Seattle City Employees' Retirement System
Board of Administration
Cecelia M. Carter, Executive Director

March 12, 2012

Sally J. Clark, President
Seattle City Council
600 Fifth Avenue, 2nd floor
Seattle, WA 98104

RE: Seattle City Employees' Retirement System – Disability Retirement Option(s)

Dear President Clark:

As I trust you are aware, the Seattle City Employees' Retirement System ("SCERS" or the "Plan") was created and is administered under the Seattle Municipal Code section 4.36. Within this section of the Code are provisions for types of retirement benefits a member may earn eligibility to receive (i.e., service retirement, disability retirement, and temporary disability retirement). The Board of Administration of SCERS is requesting a modification to the Code related to disability retirement and temporary disability retirement options.

Both disability retirement and temporary disability retirement are permitted to members of the Plan under the following conditions:

> "Any member may be retired for permanent and total disability, either ordinary or accidental, occurring while in City service and *not connected with any illness or disability existing prior to entering City service*, upon examination as hereinafter set forth, if such employee meets either of the following requirements: (1) The disability of such member arose out of and in the course of the his employment as an employee of the City, or (2) Such member had, at the time of occurrence of the such disability, at least ten (10) years of City service, over a period of not to exceed fifteen (15) years immediately preceding retirement…" [*SMC 4.36.220*] [*emphasis added*]

It is the conditional provision of "not connected with any illness or disability existing prior to entering City service" that the Board is requesting be modified to eliminate this restrictive provision.

The Board of Administration had reason to review this provision and finds the section(s) as written do not appear to be in alignment with the City's sentiment and intent towards its employees. The City has always proved itself to be a champion of equitable employment opportunities to all its citizens. The disability retirement provisions as written would stand as an obstacle for an employee entering City service, with any illness or disability, the right to be granted a disability retirement. This can prove problematic when an employee who clearly demonstrated the ability to perform his/her job duties upon entering City service then encounters a change in condition and subsequently finds himself unable to perform his/her job duties. So long as all other conditions have been met; membership in SCERS and at least ten years of service, etc., the Board questions whether the *pre-existing condition* is consistent with the intent of the City in its relationship with its employees.

Example –

An employee is hired into the City and performs his/her job duties for over twelve years. This employee suddenly falls ill and is no longer able to perform his/her job duties. The inability to perform his/her duties is attributable to a recurrence of an illness which had been in remission years prior to beginning City service.

Under current language of the SMC, the Board would be precluded from granting a disability retirement to this employee and the employee would be left with one of two options: (a) leave his/her employee contributions in the Plan until such time as the employee were of an age to be eligible for a regular service retirement; or (2) take a lump sum distribution of his/her employee contributions (plus interest) and forfeit any future retirement benefit from the Plan.

A disability retirement is calculated based on 1.5% of a member's Final Compensation and generally results in a monthly retirement benefit equal to 33% of Final Compensation. The retirement payment options available to a member retiring under a disability are limited – however do provide for a member's spouse or domestic partner.

Associated Cost –

Milliman (actuaries to SCERS) was asked to give an estimate on the cost associated with eliminating the pre-existing condition language from the SMC. Based on SCERS January 1, 2011 Valuation Report, Milliman estimates the cost impact of one additional disability retirement would result in a 1 basis point increase to Normal Cost and thus the Total 30-year Funding Rate (see attached). The chart below is intended to explain the associated cost.

($ Millions)	Current Provisions*	Revised Disability Eligibility	Estimated Cost of Change
Funded Status of SCERS as of January 1, 2011			
Actuarial Accrued Liability	$ 2,709.0	$ 2,709.1	$ 0.1
Actuarial Value of Assets	2,013.7	2,013.7	-
Unfunded Actuarial Accrued Liability	$ 695.4	$ 695.5	$ 0.1
Funded Ratio	74.3%	74.3%	0.0%
30-Year Funding Rate			
Normal Cost	15.19%	15.20%	0.01%
Unfunded Actuarial Accrued Liability	6.11%	6.11%	0.00%
Total 30-Year Funding Rate	21.30%	21.31%	0.01%

**Rates shown are based on the January 1, 2011 actuarial valuation, and do not reflect the change to the member crediting rate adopted after the valuation.*

Next Steps –

The Board of Administration voted on this matter at its March 8, 2012 Board meeting and directed me to send you this letter requesting a modification of the Code.

The City Budget Office will also be notified of this request as this change will have an impact on the City's budget. As indicated above however, the change will have a negligible effect.

On behalf of the Board of Administration, I ask for your support in modifying the Seattle Municipal Code to provide the ability for all City employees who are members of SCERS the opportunity to access a retirement benefit when warranted, regardless of any pre-existing illness or disability they may have had when entering City service.

Your support is greatly appreciated and I thank you in advance for all consideration given to this request.

Very truly yours,

Cecelia M. Carter
Executive Director

Attachment

cc: SCERS Board of Administration

Milliman

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February 3, 2012

Ms. Cecelia Carter
Executive Director
Seattle City Employees' Retirement System
720 Third Ave., Suite 1000
Seattle, WA 98104

Re: Disability Retirement Eligibility Cost Study

Dear Cecelia:

Under certain conditions, monthly benefits are payable to disabled members of the Seattle City Employees' Retirement System (SCERS). To be eligible for this benefit, the member must have at least 10 years of service (or the disability must have occurred in the course of City employment) and the condition must not have existed prior to entrance into service with the City. It is our understanding that consideration is being given to removing the pre-existing condition exclusion. The purpose of this letter is to discuss the actuarial impact, per your request.

Variability

Any actuarial cost estimate is based on a number of assumptions which can have a significant impact on the results. This is particularly true in this case, as we have no experience on which to base some of our assumptions. In particular, we have no way of knowing how many additional disability retirements will occur due to this change. The actual cost will vary significantly depending on the actual number of additional disability retirements that may occur due to this proposed change.

Since we have no credible way of estimating the increase in disabilities due to the proposed change, we have not attempted to make any assumption with regard to this. To give some estimate of the potential cost, we have shown the cost impact if there was an increase in non-duty disability retirements of one per year. Note that under the current assumptions, approximately two disability retirements (not duty related) are assumed to occur each year.

Findings

The following chart shows the estimated cost impact of one additional disability retirement each year. The results shown are based on the actuarial valuation as of January 1, 2011.

($ Millions)		Current Provisions*		Revised Disability Eligibility		Estimated Cost of Change
Funded Status of SCERS as of January 1, 2011						
Actuarial Accrued Liability	$	2,709.0	$	2,709.1	$	0.1
Actuarial Value of Assets		2,013.7		2,013.7		-
Unfunded Actuarial Accrued Liability	$	695.4	$	695.5	$	0.1
Funded Ratio		74.3%		74.3%		0.0%
30-Year Funding Rate						
Normal Cost		15.19%		15.20%		0.01%
Unfunded Actuarial Accrued Liability		6.11%		6.11%		0.00%
Total 30-Year Funding Rate		21.30%		21.31%		0.01%

**Rates shown are based on the January 1, 2011 actuarial valuation, and do not reflect the change to the member crediting rate adopted after the valuation.*

The above chart shows the estimated increase in costs if the revised eligibility requirements for disability retirement were adopted, and it caused one additional person to take a non-duty disability retirement each year. For example, the increase in the ongoing annual cost (normal cost) plus the amount required to finance the increase in the unfunded actuarial accrued liability (UAAL) over a 30-year period is estimated to be an additional 0.01% of payroll. We have used 30 years as it is the period the Board ordinarily uses to measure funding sufficiency.

As previously noted, the estimated costs are based on one additional disability retirement per year. Therefore, if there were two additional disability retirements per year, the estimated cost increase would double. Similarly, if only one additional disability retirement occurred every two years, the estimated increase in costs would be half of the value shown above.

All values shown are based on the January 1, 2011 actuarial valuation and therefore only partially reflect the impact of the market decline that occurred in the fiscal year ended in 2008. Deferred losses will be recognized in the Actuarial Value of Assets in upcoming years. If the full impact of the decline were reflected in the exhibit, the Funded Ratio shown in the chart would decrease materially. However, the relative cost of the proposed change would not be affected.

Additional Comments

Based on the 2011 valuation and these actuarial calculations, it does not appear that the adoption of this change would materially affect the System's funded status. However, SCERS is currently projected to need increases in contribution rates in order to amortize its UAAL in the future. The Board should take this into consideration as they contemplate whether to adopt the proposed revision to the current disability retirement provisions.

Assumptions and Methods

All data, methods and assumptions are the same as those used in our January 1, 2011 actuarial valuation of SCERS, except for the adjustment for the change in the disability retirement eligibility. Please refer to that report for further details.

To reflect an increase of approximately one disability per year, we have increased the non-duty disability rates as follows:

Non-Duty Related Disability Rates*

	Male and Female	
Age	Current Provisions	Adjusted Assumptions
20	.00 %	.00 %
25	.00	.00
30	.03	.04
35	.03	.04
40	.03	.05
45	.03	.05
50	.05	.08
55	.05	.08
60	.05	.08
65	.00	.00

**Non-duty disability rates under current provisions are equal to 2/3rd of the total disability rates, as shown in Appendix A of the January 1, 2011 valuation report.*

It should be noted that we have not made any other changes in the demographic assumptions, as it is difficult to anticipate how plan changes will impact participant behavior, but changes in behavior could result.

Actuarial Certification

The cost estimates shown in this letter reflect the data, methods and assumptions used for the January 1, 2011 actuarial valuation. These cost estimates are subject to the uncertainties of a regular actuarial valuation; the costs are inexact because they are based on assumptions that are themselves necessarily inexact, even though we consider them reasonable. Thus, the emerging costs may vary from those presented in this letter to the extent actual experience differs from that projected by the actuarial assumptions.

The cost estimates presented in this letter are based on the January 1, 2011 actuarial valuation report. In preparing that report, we relied without audit on information (some oral and some in writing) supplied by SCERS' staff. This information includes, but is not limited to, statutory provisions, employee data, and financial information. We used SCERS' benefit provisions as stated in our January 1, 2011 Actuarial Valuation report. Note that this means we did not reflect the adjustment to the interest crediting rate that occurred subsequent to the valuation. In our examination, after discussion with SCERS and certain adjustments, we have found the data to be reasonably consistent and comparable with data used for other purposes. Since the valuation results, as well as the estimates shown in this letter, are dependent on the integrity of the data supplied, the results can be expected to differ if the underlying data is incomplete or missing. It should be noted that if any data or other information is inaccurate or incomplete, our determinations might need to be revised.

The emerging costs will vary from those presented in this letter to the extent that actual experience differs from that projected by the actuarial assumptions. Future actuarial measurements may differ significantly from the current measurements presented in this letter due to a number of factors. Due to the scope of this assignment, we did not perform an analysis of the potential range of such measurements. Actuarial computations presented in this letter are for purposes of studying the cost impact of changing disability eligibility. Determinations for other purposes may be significantly different from the results contained in this letter.

Milliman's work is prepared solely for the internal business use of SCERS. To the extent that Milliman's work is not subject to disclosure under applicable public records laws, Milliman's work may not be provided to third parties without Milliman's prior written consent. Milliman does not intend to benefit or create a legal duty to any third party recipient of its work product. Milliman's consent to release its work product to any third party may be conditioned on the third party signing a Release, subject to the following exceptions:

(a) The System may provide a copy of Milliman's work, in its entirety, to the System's professional service advisors who are subject to a duty of confidentiality and who agree to not use Milliman's work for any purpose other than to benefit the System.

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No third party recipient of Milliman's work product should rely upon Milliman's work product. Such recipients should engage qualified professionals for advice appropriate to their own specific needs.

The consultants who worked on this assignment are pension actuaries. Milliman's advice is not intended to be a substitute for qualified legal or accounting counsel.

On the basis of the foregoing, we hereby certify that, to the best of our knowledge and belief, this letter is complete and accurate and has been prepared in accordance with generally recognized and accepted actuarial principles and practices.

I, Nick Collier, am a member of the American Academy of Actuaries and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Respectfully submitted,

Nick Collier

Nick J. Collier, ASA, EA, MAAA
Consulting Actuary
NJC/nlo