

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

**Duty Disability Actuarial Reduction
Final Proposal**

December 9, 2004

Issue

The pension benefits for LEOFF Plan 2 members who become disabled in the line of duty are subject to an actuarial reduction for "early retirement" based on the member's age.

Staff

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Members Impacted

For purposes of HB 2418 in 2004 the Office of the State Actuary estimated that 12 LEOFF Plan 2 members per year become disabled in the line of duty. However, exact historical disability information for LEOFF Plan 2 is not available.

Current Situation

A LEOFF Plan 2 member who becomes totally incapacitated for continued employment as a law enforcement officer or firefighter is eligible to receive a disability retirement benefit. The disability retirement benefit is actuarially reduced based on the difference between the member's age and age 53, the plan's normal retirement age. The actuarial reduction applies whether the disability is duty-related or not. Members who are totally disabled and incapable of substantial future employment in any capacity receive the same benefits as members who may be capable of non-LEOFF employment.

History

HB 2418 in 2004 provided minimum duty disability benefits for LEOFF Plan 2 members. That legislation did not adjust the actuarial reduction for disability retirements.

Example

A law enforcement officer or firefighter who is age 43 with 15 years of service credit and a final average salary of \$45,000/year is totally incapacitated for continued employment. The member is eligible for a disability pension even though they do not meet the age and service requirements for normal retirement.

The member's base pension is equal to 2% of their final average salary multiplied by their years of service. In this case, $2\% \times \$45,000/\text{year} \times 15 =$ a base pension of \$13,500/year or \$1125/month.

The member's base pension is reduced by an actuarial factor determined by how far the member is from the age 53 normal retirement age. In this case, the member is ten years from

normal retirement eligibility so the reduction factor is 0.43 and the member's base pension would be reduced to \$483.75/month.

Background Information and Policy Issues

Duty Disability benefits were given initial consideration by the Board on May 26, 2004. A Preliminary Report was discussed by the Board on May 26, 2004. The Board had follow-up discussions on August 25, 2004 and September 22, 2004.

Comparison of Duty v. Non-Duty Benefits:

The disability retirement benefits for LEOFF Plan 2 are provided in RCW 41.26.470 [see Appendix A]. LEOFF Plan 2 members whose disability occurs in the line of duty are eligible for some benefits that are not available to members whose disability is not duty related.

Specifically,

- The member may receive service credit for up to six months from the date of injury or illness; and
- The member may be entitled to a disability leave supplement from their employer equal to 50% of base monthly salary for periods of temporary total disability up to a maximum of six months; and
- The member is entitled to either withdraw 150% of their accumulated contributions and interest or receive a disability retirement pension that cannot be reduced below 10% of the member's average final salary.

Determination of Disability:

The Department of Retirement Systems evaluates LEOFF Plan 2 disability retirement applications. The member must be totally incapacitated for employment by a LEOFF employer and the disabling injury or illness must be sustained in the course of employment in order to qualify for duty-related disability retirement benefits. The Department uses medical records and findings of the Department of Labor & Industries to determine whether the member's disabling condition was sustained in the course of employment.

Actuarial Benefit Reduction:

The base pension formula for disability retirees is the same whether the disability is duty-related or not. The base formula is 2 percent multiplied by the member's final average salary multiplied by the member's years of service and actuarially reduced by the difference between the member's age at the time of disability and age 53.

- The member's final average salary is the average of the member's basic salary for the highest consecutive sixty months prior to retirement.
- The actuarial reduction factors are found in WAC 412-02-320 [see Appendix B].

The member's base pension may be further reduced at the member's option in order to provide a survivor benefit to a beneficiary such as the retiree's spouse or to pay premiums for health insurance.

Comparison to Other Public Pension Plans in Washington:

LEOFF Plan 2 and the Plan 2/3 systems for PERS, TRS and SERS all have roughly the same disability benefit (2% x average final salary x years of service actuarially reduced by the member's age compared to normal retirement age) and the same statutory standard, "totally

incapacitated for continued employment by an employer as determined by the Department of Retirement Systems.”

LEOFF Plan 2 and the Plan 2/3 systems for PERS, TRS and SERS all use a 60-month period for determining final average salary. The effect of the actuarial reduction for the member’s age compared to normal retirement age is different between LEOFF 2 and the Plan 2/3 systems for PERS, TRS and SERS for two reasons:

- The normal retirement age in LEOFF 2 is age 53 compared to age 65 in the other Plan 2/3 systems; and
- The Plan 2/3 systems for PERS, TRS and SERS use a different actuarial reduction factor than that used for LEOFF Plan 2 [WAC 415-02-320(6)]. The reason for the difference in the factors is the different experience for LEOFF Plan 2.

The Plan 1 retirement systems (PERS 1, TRS 1, and LEOFF 1) and the Washington State Patrol Retirement System (WSPRS) all have very different disability retirement benefits and different disability standards.

Post-Retirement Employment:

The current LEOFF Plan 2 disability standard allows a member to qualify for a disability benefit if they are no longer capable of performing the duties of a law enforcement officer or firefighter, even if they are capable of other non-LEOFF employment.

A LEOFF Plan 2 retiree, including a disability retiree, is not eligible to receive their pension if they are re-employed as a law enforcement officer or firefighter or if they are employed in an eligible position in the public employees’ retirement system (PERS), the teachers’ retirement system (TRS), or the school employees’ retirement system (SERS). The retiree’s benefits are reinstated when they terminate the employment that causes the benefits to be suspended.

A retiree’s pension is not suspended if they return to work for a private employer, for a public employer in another state, or if the retiree returns to work in an ineligible position for a public employer in Washington.

The amount of the current disability benefit (see example on page one) and the ability to receive a disability benefit while engaged in non-LEOFF employment are both indicators that the current benefit is based on the assumption that the disabled member will continue to work in some capacity.

IRS Treatment of Duty-Related Disability Retirement Benefits:

Duty-related disability retirement benefits may qualify for favorable federal income tax treatment if the benefits meet certain statutory requirements. Some of the key requirements are:

- The disabling injury or illness must have occurred as a result of the member’s employment; and
- The benefit cannot be based on the member’s service; and
- The benefit cannot be based on the member’s age.

The base pension benefit in LEOFF Plan 2 does not qualify for favorable federal income tax treatment even if the disability is duty-related because the base pension is based on a member's years of service and may be actuarially reduced based on the member's age.

House Bill 2418 which was passed by the Legislature in 2004 established a minimum benefit for duty-related disabilities equal to 10% of the member's final average salary or 150% of the member's accumulated contributions and interest. This benefit qualifies for favorable income tax treatment under current law.

Comparisons with other States:

Duty-related disability benefits in police and fire plans around the nation typically fall into three categories:

- A minimum benefit based on the member's salary and unrelated to the member's age and/or service. The 10% minimum benefit in LEOFF Plan 2 is an example of this type of benefit.
- A pension based on the member's service which may or may not be reduced by the member's age. The base disability benefit in LEOFF Plan 2 is an example of this type of benefit.
- A special benefit for members who are extremely disabled. LEOFF Plan 2 does not have a benefit which falls into this category. The disability standard and benefit vary greatly from plan to plan in other states but an example of this type of benefit would be a lifetime benefit based on the member's salary and might include medical care for a member whose disability prevents all further employment in any capacity, public or private.

Number of Members Affected:

There have been very few disability retirements in LEOFF Plan 2 since the plan became effective in 1977. There are a number of possible reasons for this historical experience.

- Members who were not vested may have chosen to withdraw their accumulated contributions plus interest.
- Members who were already eligible for a service retirement would have received no additional retirement benefit from a disability retirement.
- Members with ten years of service who were not eligible for a service retirement may have preferred to withdraw 150% of their accumulated contributions and interest rather than take an actuarially-reduced pension.
- Members who were not eligible for a service retirement may have elected to defer retirement until normal retirement age rather than take an actuarially-reduced pension.

The Office of the State Actuary (OSA) estimated that 12 LEOFF Plan 2 members become disabled in the line of duty each year in the fiscal note for HB 2418 in 2004. OSA used historical experience in the State Patrol Retirement System and LEOFF Plan 1 to develop that estimate. The estimated number of duty-related disabilities for future legislation may differ from the estimates for HB 2418 depending on actual experience and the type of disability benefit that is proposed.

Policy Options

Option 1: Eliminate the actuarial reduction for a member's age

This approach would provide the member with their full earned pension in the event of a duty-related disability by eliminating the actuarial reduction based on the difference between the member's age at the time of disability and the normal retirement age. The duty disability standard would remain unchanged. This approach would not allow for favorable federal income tax treatment since the member's benefit is still based on years of service.

Example:

A law enforcement officer or firefighter who is age 43 with 15 years of service credit and an final average salary of \$45,000/year is totally incapacitated for continued employment. The member is eligible for a disability pension even though they do not meet the age and service requirements for normal retirement.

The member's base pension is equal to 2% of their final average salary multiplied by their years of service. In this case, $2\% \times \$45,000/\text{year} \times 15 =$ a base pension of \$13,500/year or \$1125/month. No actuarial reduction for early retirement would be applied so the member would receive the base pension amount less any optional reductions that may be selected by the retiree such as a survivor benefit or health care insurance.

A non-duty disability would continue to operate under current law. The member's base pension would be reduced by an actuarial factor determined by how far the member is from the age 53 normal retirement age. In this case, the member is ten years from normal retirement eligibility so the reduction factor is 0.43 and the member's base pension would be reduced to \$483.75/month.

Option 2: Establish a special benefit for extreme disabilities

This approach would create a higher disability standard and provide a correspondingly higher level of benefits. The primary policy underlying this type of approach is recognition of the fact that some disabled members may be incapable of substantial future employment in any capacity and therefore require a disability benefit that replaces future employment rather than supplements future employment. This approach may allow for favorable federal income tax treatment.

This approach requires a definition of the disability standard and the level of post-disability employment that would be permissible without affecting the disability pension.

Example One - Fire & Police Pension Association of Colorado:

Total Disability means the member 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 12 months. The benefit amount is 70% of base salary.

The member in the example on page one would receive \$2625/month under this model and the entire benefit would be tax-free.

Example Two – Federal Social Security:

Disability under Social Security is based on a person's inability to work. A person is only considered disabled under Social Security rules if they cannot do work that they did before

and if the Social Security Administration (SSA) decides that the person cannot adjust to other work because of their medical condition(s). The person's disability must also last or be expected to last for at least one year or to result in death.

The issue of defining "substantial employment" for federal social security disability benefits is dealt with by an earnings test. If a person is working in 2004 and their earnings average more than \$810 a month, they generally cannot be considered disabled by SSA. The permissible earnings amount is adjusted annually for inflation.

Example Three – Ohio Police & Fire:

Permanent & Total Disability means that a person is unable to perform either their official police & fire duties or the duties of any gainful occupation for which the person is reasonably fit by training, experience, and accomplishments, and there is no present indication of recovery. The annual benefit for a permanent and total disability is 72% of your average annual salary.

Example Four – Arkansas Local Police & Fire:

Duty Disability means the total and permanent injury or disease arose out of, and in the course of, the actual performance of the duties as a police officer or firefighter. In the event of a duty disability, the disability benefit awarded is 65% of Final Average Pay.

Example Five – Kentucky:

The legislative bodies of cities of the third and fourth classes may, in their discretion, pay unto any member of the police or fire departments, in case the member is disabled from an injury received while acting in their official capacity and in the line of duty to such an extent as they are unable to execute the duties of the member's official capacity or pursue a gainful occupation for which the member is fitted by training or experience, monthly compensation benefits equal to the member's monthly earnings at the time of their injury, so long as the disability continues, but in no event shall the total amount paid as compensation benefits to any member exceed the sum of five thousand dollars (\$5,000).

Option 3: Limit eligibility to emergency responders

The federal government provides certain death benefits to public safety officers who are killed or disabled while engaged in their authorized law enforcement, fire suppression, rescue squad, or ambulance duties. This federal benefit policy recognizes the special nature of the public service provided by emergency responders including law enforcement officers and firefighters by providing them with a higher level of duty-related death and disability benefits.

The Office of the State Actuary compared the disability rates for police and fire members to disability rates for public employees and assumed that the difference in rates was due to disabilities that resulted from responding to emergencies and training. They found that, in general, the police and fire rates were about ten times higher than the rates for public employees so the assumption would be that 90% of police and fire disabilities result from responding to emergencies and training.

Estimated Fiscal Impact

The Office of the State Actuary reviewed three proposed improvements for LEOFF Plan 2 duty-related disability benefits.

Option 1 would provide a disability retirement benefit equal to the accrued benefit, unreduced for early commencement, for duty-related disability, whether total or occupational. Option 1 would increase the contribution rate by 0.14% to 0.48% which results in a total employer cost increase for the biennium of \$1.6 to \$5.4 million and a 25-year total employer cost increase of \$44.8 to \$153.5 million. The impact on contribution rates would decrease if the benefit were limited to emergency responders to 0.12% to 0.42% which results in a total employer cost increase for the biennium of \$1.3 to \$4.7 million and a 25-year total employer cost increase of \$38.4 to 134.0 million. The number of expected disabilities per year ranged from 13-30 (reduced to 12-27 if limited to emergency responders).

Option 2 would provide a disability retirement benefit equal to 70% of pay, unreduced for early commencement, for duty-related total disability, using a strict definition of total disability as defined by the Social Security Administration. Option 2 would increase the contribution rate by 0.10% to 0.16% which results in a total employer cost increase for the biennium of \$1.1 to \$1.8 million and a 25-year total employer cost increase of \$31.8 to \$51.2 million. The impact on contribution rates would decrease if the benefit were limited to emergency responders to 0.06% to 0.14% which results in a total employer cost increase for the biennium of \$0.6 to \$1.6 million and a 25-year total employer cost increase of \$19.1 to \$44.8 million. The number of expected disabilities per year ranged from 3-6 (reduced to 3-5 if limited to emergency responders).

Option 3 would provide a disability retirement benefit equal to 50% of pay, unreduced for early commencement, for duty-related disability incurred while responding to an emergency, whether total or occupational. Option 3 would increase the contribution rate by 0.38% to 0.84% which results in a total employer cost increase for the biennium of \$4.3 to \$9.2 million and a 25-year total employer cost increase of \$121.8 to \$268.1 million. The number of expected disabilities per year ranged from 12-27.

Supporting Information

Appendix A

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.

(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, and shall have the allowance actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age fifty-three. An additional benefit shall not result in a total monthly benefit greater than that provided in subsection (1) of this section.

Appendix B

WAC 415-02-320

(5) **Table - Early retirement factors (ERF)** for these systems/plans: LEOFF Plan 2, WSP Plan 2, PERS Plan 1, TRS Plan 1, and WSP Plan 1 and 2 vested/terminated members:

Yrs Early	Month 0	Month 1	Month 2	Month 3	Month 4	Month 5	Month 6	Month 7	Month 8	Month 9	Month 10	Month 11
0	1.000	.9933	.9866	.9799	.9732	.9665	.9598	.9531	.9464	.9397	.9330	.9263
1	.9200	.9133	.9066	.8999	.8932	.8865	.8798	.8731	.8664	.8597	.8530	.8463
2	.8400	.8333	.8266	.8199	.8132	.8065	.7998	.7931	.7864	.7797	.7730	.7663
3	.7600	.7558	.7516	.7474	.7432	.7390	.7348	.7306	.7264	.7222	.7180	.7138
4	.7100	.7058	.7016	.6974	.6932	.6890	.6848	.6806	.6764	.6722	.6680	.6638
5	.6600	.6558	.6516	.6474	.6432	.6390	.6348	.6306	.6264	.6222	.6180	.6138
6	.6100	.6058	.6016	.5974	.5932	.5890	.5848	.5806	.5764	.5722	.5680	.5638
7	.5600	.5558	.5516	.5474	.5432	.5390	.5348	.5306	.5264	.5222	.5180	.5138
8	.5100	.5067	.5034	.5001	.4968	.4935	.4902	.4869	.4836	.4803	.4770	.4737
9	.4700	.4667	.4634	.4601	.4568	.4535	.4502	.4469	.4436	.4403	.4370	.4337
10	.4300	.4267	.4234	.4201	.4168	.4135	.4102	.4069	.4036	.4003	.3970	.3937
11	.3900	.3867	.3834	.3801	.3768	.3735	.3702	.3669	.3636	.3603	.3570	.3537
12	.3500	.3467	.3434	.3401	.3368	.3335	.3302	.3269	.3236	.3203	.3170	.3137
13	.3100	.3083	.3066	.3049	.3032	.3015	.2998	.2981	.2964	.2947	.2930	.2913
14	.2900	.2883	.2866	.2849	.2832	.2815	.2798	.2781	.2764	.2747	.2730	.2713
15	.2700	.2683	.2666	.2649	.2632	.2615	.2598	.2581	.2564	.2547	.2530	.2513
16	.2500	.2483	.2466	.2449	.2432	.2415	.2398	.2381	.2364	.2347	.2330	.2313
17	.2300	.2283	.2266	.2249	.2232	.2215	.2198	.2181	.2164	.2147	.2130	.2113
18	.2100	.2092	.2084	.2076	.2068	.2060	.2052	.2044	.2036	.2028	.2020	.2012
19	.2000	.1992	.1984	.1976	.1968	.1960	.1952	.1944	.1936	.1928	.1920	.1912
20	.1900	.1892	.1884	.1876	.1868	.1860	.1852	.1844	.1836	.1828	.1820	.1812
21	.1800	.1792	.1784	.1776	.1768	.1760	.1752	.1744	.1736	.1728	.1720	.1712
22	.1700	.1692	.1684	.1676	.1668	.1660	.1652	.1644	.1636	.1628	.1620	.1612
23	.1600	.1592	.1584	.1576	.1568	.1560	.1552	.1544	.1536	.1528	.1520	.1512
24	.1500	.1492	.1484	.1476	.1468	.1460	.1452	.1444	.1436	.1428	.1420	.1412
25	.1400	.1392	.1384	.1376	.1368	.1360	.1352	.1344	.1336	.1328	.1320	.1312
26	.1300	.1292	.1284	.1276	.1268	.1260	.1252	.1244	.1236	.1228	.1220	.1212
27	.1200	.1192	.1184	.1176	.1168	.1160	.1152	.1144	.1136	.1128	.1120	.1112
28	.1100	.1092	.1084	.1076	.1068	.1060	.1052	.1044	.1036	.1028	.1020	.1012
29	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
30	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
31	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
32	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
33	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
34	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
35	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
36	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
37	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
38	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
39	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000
40	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000	.1000

BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0219.1/05

ATTY/TYPIST: LL:seg

BRIEF DESCRIPTION: Receiving a disability allowance under the law enforcement officers' and fire fighters' retirement system, plan 2.

1 AN ACT Relating to receiving a disability allowance under the law
2 enforcement officers' and fire fighters' retirement system, plan 2;
3 amending RCW 41.26.470; and declaring an emergency.

4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

5 **Sec. 1.** RCW 41.26.470 and 2004 c 4 s 1 are each amended to read as
6 follows:

7 (1) A member of the retirement system who becomes totally
8 incapacitated for continued employment by an employer as determined by
9 the director shall be eligible to receive an allowance under the
10 provisions of RCW 41.26.410 through 41.26.550. Such member shall
11 receive a monthly disability allowance computed as provided for in RCW
12 41.26.420 and shall have such allowance actuarially reduced to reflect
13 the difference in the number of years between age at disability and the
14 attainment of age fifty-three, except under subsection (7) of this
15 section.

16 (2) Any member who receives an allowance under the provisions of
17 this section shall be subject to such comprehensive medical
18 examinations as required by the department. If such medical
19 examinations reveal that such a member has recovered from the

1 incapacitating disability and the member is no longer entitled to
2 benefits under Title 51 RCW, the retirement allowance shall be canceled
3 and the member shall be restored to duty in the same civil service
4 rank, if any, held by the member at the time of retirement or, if
5 unable to perform the duties of the rank, then, at the member's
6 request, in such other like or lesser rank as may be or become open and
7 available, the duties of which the member is then able to perform. In
8 no event shall a member previously drawing a disability allowance be
9 returned or be restored to duty at a salary or rate of pay less than
10 the current salary attached to the rank or position held by the member
11 at the date of the retirement for disability. If the department
12 determines that the member is able to return to service, the member is
13 entitled to notice and a hearing. Both the notice and the hearing
14 shall comply with the requirements of chapter 34.05 RCW, the
15 Administrative Procedure Act.

16 (3) Those members subject to this chapter who became disabled in
17 the line of duty on or after July 23, 1989, and who receive benefits
18 under RCW 41.04.500 through 41.04.530 or similar benefits under RCW
19 41.04.535 shall receive or continue to receive service credit subject
20 to the following:

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

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

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

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

30 (e) State contributions shall be as provided in RCW 41.45.060 and
31 41.45.067.

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

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

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

1 (4)(a) If the recipient of a monthly retirement allowance under
2 this section dies before the total of the retirement allowance paid to
3 the recipient equals the amount of the accumulated contributions at the
4 date of retirement, then the balance shall be paid to the member's
5 estate, or such person or persons, trust, or organization as the
6 recipient has nominated by written designation duly executed and filed
7 with the director, or, if there is no such designated person or persons
8 still living at the time of the recipient's death, then to the
9 surviving spouse, or, if there is neither such designated person or
10 persons still living at the time of his or her death nor a surviving
11 spouse, then to his or her legal representative.

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

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

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

32 (7)(a) A member who becomes disabled in the line of duty shall be
33 entitled to receive a minimum retirement allowance equal to ten percent
34 of such member's final average salary. The member shall additionally
35 receive a retirement allowance equal to two percent of such member's
36 average final salary for each year of service beyond five(~~(, and shall~~
37 ~~have the allowance actuarially reduced to reflect the difference in the~~
38 ~~number of years between age at disability and the attainment of age~~

1 ~~fifty-three~~)). An additional benefit shall not result in a total
2 monthly benefit greater than that provided in subsection (1) of this
3 section.

4 (b) A member who is totally disabled in the line of duty is
5 entitled to receive a retirement allowance equal to seventy percent of
6 such member's final average salary. A member shall be considered
7 totally disabled if he or she is unable to perform any substantial
8 gainful activity due to a physical or mental condition that may be
9 expected to result in death or that has lasted or is expected to last
10 at least twelve months. Substantial gainful activity is defined as
11 average earnings of no more than eight hundred ten dollars a month in
12 2004 adjusted annually for inflation as determined by the director.

13 NEW SECTION. **Sec. 2.** This act is necessary for the immediate
14 preservation of the public peace, health, or safety, or support of the
15 state government and its existing public institutions, and takes effect
16 immediately.

--- END ---

DRAFT FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/08/04	LEOFF 2 Disability

SUMMARY OF BILL:

This bill impacts the Law Enforcement Officer's and Fire Fighters Retirement System plan 2 (LEOFF 2) by eliminating the actuarial reduction for a member experiencing a duty disability and establishing a total disability benefit equal to 70 percent of a member's final average salary if they are disabled to the point where they cannot perform any substantial gainful activity. Substantial gainful activity is defined as average earnings of no more than \$810 per month in 2004, which shall be adjusted annually for inflation as determined by the director.

Effective Date: Immediately upon passage.

CURRENT SITUATION:

Currently, disabled LEOFF 2 members are entitled to receive a minimum retirement allowance equal to 10 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, and shall have the allowance actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age 53.

MEMBERS IMPACTED:

We estimate that all of the 14,560 active members of this system, as well as all future active members could be affected by this bill. For a typical member, currently about 40 years of age with 11 years of service, an annual salary of \$66,000, and final average salary of \$61,000, the increase in annual disability benefits are shown below:

Current disability provision = 2% of average final compensation per year of service, actuarially reduced from 53 to age 40 = $2\% \times \$61,000 \times 11 \times 0.3059 = \$4,105$ per year.

Proposed disability provision, non-duty related = 2% of average final compensation per year of service, actuarially reduced (same as current provision) = $2\% \times \$61,000 \times 11 \times 0.3059 = \$4,105$ per year.

Proposed disability provision, duty-related, occupational disability = 2% of average final compensation per year of service, no actuarial reduction = $2\% \times \$61,000 \times 11 = \$13,420$ per year.

Proposed disability provision, duty-related, total disability = 70% of average final compensation per year of service, no actuarial reduction = $70\% \times \$61,000 = \$42,700$ per year.

We expect that in the first year after the effective date, approximately 11 members would have duty-related total disabilities, and that about 48 members would have occupational duty-related disabilities.

ASSUMPTIONS:

The costs depend on our assumptions for the probability of disability and post-disablement mortality. This includes assumptions for total disability, occupational disability, and duty-related disability. We needed to increase our existing assumptions for rates of disability because currently members who become disabled may elect to receive terminated vested benefits or retirement benefits because the disability benefits are the actuarial equivalent of those benefits. The removal of the actuarial equivalent reduction factor or the availability of the tax-free 70% of pay benefit would change members' selection of benefits.

We changed our disability assumption to use rates based on the disability rates used by the Colorado Fire and Police Pension Association Death and Disability Fund for their January 1, 2004 valuation prepared by Mellon. We used 85% of the Colorado rates to reflect our assumption that 85% of disabilities are duty-related. We assume that 18% of all disabilities are total disabilities and 82% are occupational disabilities (the inability to continue working in law enforcement or firefighting).

Otherwise, we used the same assumptions as disclosed in the 2003 valuation report. We did not change our assumption for post-disablement mortality (although the mortality experience for those severely disabled would be expected to be less favorable than for those with occupational disabilities). Also, we did not include any waiting period for benefit commencement.

We used linear interpolation for the rates in between the following ages:

Age	Annual Rate of Disablement Per 1,000 Members
20	1.01
30	1.28
40	2.47
45	3.36
50	11.76
55	28.91

For example, for a 55 year old member, we used a rate of 85% of 18% of 0.0289, or 0.004423, for total disability and 85% of 82% of 0.0289, or 0.020150, for occupational.

We reduced our decrements from other causes such as termination and retirement to be consistent with the higher disability rates. The total number of expected members leaving the system each year remained the same. In other words, we shifted some members from the category of termination or retirement to disability.

We assumed that disability rates would continue past eligibility for early and normal retirement. We considered but did not include any liability for members who might choose a taxable retirement benefit based on long service such as greater than 40 years, over the 70% of pay tax-free disability benefit. In other words, because the 70% is tax-free, we assumed that members would choose to take this disability benefit instead of a greater retirement benefit that is taxable.

We changed the disability assumptions to determine the base liabilities first, then added the proposed disability benefits. With everything else being equal, using higher disability rates would reduce the plan liabilities, because the mortality experience of disabled pensioners is less favorable than the experience of healthy pensioners. The cost of the proposed benefit improvement is based on the difference in the liabilities after the assumption change.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

System: Law Enforcement Officers' and Firefighters' Plan 2			
<i>(Dollars in Millions)</i>	Current	Increase	Total
Actuarial Present Value of Projected Benefits (The Value of the Total Commitment to all Current Members)	\$4,382.92	\$93.69	\$4,476.61
Unfunded Actuarial Accrued Liability (The Portion of the Plan 1 Liability that is Amortized at 2024)	\$0.00	\$0.00	\$0.00
Unfunded Liability (PBO) (The Value of the Total Commitment to all Current Members Attributable to Past Service)	\$(546.57)	\$48.86	\$(497.71)
Increase in Contribution Rates: (Effective 09/01/2005)			
Employee	0.43%		
Employer	0.25%		
State	0.18%		

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

Costs (in Millions):	<u>LEOFF 2</u>
2005-2007	
State:	
General Fund	\$3.9
Non-General Fund	<u>0.0</u>
Total State	\$3.9
Local Government	\$5.5
Total Employer	\$9.4
Total Employee	\$9.4
2007-2009	
State:	
General Fund	\$4.7
Non-General Fund	<u>0.0</u>
Total State	\$4.7
Local Government	\$6.6
Total Employer	\$11.3
Total Employee	\$11.3
2005-2030	
State:	
General Fund	\$91.8
Non-General Fund	<u>0.0</u>
Total State	\$91.8
Local Government	\$133.3
Total Employer	\$225.1
Total Employee	\$225.1

STATEMENT OF DATA AND ASSUMPTIONS USED IN PREPARING THIS FISCAL NOTE:

The costs presented in this fiscal note are based on our understanding of the bill as well as generally accepted actuarial standards of practice including the following:

1. Costs were developed using the same membership data, methods, assets and assumptions as those used in preparing the September 30, 2003 actuarial valuation report of the Law Enforcement Officers' and Firefighters' Retirement System except for the disability rates disclosed in this fiscal note.
2. As with the costs developed in the actuarial valuation, the emerging costs of the System will vary from those presented in the valuation report or this fiscal note to the extent that actual experience differs from that projected by the actuarial assumptions.
3. Additional assumptions used to evaluate the cost impact of the bill which were not used or disclosed in this fiscal note or the actuarial valuation report include the following: None.
4. The analysis of this bill does not consider any other proposed changes to the system. The combined effect of several changes to the system could exceed the sum of each proposed change considered individually.
5. This fiscal note is intended for use only during the 2005 Legislative Session.
6. The funding method used for Plan 1 utilizes the Plan 2/3 employer/state rate as the Normal Cost and amortizes the remaining liability (UAAL) by the year 2024. Benefit increases to Plan 2/3 will change the UAAL in Plan 1. The cost of benefit increases to Plan 1 increases the UAAL.
7. Plan 2/3 utilizes the Aggregate Funding Method. The cost of Plan 2/3 is spread over the average working lifetime of the current active Plan 2/3 members.
8. The cost increases for the bill used to determine the increase in funding expenditures for future new entrants are 0.30% for LEOFF Plan 2 members and 0.30% for LEOFF Plan 2 employers, based on 50% of a total entry age normal cost increase of 0.60% for members and employers.

GLOSSARY OF ACTUARIAL TERMS:

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of Actuarial Assumptions (i.e. interest rate, rate of salary increases, mortality, etc.)

Projected Benefits: Pension benefit amounts which are expected to be paid in the future taking into account such items as the effect of advancement in age as well as past and anticipated future compensation and service credits.

Normal Cost: Computed differently under different funding methods, the normal cost generally represents the portion of the cost of projected benefits allocated to the current plan year.

Unfunded Actuarial Accrued Liability (UAAL): The cost of Plan 1 is divided into two pieces:

- The Normal Cost portion is paid over the working lifetime of the Plan 1 active members. The remaining cost is called the UAAL.
- The UAAL is paid for by employers as a percent of the salaries of all plan 1, 2 and 3 members until the year 2024.

Pension Benefit Obligation (PBO): The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date (past service).

Unfunded Liability (Unfunded PBO): The excess, if any, of the Pension Benefit Obligation over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.



WASHINGTON STATE LEGISLATURE
Office of the State Actuary

October 15, 2004

TO: Steve Nelsen, Executive Director
LEOFF 2 Retirement Board

FROM: Marty McCaulay, Associate Actuary
Office of the State Actuary

CC: Matt Smith, State Actuary
Office of the State Actuary

RE: **PROPOSED LEOFF 2 DISABILITY BENEFIT IMPROVEMENTS -
UPDATED**

We reviewed three proposed improvements for the LEOFF 2 disability benefits. Option 1 would provide a disability retirement benefit equal to the accrued benefit, unreduced for early commencement, for duty-related disability, whether total or occupational. Option 2 would provide a disability retirement benefit equal to 70% of pay, unreduced for early commencement, for duty-related total disability, using a strict definition of total disability as defined by the Social Security Administration.

Costs

The cost for Option 1 (removal of reduction factor, total or occupational) is a total increase in the contribution rate of 0.40% (0.20% member and 0.20% employer), a total employer cost increase for the 2005-07 biennium of \$4.5 million, and a 25-year total employer cost increase of \$127.8 million.

The cost for Option 2 (70% of pay, total disability only) is a total increase in the contribution rate of 0.16% (0.08% member and 0.08% employer), a total employer cost in the 2005-07 biennium of \$1.8 million, and a 25-year total employer cost increase of \$51.2 million.

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Assumptions

The costs depend on our assumptions for the probability of disability and post-disablement mortality. This includes assumptions for total disability, occupational disability, and duty-related disability. We needed to increase our existing assumptions for rates of disability because currently members who become disabled may elect to receive terminated vested benefits or retirement benefits because the disability benefits are the actuarial equivalent of those benefits. The removal of the actuarial equivalent factor would change members' selection of benefits.

We used disability rates used by Colorado Police and Fire. We assume that 85% of disabilities are duty related. We assume that 20% of all disabilities are total disabilities and 80% are occupational disabilities (the inability to continue working in law enforcement or firefighting). Otherwise we used the same assumptions as in the 2002 actuarial valuation report. We did not change our assumption for post-disablement mortality (although the mortality experience for those severely disabled would be expected to be less favorable than for those with occupational disabilities). Also, we did not include any waiting period for benefit commencement.

Option 1 – Removal of Reduction Factor

The Option 1 disabilities would be duty-related, but they could be total disabilities or occupational disabilities (the inability to perform one's occupation). The actual experience would depend on how the definition of disability is interpreted. We expect 31 of these disabilities for the current year. The cost increase for Option 1 is summarized below:

Option 1	
(Removal of reduction factor)	
Employee rate increase	0.20%
Employer rate increase	0.12%
State rate increase	0.08%
Total increase	0.40%

2005-2007 Biennium	
(\$ in millions)	
State General Fund	\$1.8
State Non-General Fund	\$0.0
Total State	\$1.8
Local Government	\$2.7
Employer Total	\$4.5
Employee	\$4.4

2005-2030 25 Years	
(\$ in millions)	
State General Fund	\$51.0
State Non-General Fund	\$0.0
Total State	\$51.0
Local Government	\$76.8
Employer Total	\$127.8
Employee	\$127.6

Option 2 – 70% of Pay

The benefit under Option 2 would be 70% of a one-year average pay, with the benefit continuing past normal retirement age. The Option 2 disabilities could be more severe than under Option 1. Disabilities would need to be total disabilities, and also duty-related. We expect 6 of these disabilities for the current year. The cost increase for Option 2 is summarized below:

Option 2	
(Removal of reduction factor)	
Employee rate increase	0.08%
Employer rate increase	0.05%
State rate increase	0.03%
Total increase	0.16%

2005-2007 Biennium	
(\$ in millions)	
State General Fund	\$0.7
State Non-General Fund	\$0.0
Total State	\$0.7
Local Government	\$1.1
Employer Total	\$1.8
Employee	\$1.8

2005-2030 25 Years	
(\$ in millions)	
State General Fund	\$19.1
State Non-General Fund	\$0.0
Total State	\$19.1
Local Government	\$32.1
Employer Total	\$51.2
Employee	\$51.0

OLIVER CONSULTING
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December 8, 2004

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

Re: Actuarial review of contribution rate impact of Duty Disability
Benefit improvements

Chairman Fox and Members of the Board:

There follow the results of our actuarial review of the LEOFF 2 contribution rate increases contained in the LEOFF 2 draft fiscal note of December 8, 2004 of the Office of the State Actuary.

Background

Currently, members "disabled in the line of duty" can elect to receive either 150% of their contribution account or an annuity equal to the member's accrued benefit actuarially reduced for early retirement, with a 10% of final average salary minimum. The benefit improvements currently being considered would remove the early retirement reduction for members disabled in the line of duty and, for those duty disablements found to be "totally disabled", would increase the annuity to 70% of final average salary.

The recommended contribution rate increases contained in the draft fiscal note of the Office of the State Actuary are shown below.

Employee	0.43%
Employer	0.25%
<u>State</u>	<u>0.18%</u>
Total	0.86%

In order to value this benefit, (1) assumptions as to incidences of disability were changed to reflect the design the new disability benefits and (2) mortality rates of those becoming disabled who previously took vested terminated benefits were changed from healthy to disabled mortality. The contribution rate increases shown above are based on these new assumptions.

Results of Review

Assumptions

Rates of disablement are based on experience of the Colorado Fire and Police Pension Association Death and Disability Fund, which provides benefits that are similar in design and administration to those being contemplated, and on the percentage of duty disablements under LEOFF 1 (85%). In addition, it has been assumed that, due to the favorable tax treatment afforded the 70% benefit, totally disabled members eligible for retirement will elect the 70% duty disability benefit rather than the service retirement benefit. We agree that these assumptions are reasonable for pricing this benefit.

Retroactive Provisions

As currently outlined, the improvement would not be retroactive. Should a retroactive provision be added, the contribution rate increases shown should be revised accordingly.

Contribution Rates

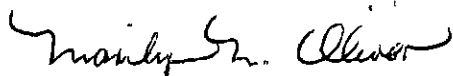
We independently calculated the increases in the LEOFF 2 Actuarial Present Value of Projected Benefits and the resulting contribution rate increases. Our results fell within a reasonable range of the State Actuary's results.

Conclusions

Contribution rates shown in the draft fiscal note of the Office of the State Actuary are appropriate for costing the contemplated benefit improvements.

The undersigned is a member of the American Academy of Actuaries and meets 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

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