCW 41.32.520, TRS 2 – RCW 41.26.805, TRS 3 – RCW 41.32.895, SERS 2 – 41.35.460, SERS 3 – RCW 41.35.710, PERS 1 – 41.40.270, PERS 2 – 41.40.700, PERS 3 – 41.40.835]. The Legislature similarly amended the death benefits for LEOFF Plan 2 and WSPRS Plan 2 in 2004 [Chapter 5, Laws of 2004, LEOFF 2 – RCW 41.26.510; Chapters 170 and 171 Laws of 2004, WSPRS 2 – RCW 41.43.295].

The final bill report for the 2003 legislation summarizes the effect of the bill as follows, “The survivor benefit paid from a member’s earned retirement benefit to survivors of PERS, SERS, and TRS members killed in the course of employment is not subject to *an early retirement* actuarial reduction.” (emphasis added). The Legislature’s intent was clear that the term “actuarial reduction” as used in the bill was intended to apply to the early-retirement actuarial reduction and not the actuarial reduction for a survivor benefit.

The Office of the State Actuary’s summary of the 2003 legislation in its fiscal note on the bill also stated that, “This bill impacts the Teachers’ Retirement System (TRS), School Employees’ Retirement System (SERS), and Public Employees’ Retirement System (PERS), by providing that the survivor benefit of a member killed in the course of employment, after having accumulated at least 10 years of service, is not subject to *an early retirement* actuarial reduction.” (emphasis added).

The Department of Retirement Systems’ summary of the 2003 legislation in its fiscal note on the bill stated, “This bill applies to members of the Teachers’ Retirement System (TRS), School Employees’ Retirement System (SERS), and Public Employees’ Retirement System (PERS). It provides that the retirement allowance for the surviving spouse or eligible child or children, is not subject to an *actuarial reduction* for retirement prior to eligibility if the member is killed in the course of employment, as determined by the Director of the Department of Labor and Industries (L&I).” (emphasis added).

Both the Office of the State Actuary and the Department of Retirement Systems used identical language in their fiscal note summaries of the 2004 legislation proposed by the LEOFF Plan 2 Retirement Board (HB 2419) that they had previously used to describe the 2003 legislation. Similarly, the House Bill Report for HB 2419 as it passed the Legislature in 2004 described the effect of the legislation as, “The survivor benefit paid from a member’s earned retirement benefit to survivors of LEOFF 2 members killed in the course of employment is not subject to *an early retirement* actuarial reduction.” (emphasis added).

It is clear that the Office of the State Actuary interpreted the effect of the 2003 and 2004 legislation as removing both the full early-retirement actuarial reduction and the subsidized early-retirement reduction.

Similarly, in the July 2004 edition of the Washington State Retirement *Outlook* published by the Department of Retirement Systems, the Legislative Update summarizes the effect of HB 2419 as follows, “Under House Bill 2419, the beneficiary of a LEOFF Plan 2 member who is killed in the course of employment, as determined by the Director of the Department of Labor & Industries, would receive benefits *without reduction for early retirement*. The member must have had at least ten years of service.” (emphasis added).

The Department of Retirement Systems’ actual administrative practice with respect to this benefit is unclear, since the Board does not have access to the actual benefits paid to surviving spouses of line-of-duty LEOFF 2 deaths, since the enactment of HB 2419. However, the Department of Retirement Systems has informed Board staff that a survivor of a line-of-duty death would receive a benefit under RCW 41.26.510 without either the full early-retirement actuarial factor or the subsidized early-retirement reduction factor.

It seems clear that the Legislature, the Office of the State Actuary, and the Department of Retirement Systems have all consistently interpreted and administered the term “actuarial reduction” as used for LEOFF Plan 2 duty-related death benefits under RCW 41.26.510 (and similar statutes for PERS, TRS and SERS) as synonymous with “early-retirement actuarial reduction” and as applying to both the full early-retirement actuarial reduction and the subsidized early-retirement actuarial reduction.

Policy Options:

Legislation would be necessary if the Board believes that either:

- Disability retirees aged 50+ with 20+ years of service should be entitled to the subsidized early-retirement reduction; or,
- The statutory language for death benefits is inappropriately vague.

6. Policy Options

Option One:

Draft a bill to provide that the eligibility requirements for service retirements and disability retirements are identical with respect to members who are age 50 with 20 years of service. Request that the Department of Retirement Systems adopt rules regarding the actuarial reductions that will be applied to death benefits.

Option Two:

Draft a bill to provide that the eligibility requirements for service retirements and disability retirements are identical with respect to members who are age 50 with 20 years of service. The bill would also codify the intended legislative interpretation of “actuarial reductions” with respect to death benefits.

7. Supporting Information

RCW 41.26.470

(1) A member of the retirement system who becomes totally incapacitated for continued employment by an employer as determined by the director shall be eligible to receive an allowance under the provisions of RCW 41.26.410 through 41.26.550. Such member shall receive a monthly disability allowance computed as provided for in RCW 41.26.420 and shall have such allowance actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age fifty-three, except under subsection (7) of this section.

(2) Any member who receives an allowance under the provisions of this section shall be subject to such comprehensive medical examinations as required by the department. If such medical examinations reveal that such a member has recovered from the incapacitating disability and the member is no longer entitled to benefits under Title 51 RCW, the retirement allowance shall be canceled and the member shall be restored to duty in the same civil service rank, if any, held by the member at the time of retirement or, if unable to perform the duties of the rank, then, at the member's request, in such other like or lesser rank as may be or become open and available, the duties of which the member is then able to perform. In no event shall a member previously drawing a disability allowance be returned or be restored to duty at a salary or rate of pay less than the current salary attached to the rank or position held by the member at the date of the retirement for disability. If the department determines that the member is able to return to service, the member is entitled to notice and a hearing. Both the notice and the hearing shall comply with the requirements of chapter 34.05 RCW, the Administrative Procedure Act.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

(7) A member who becomes disabled in the line of duty shall be entitled to receive a minimum retirement allowance equal to ten percent of such member's final average salary. The member shall additionally receive a retirement allowance equal to two percent of such member's average final salary for each year of service beyond five.

(8) A member who is totally disabled in the line of duty is entitled to receive a retirement allowance equal to seventy percent of the member's final average salary. The allowance provided under this subsection shall be offset by:

(a) Temporary disability wage-replacement benefits or permanent total disability benefits provided to the member under Title 51 RCW; and

(b) Federal social security disability benefits, if any;
so that such an allowance does not result in the member receiving combined benefits that exceed one hundred percent of the member's final average salary. However, the offsets shall not in any case reduce the allowance provided under this subsection below the member's accrued retirement allowance.

A member is considered totally disabled if he or she is unable to perform any substantial gainful activity due to a physical or mental condition that may be expected to result in death or that has lasted or is expected to last at least twelve months. Substantial gainful activity is defined as average earnings in excess of eight hundred sixty dollars a month in 2006 adjusted annually as determined by the director based on federal social security disability standards. The department may require a person in receipt of an allowance under this subsection to provide any financial records that are necessary to determine continued eligibility for such an allowance. A person in receipt of an allowance under this subsection whose earnings exceed the threshold for substantial gainful activity shall have their benefit converted to a line-of-duty disability retirement

allowance as provided in subsection (7) of this section.

Any person in receipt of an allowance under the provisions of this section is subject to comprehensive medical examinations as may be required by the department under subsection (2) of this section in order to determine continued eligibility for such an allowance.

RCW 41.26.510

(1) Except as provided in RCW 11.07.010, if a member or a vested member who has not completed at least ten years of service dies, the amount of the accumulated contributions standing to such member's credit in the retirement system at the time of such member's death, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's estate, or such person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's accumulated contributions standing to such member's credit in the retirement system, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) If a member who is eligible for retirement or a member who has completed at least ten years of service dies, the surviving spouse or eligible child or children shall elect to receive either:

(a) A retirement allowance computed as provided for in RCW 41.26.430, actuarially reduced by the amount of any lump sum benefit identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670 and actuarially adjusted to reflect a joint and one hundred percent survivor option under RCW 41.26.460 and if the member was not eligible for normal retirement at the date of death a further reduction as described in RCW 41.26.430; if a surviving spouse who is receiving a retirement allowance dies leaving a child or children of the member under the age of majority, then such child or children shall continue to receive an allowance in an amount equal to that which was being received by the surviving spouse, share and share alike, until such child or children reach the age of majority; if there is no surviving spouse eligible to receive an allowance at the time of the member's death, such member's child or children under the age of majority shall receive an allowance share and share alike calculated as herein provided making the assumption that the ages of the spouse and member were equal at the time of the member's death; or

(b)(i) The member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670; or

(ii) If the member dies on or after July 25, 1993, one hundred fifty percent of the member's accumulated contributions, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670. Any accumulated contributions attributable to restorations made under RCW 41.50.165(2) shall be refunded at one hundred percent.

(3) If a member who is eligible for retirement or a member who has completed at least ten years of service dies after October 1, 1977, and is not survived by a spouse or an eligible

child, then the accumulated contributions standing to the member's credit, less any amount identified as owing to an obligee upon withdrawal of accumulated contributions pursuant to a court order filed under RCW 41.50.670, shall be paid:

(a) To an estate, a person or persons, trust, or organization as the member shall have nominated by written designation duly executed and filed with the department; or

(b) If there is no such designated person or persons still living at the time of the member's death, then to the member's legal representatives.

(4) The retirement allowance of a member who is killed in the course of employment, as determined by the director of the department of labor and industries, is not subject to an actuarial reduction. The member's retirement allowance is computed under RCW 41.26.420.

(5) The retirement allowance paid to the spouse and dependent children of a member who is killed in the course of employment, as set forth in RCW 41.05.011(14), shall include reimbursement for any payments of premium rates to the Washington state health care authority pursuant to RCW 41.05.080.