

NO. 47337-2-II

**COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON**

TIM LENANDER,

Appellant,

v.

WASHINGTON DEPARTMENT OF RETIREMENT SYSTEMS,

Respondent.

**BRIEF OF RESPONDENT
WASHINGTON DEPARTMENT OF RETIREMENT SYSTEMS**

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I. INTRODUCTION

The Washington State Patrol Retirement System (WSPRS) is one of the State's public retirement systems. Historically, married members of WSPRS could receive their retirement benefit in only one form, Option A. That changed in July 2000, with the passage of legislation allowing married members of WSPRS the choice to receive retirement benefits in one of two forms, Option A or Option B. The Legislature required that the two forms of the retirement benefit have equal value (to the member and spouse over their joint lifetimes) and therefore equal cost to the system. Put differently, the Legislature required that the two forms be "actuarially equivalent."

To ensure that Options A and B would have equal value, the Legislature required that the member's monthly allowance for Option B (i) would begin at an amount lower than Option A, but (ii) would increase more uniformly than Option A during the joint lifetimes of member and spouse. Accordingly, when Option B was adopted, the then-State Actuary recommended and the Department of Retirement Systems adopted in rule a 3% reduction factor to achieve actuarial equivalence between Options A and B.

Because many of the variables affecting actuarial equivalence are based on changing economic and demographic conditions, the factors used

to ensure actuarial equivalence between benefit alternatives (in all the Washington public retirement systems) must be updated regularly to maintain that equivalence. Washington statute (RCW 41.45) recognizes this and provides for the updating of these actuarial factors on a six-year cycle. In 2010, on the established statutory cycle, the State Actuary recommended and the Department adopted updated factors to provide continuing equivalence between WSPRS Options A and B.

In 2011, Mr. Lenander retired from WSPRS and chose Option B—after the updated factors had become effective. Under the updated factors, his Option B benefit started 5.3% lower than an Option A benefit would have started. This reduction ensured that his Option B benefit would be of equal value to the amount he and his spouse would have received over their joint lifetimes had he chosen Option A.

In this proceeding, Mr. Lenander seeks an Option B benefit of greater value than Option A. He objects to the 2010 factors on the bases that their adoption exceeded the Department's statutory authority and unconstitutionally impaired his benefit. His argument regarding the Department's statutory authority fails to recognize RCW 41.45, setting the modern requirements for the State Actuary's role in the adoption of actuarial factors, and fails to harmonize a RCW 43.43.120 (a 1951 WSPRS statute from a former actuarial regime) with these requirements.

His constitutional arguments fail to establish that he had a contractual right to anything more than the actuarially equivalent Option B benefit he is presently receiving. He has suffered no impairment of a contractual right.

The Department asks this Court to affirm the superior court, upholding the challenged rules that establish amended Option B factors, both on their face and as applied to Mr. Lenander. This will ensure that WSPRS members are treated equally, whether they choose Option A or Option B; and will uphold the complete actuarial system in RCW 41.45, the provisions of which are meticulously integrated to ensure that the State's public retirement systems, including WSPRS, will be adequately funded.

II. COUNTERSTATEMENT OF THE ISSUES

1. Under RCW 43.43.278 (requiring the Department to adopt actuarially equivalent retirement options) and RCW 41.45.090 (requiring the amendment of actuarial factors on a six-year cycle), was the amendment of WACs 415-103-215 and 415-02-380 (updating the factors necessary to achieve actuarial equivalence between WSPRS Options A and B) within the Department's statutory authority?

2. Where Mr. Lenander had no contractual right to the use of a 3% reduction factor in the calculation of his Option B benefit, was the

amendment of WACs 415-103-215 and 415-02-380 constitutionally valid under article I, section 23 of the Washington Constitution as applied to Mr. Lenander?

3. Where DRS is not Mr. Lenander's employer; where Mr. Lenander has not "substantially prevailed;" and where Mr. Lenander did not request common fund fees in his Petition for Review, should this Court deny attorneys' fees under RCW 49.48.030, RCW 4.84.340-.350, and the common fund doctrine?

III. STATEMENT OF THE CASE

A. Proper Funding of the Public Retirement Systems Relies on Solid Actuarial Analysis

Understanding the issues raised in this case requires background regarding the separate actuarial schemes that supported the State's public retirement systems prior to 1989 and the modern actuarial scheme promulgated in 1989 to consolidate the prior schemes under one statutory framework. The fundamental premise is that the Washington public retirement systems must be able to pay benefits to their members when those benefits become due. To ensure adequate funding to pay these future liabilities, adequate contributions must be paid into the system during the working lives of their members. The primary role of an actuary is to determine the level of contributions that will provide for the proper operation of the system through adequate funding. RCW 41.45.010.

1. Since Its Inception, Expert Actuarial Analysis Has Been Fundamental to the Proper Operation of WSPRS

Many of the State's retirement systems, including WSPRS, date back to the 1940s or before. These systems were created by statute and governed by statutorily created retirement boards. Each board was required to retain a private actuary to make recommendations to the board and governor regarding the contribution rates necessary to ensure adequate funding. Rem. Supp. 1949 § 10726o (CP 675). To support these recommendations, once every five years, the actuary was required to make an actuarial investigation into the demographic experience of the members and beneficiaries of each retirement system (including mortality, service, and compensation); and to complete an actuarial valuation of the assets, liabilities, and overall financial condition of the system. In turn, Rem. Supp. Title 73-1 required each board to collect the data necessary for these studies and provide that data to the actuary. Rem. Supp. 1949 § 10726n (CP 674-75). The analysis of these actuaries depended on demographic information regarding members and economic information regarding the investment performance of the retirement fund.

On this five-year cycle, the boards were required to “adopt such tables, schedules, factors, and regulations as [were] deemed necessary in the light of the findings of the actuary for the proper operation of the

retirement system” Rem. Supp. 1949 § 10726n (CP 673-75).

Consistent with this general statutory framework, WSPRS’ statute required its governing board to retain and provide data to a competent actuary to make the foregoing actuarial investigations. The actuary would report to the board and to make “such recommendations as he shall deem advisable for the . . . proper operation of the [WSPRS] Retirement Fund.” Rem. Supp. 1947 § 6362-89 (CP 676-86). By 1951, the Legislature allowed WSPRS members to receive their benefit in three alternate forms, each required to be “actuarially equivalent” (i.e., of equal value) one to another. Former RCW 43.43.250, .270 (1951) (Laws of 1951, ch. 140, §§ 4, 6). The factors needed to achieve this equivalence were among those tables, factors, and schedules recommended by its actuary after necessary input, including input regarding the mortality of WSPRS members and the investment return (interest rate) of the WSPRS fund. Former RCW 43.43.120(15) (1951) (Laws of 1951, ch. 140, § 1) (defining “actuarial equivalent” as “a benefit of equal value when computed upon the basis of such mortality table as may be adopted and such interest rate as may be determined by the board”).

2. To Improve the Operation of and Actuarial Support for the Retirement Systems, the Work of the Separate Boards and Private Actuaries Was Consolidated

As the retirement systems grew and their administration became

increasingly complex, the Legislature began to consolidate the work of the individual retirement boards and private actuaries to provide institutional expertise. In 1976, the Department of Retirement Systems was created in RCW 41.50, and the powers, duties, and functions of the various retirement boards, including the WSPRS Board, were transferred to it. RCW 41.50.030. The Office of the State Actuary was created in RCW 44.44 to perform all actuarial services for the Department, including all studies required by law. RCW 44.44.040; RCW 41.50.090(1).

In 1989, RCW 41.45 was enacted to improve the actuarial service to all the State's retirement systems and "provide a dependable and systematic process for funding the benefits provided to [their] members" RCW 41.45.010. *See generally* RCW 41.45, Actuarial Funding of State Retirement Systems. The actuarial services previously performed by private actuaries periodically retained by the individual boards were centralized in the Office of the State Actuary. RCW 44.44.010. Laws of 1989, ch. 273, § 1 (*codified as* RCW 41.45.010). The provisions governing the actuarial services provided to individual boards were repealed. Laws of 1989, ch. 273, §§ 29-30.

Using the comprehensive system created in RCW 41.45, the State Actuary makes recommendations regarding the contribution rates (both

employee and employer) that are required to ensure that the retirement systems will be able to meet their future liabilities. RCW 41.45.050, .060, .061, .0631. To this end, RCW 41.45 sets out a detailed framework through which contribution rates are updated every two years to adjust for changing economic and demographic conditions and ensure that the retirement systems remain adequately funded. RCW 41.45.060. CAR1 277.¹

Relevant economic conditions include, for example, changes in inflation; changes in the salaries of public employees; and the investment rate of return (or interest rate) on the pension funds. Unlike the prior actuarial schemes in which the boards were required to provide this information to the actuary, the values for these long-term economic assumptions are now set in statute. RCW 41.45.035. Every second year the State Actuary reviews the statutory economic assumptions and makes recommendations to a Pension Funding Council regarding potential changes.² RCW 41.45.030. The Pension Funding Council may adopt changes in these economic assumptions, subject to revision by the Legislature. RCW 41.45.060(2). Unless and until changed, the statutory assumptions “shall” be used by the State Actuary in all actuarial work

¹ CAR1 will refer to the Certified Administrative Record in Cause No. 10-2-01949-6. CAR2 will refer to the record in Cause No. 13-2-02465-6.

² The Pension Funding Council includes the Department Director. RCW 41.45.100.

performed for the State's public retirement systems: in setting contribution rates; in "conducting all actuarial studies of the state retirement systems"; and "for the administration of benefits under the [State's] retirement plans" RCW 41.45.030(3).³

In addition to these statutory economic assumptions, actuarial calculations require demographic data. RCW 41.45.090 establishes a process for the collection of this data, similar to that required of the predecessor boards. Instead of the boards, the Department collects the relevant demographic data, including without limitation, mortality, service, and compensation. RCW 41.45.090. Once every six years, the Department provides the collected data to the State Actuary to conduct an actuarial experience study of the members and beneficiaries of each state retirement system, and a study into the financial condition of each system.

Id.

On this six-year cycle, based on the foregoing actuarial studies and investigation, the Actuary is required to review the existing actuarial tables, schedules, and factors to determine whether changes are necessary for the proper operation and adequate funding of the retirement systems.

³ The statutory process is consistent with the modern Actuarial Standards of Practice (ASOP) No. 27, "Selection of Economic Assumptions for Measuring Pension Obligations." As a member of the American Academy of Actuaries, the State Actuary is bound by ASOPs. ASOP No. 1. See <http://www.actuarialstandardsboard.org/asops.asp> (last visited Sept. 8, 2015).

In turn, the Department is required to “adopt such tables, schedules, factors, and regulations as are deemed necessary in the light of the findings of the actuary for the proper operation of the state retirement systems.” RCW 41.45.090. Accurate tables, schedules, and factors ensure that alternate benefit forms provided by the systems are actuarially equivalent, i.e., have equal value and equal cost. *See generally* RCW 41.45. Decisions regarding the adequate funding and proper operation of the system are predicated on the understanding that alternate benefit forms indeed have equal cost to the system.

Although most of the statutes governing the prior boards and private actuaries were repealed in 1989, a few provisions remained in the chapters governing individual retirement systems, including RCW 43.43.120, the 1951 statute defining actuarial equivalence in WSPRS.⁴

3. As Required by RCW 41.45, the Department Adopts the Tables, Schedules, and Factors Recommended by the State Actuary in Rule

As required by RCW 41.45, the Department adopts the tables, schedules, and factors recommended by the State Actuary in WAC 415-02. Consistent with the six-year statutory cycle, WAC 415-02-300(3) provides that these factors “may be amended from time to time,

⁴ Mr. Lenander relies heavily on this statute in this proceeding.

based upon subsequent actuarial investigations” (but that they will be in effect until any such subsequent amendment). The proper operation of the retirement systems with adequate funding depends on the Department’s adoption of and use of these actuarial factors in its administration of benefits. RCW 41.45.090; *see generally* RCW 41.45.

B. Until 1999, the WSPRS Core Retirement Benefit Required a “Cutback” for Surviving Spouse Benefits

Since at least 1947, WSPRS has existed to provide retirement benefits to members of the Washington State Patrol. Historically, WSPRS members had no choice in the form of the benefit they received. In general, members received a monthly service retirement allowance based on a formula that considered the member’s years of service and compensation at the time of retirement. After retirement, the retiree’s monthly allowance increased by 2% each year. RCW 43.43.260.

If the WSPRS member was married at the time of retirement, the statute provided a separate benefit for the retired member’s spouse: specifically, if the retired member predeceased his/her spouse, the spouse would continue to receive a monthly allowance for life. In most cases, the amount of the surviving spouse’s monthly allowance was reduced from the allowance the retiree was receiving at the time of death. And the spouse’s reduced allowance remained constant for the remainder of his/her lifetime

(no annual 2% increases). In 1999, this spousal “cutback method” was altered slightly: although the cutback remained in place, an annual increase (less favorable than the retiree’s own annual increase) was made available to the surviving spouse. Laws of 1999, ch. 74, § 2 (*codified as* RCW 43.43.272) (CP 690).⁵

C. In 1999, the Legislature Provided an Alternative Form of Payment for the WSPRS Core “Cutback” Benefit

The “cutback method” for surviving spouse benefits generated some dissatisfaction among members, and in 1999 the Legislature provided an alternative form of payment of the core cutback benefit.⁶ RCW 43.43.278. From that point forward, the historical cutback method was labeled Option A, and the new alternative was labeled Option B. At retirement, a married WSPRS member was required to choose between Options A and B.

Option B eliminated the potential cutback for the surviving spouse. Instead, if the member predeceased his/her spouse, the spouse’s monthly benefit would continue at the level the member was receiving at the time of death. In addition, the surviving spouse would receive the same 2% annual increase that the member had previously received.

⁵ As Mr. Lenander indicates, the Legislature reserved the right to repeal the spousal annual increase. Appellant’s Op. Br. at 10-11. This reservation has no relevance to the outcome of this proceeding, as explained below.

⁶ Final B. Rep., SSB 5030 (Wash. 1999).

However, to ensure that the new Option B would be fair to members and not burden WSPRS with additional costs, the Legislature also provided that the member's initial benefit (calculated at the time of retirement) would be reduced. As a result of this initial reduction in the member's core benefit, the total amount paid out over the joint lifetimes of member and spouse would be equivalent, regardless whether the member chose Option A or the new Option B. *See* CP 690.

D. A Three Percent Reduction Initially Provided Actuarial Equivalence for Option B

The 1999 legislation creating Option B delegated to the Department the obligation to set the precise reduction to make Option B actuarially equivalent to Option A:

By July 1, 2000, the department of retirement systems shall adopt rules that allow a member to select an *actuarially equivalent* retirement option [i.e., equivalent to Option A] that pays the member a reduced retirement allowance and upon death shall be continued throughout the life of a lawful surviving spouse [Option B].

Laws of 1999, ch. 74, § 4 (*codified as* former RCW 43.43.278 (2000)) (emphasis added). An "actuarially equivalent" option was an option of "equal value," computed using actuarial science. RCW 43.43.120(1) (formerly RCW 43.43.120(15) (1951)).

Consistent with statutory requirements that actuarial services required by the Department be performed by the State Actuary, the former

State Actuary determined that a 3% reduction produced actuarial equivalence at that time. That is, if a WSPRS retiree chose Option B and the retiree's initial benefit was reduced from the Option A amount by 3%, the amount received by member and spouse over their joint lifetimes would be of "equal value" to the amount they would have received with Option A. CAR1 83.

E. The Department Promulgated Rules to Implement Option B

As required by RCW 43.43.278, the Department in 2000 adopted the recommended 3% reduction as the reduction then necessary to allow members to select "an actuarially equivalent retirement option" (i.e., Option B). CAR1 84-88.

Retirement benefit options. RCW 43.43.278 requires the department to provide retiring members with an *actuarially equivalent retirement option* by July 1, 2000. . . . When retiring for service, the married member can select either the historic retirement option under RCW 43.43.270 (Option A) or the *actuarially equivalent retirement option* (Option B). . . .

(1) *Option A (historic retirement option and survivor benefit).* The department pays the retiree a monthly retirement allowance in accordance with RCW 43.43.260. The department pays survivor benefits in accordance with RCW 43.43.270. . . .

(2) *Option B (actuarially equivalent retirement option and survivor benefit).* The department pays the retiree a monthly retirement benefit that is *actuarially reduced by three percent* to offset the cost of the survivor feature.

Former WAC 415-103-215 (2001) (emphasis added).

The following year, Options A and B both changed. Laws of 2001, ch. 329, §§ 4, 9. Option A still had a cutback feature; Option B still required an initial actuarial reduction in the member's calculated allowance in lieu of the cutback. However, the automatic annual increases (then available to retirees and spouses under both Options A and B) were amended to become true cost-of-living adjustments, fluctuating up or down with changes in the consumer price index. Consistent with the existing statutory scheme for updating actuarial factors on a six-year cycle, the 3% actuarial factor was not immediately adjusted to reflect these changes. *See* RCW 41.45.090.

F. In 2008 and 2009, a Project Team From the Department Worked With the State Actuary to Develop Amended Actuarial Factors

Pursuant to the six-year cycle established in RCW 41.45.090, in late 2008 a new State Actuary filed the 2001-2006 Actuarial Experience Study and initiated a review of the actuarial tables, schedules, and factors used in the administration of retirement benefits. CAR1 243-45. The factor used to reduce WSPRS Option A to produce an actuarially equivalent Option B was one of the factors included in this review. Before making a final recommendation regarding the Option B factor, the State Actuary sought the Department's input regarding the mortality table to be used in calculating the new factors, recommending one from a range of

options. CAR1 243, 246. The Actuary recognized that the choice of mortality tables from among these options was a policy decision delegated to the Department by statute (RCW 43.43.120). CAR1 252. In response to the request for input, the Department instructed the Actuary to use the mortality table he had recommended. CAR1 246-49, 257, 265-66.

The State Actuary further indicated that better actuarial equivalence could be obtained by developing different reduction factors for different subgroups of WSPRS retirees (rather than taking the “average” of these subgroups to produce a single reduction factor applicable to all retirees).⁷ CAR1 250, 260. For consistency with the other public retirement plans, the Actuary and the Department decided that the subgroups would be based on the difference between the member’s and spouse’s ages.

Using the foregoing policy input from the Department, the State Actuary made a final recommendation to the Department for Option B factors that would “provide better actuarial equivalence” than the prior 3% reduction factor. CAR1 265. The recommended factors were based on the changed nature of Option A and B benefits;⁸ updated economic

⁷ The Actuary indicated that use of a single factor (such as had been used before) tended to produce only a “crude approximation” of actuarial equivalence. CAR1 271.

⁸ The initial 3% reduction factor had never been recalculated to accommodate the effect of the 2001 statutory changes in the cost-of-living adjustments for both Option A and Option B.

assumptions (including the statutory 8% interest rate); updated demographic assumptions from the most recent actuarial experience study; policy decisions by the Department regarding the mortality table; and an improved actuarial methodology appropriate for the valuation of the Option A benefit. CAR1 264, 271. The Actuary's recommendation was presented in the form of a complete "actuarial communication," certifying that "[a]ll of the data, assumptions, and methods . . . used in developing the administrative factors [were] reasonable and appropriate" for the project.⁹ CAR1 265.

G. In 2010, the Department Adopted the State Actuary's Recommended Factors and Amended the Rules that Mr. Lenander Now Challenges

In July 2010, the Department adopted the factors recommended by the State Actuary by amending WAC 415-103-215 and WAC 415-02-380 (hereinafter, the Option B Equivalence Rules). Amended WAC 415-103-215 provided:

Option B (actuarially equivalent retirement option and survivor benefit). The department pays the retiree a monthly retirement benefit that is actuarially reduced by three percent to offset the cost of the survivor feature from the benefit calculated under Option A. ~~---~~ The department pays survivor benefits in accordance with RCW 43.43.278 using actuarial factors in WAC 415-02-380(10) and (11).

Former WAC 415-103-215 (2011) (strike-through and underlining added

⁹ Through an "actuarial communication," a term of art governed by rigorous standards set out in ASOP No. 41, an actuary takes responsibility for his/her work.

to show changes from 2000 version). The tables of actuarial factors themselves, recommended by the Actuary and “deemed necessary . . . for the proper operation of the state retirement systems,” were codified at former WAC 415-02-380(10) and (11) (2011). *See* RCW 41.45.090.

H. The Superior Court Upheld the Department’s 2010 Rule Amendments Updating the Actuarial Factors Necessary to Maintain Equivalence Between WSPRS Options A and B

Mr. Lenander sought judicial review of the 2010 amendments to the Option B Equivalence Rules, claiming that the amended rules exceeded the Department’s statutory authority (Cause No. 10-2-01949-6) and that the amended rules were unconstitutional as applied to him (Cause No. 13-2-02465-6). In January 2014 the two proceedings were consolidated under Cause No. 10-2-01949-6. CP 597-99. In an oral ruling on March 13, 2015, the Thurston County Superior Court rejected both of Mr. Lenander’s claims.¹⁰

First, with regard to the Department’s authority, the superior court held that the Department had authority to adopt the initial Option B factor in 2000 and continues to have authority to amend Option B factors periodically to maintain actuarial equivalence between Options A and B. Verbatim Report of Proceedings (VRP) (March 13, 2015) at 15. The court

¹⁰ Mr. Lenander’s detailed description of the procedural history of this case is not relevant to the issues raised before this Court on judicial review. *See* Appellant’s Op. Br. at 4-8.

rejected Mr. Lenander’s argument that the Department could amend the Option B factor only when mortality and interest rates changed, without regard to ensuring that Options A and B remained of “equal value” pursuant to RCW 43.43.120(1). VRP at 15-16.

Second, the court rejected Mr. Lenander’s constitutional claim. The court found that at most Mr. Lenander had a right to receive the core benefit (Option A) and, potentially, a right to receive value equal to Option A through an alternative “approach to the payout.” VRP at 18-19. However, the value received through either approach “needed to be actuarially equivalent.” VRP at 19. Mr. Lenander was not entitled to receive an Option B that was of greater value than Option A.

In response to Mr. Lenander’s argument that neither the Option B statute nor the 2000 rule expressly reserved the right change the initial Option B factor, the court held that “there was nothing that needed to be reserved.” VRP at 20. Inherent in the statutory and regulatory requirements—that Option B be actuarially equivalent to Option A—was the authority to change the initially adopted factor when necessary to maintain equivalence. *Id.*

IV. ARGUMENT

On judicial review under the Administrative Procedure Act, a court may invalidate an agency rule only if the rule (i) violates a constitutional

provision; (ii) was not adopted in compliance with statutory rule-making procedures; (iii) exceeds the statutory authority of the agency; or (iv) was arbitrary and capricious. RCW 34.05.570(2)(c). The court presumes that a duly enacted rule is valid; the burden is on the challenging party to present compelling reasons why the rule is in conflict with the intent and purpose of the statute being implemented. *Hi-Starr, Inc. v. Liquor Control Bd.*, 106 Wn.2d 455, 459, 722 P.2d 808 (1986).

Mr. Lenander challenges the Department's amendment of two rules establishing the factors necessary to maintain actuarial equivalence between WSPRS Options A and B (the Option B Equivalence Rules) on two of these bases. He claims that the amended rules exceeded the Department's statutory authority and were unconstitutional as applied to him. Mr. Lenander has not sustained his high burden to prove that the rules are in conflict with the intent and purpose of the statutes they implement, RCW 43.43.278 and RCW 43.43.120, or that they are unconstitutional as applied to him.

A. The Department Had Statutory Authority to Amend the Option B Equivalence Rules

For a rule to be within an agency's statutory authority for purposes of RCW 34.05.570(2)(c), the agency must have authority, express or implied, to engage in rulemaking in the first instance, *State v. Brown*,

142 Wn.2d 57, 62, 11 P.3d 818 (2000), and the adopted rule must be “reasonably consistent with the . . . statute” that the rule purports to implement. *Wash. Pub. Ports Ass’n v. Dep’t of Rev.*, 148 Wn.2d 637, 646, 62 P.3d 462 (2003). The Option B Equivalence Rules are valid in both regards.

First, the Legislature delegated to the Department the express authority and the express duty to adopt the actuarial factors necessary to ensure that alternative benefit options are actuarially equivalent. In general, RCW 41.45.090 requires the Department to adopt in rule the factors necessary to maintain actuarial equivalence—equal cost and equal value—between benefit alternatives to ensure the proper operation of the various systems:

[Every six years, u]pon the basis of . . . actuarial investigation [performed by the State Actuary,] the department shall adopt such tables, schedules, factors, and regulations as are deemed necessary in the light of the findings of the actuary for the proper operation of the state retirement systems.

And specifically for WSPRS Options A and B, RCW 43.43.278 requires the Department to adopt rules to ensure that the two alternatives remain actuarially equivalent:

[T]he department of retirement systems shall adopt rules that allow a member to select an actuarially equivalent retirement option [Option B] that pays the member a reduced retirement allowance and upon death shall be

continued throughout the life of a lawful surviving spouse or lawful domestic partner.

In these provisions, the Legislature plainly provides the Department authority and duty to adopt and amend the Option B Equivalence Rules.

Second, the amendment of the challenged rules was not only “reasonably consistent” but *entirely* consistent with the statutes they implement: RCW 41.45.090, RCW 43.43.278, and RCW 43.43.120. As required by RCW 41.45.090, the rules were amended as part of a larger project to update the actuarial tables, factors, and schedules (used administratively by the Department to provide actuarially equivalent benefit options) on a six-year cycle. As required by RCW 41.45.090, they were adopted on the basis of actuarial investigation performed by the State Actuary and in light of his findings. Consistent with RCW 43.43.120, the Actuary sought the Department’s input in areas in which policy decisions were appropriate (e.g., the applicable mortality table), and used that policy decision in conjunction with statutorily required economic assumptions, demographic assumptions from the most recent experience study, the tools of his profession, and his professional expertise, to develop factors that would provide equivalence between alternative benefit forms. And, as required by RCW 43.43.278, these factors, adopted by rule, allow WSPRS

members to select between two actuarially equivalent retirement options—
A and B.

Nonetheless, Mr. Lenander claims that the rule did not meet the statutory requirements of RCW 43.43.278 and RCW 43.43.120. He claims that (i) once adopted in July 2000, the factors could not be changed; but (ii) if the factors could be changed, such changes could occur (a) only when mortality and/or interest rates changed and (b) only with the additional input from the Department. Appellant’s Op. Br. at 14-19. His arguments should be rejected.

1. RCW 43.43.278 Does Not Limit the Department to a One-Time Adoption of Factors

RCW 43.43.278 provides, “By July 1, 2000, the department of retirement systems shall adopt rules that allow a member to select an actuarially equivalent retirement option [Option B]” Mr. Lenander argues that this language delegated to the Department a one-time duty to adopt immutable Option B factors. He claims that the statute did not include the authority to change the factors once adopted. Appellant’s Op. Br. at 14-16. This argument fails for three reasons: (i) the plain language of the statute does not limit the Department to a one-time adoption; (ii) harmonizing RCW 43.43.278 with the actuarial requirements in RCW 41.45 requires that the actuarial factors be initially adopted by

July 2000 and updated on a six-year cycle; and (iii) reading the statute to allow only a one-time adoption would create an absurd result where the Option B equivalence factors could not change, defeating the express requirement that Options A and B provide equal value to members and equal cost to the retirement system.

First, nothing in the plain language of the statute limits the Department to a one-time adoption. As in many other retirement statutes, the stated date was simply a deadline for the initial adoption of Option B equivalence factors.¹¹

Rather than read the language in RCW 43.43.278 as a requirement for a one-time adoption, the deadline in RCW 43.43.278 must be harmonized with all other retirement statutes dealing with the adoption of actuarial factors. In particular, it must be harmonized with RCW 41.45, which sets the overarching actuarial requirements for the proper operation of all the retirement systems, including WSPRS. *See Hallauer v. Spectrum Props.*, 143 Wn.2d 126, 146, 18 P.3d 540 (2001) (statutes that relate to the same subject matter or stand in *pari materia* must be read

¹¹ The retirement statute contains numerous similar instances in which the Legislature provides a new actuarially equivalent benefit option and the Department is required to adopt initial actuarial factors by a given date, followed by the ongoing update of such factors according to the requirements of RCW 41.45.090. *See, e.g.*, RCW 41.32.530(4) (additional TRS options with original deadline for actuarial factors in July 2001); RCW 41.35.220 (additional SERS options with original deadline for actuarial factors in July 2003).

together as “constituting a unified whole, . . . a harmonious . . . statutory scheme . . . which maintains the integrity of the respective statutes”).

To read RCW 43.43.278 and RCW 41.45 as a unified whole, RCW 43.43.278 should be interpreted simply as setting the deadline for the initial adoption of Option B equivalence factors, to be followed by regular updating of the Option B factors on the six-year cycle in RCW 41.45. Since 1989, RCW 41.45 has provided the modern actuarial framework for updating the actuarial factors for the state’s public pension systems on a six-year cycle. In 1999, the Legislature adopted a new alternate form of WSPRS benefit (Option B) to be effective in July 2000, and directed the Department to adopt the rules necessary to implement the option “by July 2000” (outside the established six-year cycle). To maintain the integrity of these respective statutes, the language in RCW 43.43.278 should not be read to mean that Option B was taken out of the overarching scheme in RCW 41.45.090 or that Option B factors could not be updated after July 1, 2000. Rather, RCW 43.43.278 should be read to require continuing actuarial equivalence between Options A and B, to be achieved through an initial calculation of actuarial factors by July 2000 and their ongoing amendment pursuant to RCW 41.45.090. This reading harmonizes the requirements of RCW 43.43.278 and RCW 41.45.090.

Finally, the courts “must . . . avoid [statutory] constructions that yield unlikely, absurd or strained consequences.” *Kilian v. Atkinson*, 147 Wn.2d 16, 21, 50 P.3d 638 (2002). Mr. Lenander’s argument that Option B factors cannot be updated according to the schedule in RCW 41.45.090 would produce absurd results indeed.

The practical effect of his argument is that if and when the 3% reduction factor ceased to produce benefit options of equal value to the member/spouse and equal cost to WSPRS, it nonetheless could not be changed. While the 3% reduction factor remained immutable, economic and demographic conditions could change, rendering:

- (i) Option A of greater value than Option B for all members; or
- (ii) Option B of greater value than Option A for all members; or
- (iii) Option A of greater value for some, and Option B of greater value for others.

Such a fixed reduction factor would work to the detriment of individual members and the system alike. Members, having no notice regarding changes in the relative value of Options A and B, would make choices between the two options on the assumption they were of equal value, when in fact they were not. Moreover, the actuarial funding of the system itself could be adversely affected. Under the framework in RCW 41.45, the employer and employee contributions necessary to fund WSPRS are calculated based on the cost of each member’s receiving the

core benefit (i.e., WSPRS Option A). This actuarial approach can succeed only if alternatives to the core benefit (e.g., Option B) have equal cost to the system. If there is no assurance that benefit alternatives have equal cost, the calculated contribution rates may not be adequate to maintain the funded status of the pension trusts. The only way to guarantee that Options A and B will have equal cost to the system is to update the Option B equivalence factors periodically.

In short, interpreting RCW 43.43.278 to require a one-time adoption of the Option B equivalence factor fails to harmonize the statute with the overarching actuarial scheme, thereby producing absurd results.

2. RCW 43.43.120 Does Not Limit When the Department May Modify the Option B Factors or the Variables That May Be Considered

RCW 43.43.278 provides that the Department “shall adopt rules that allow a member to select an actuarially equivalent retirement option [i.e., Option B]” RCW 43.43.120(1) defines “actuarial equivalent” as “a benefit of equal value when computed upon the basis of such mortality table as may be adopted and such interest rate as may be determined by the [Department’s] director.” From these statutes, Mr. Lenander argues that if the Option B factors may be updated, (i) they can be updated only upon a *change* in mortality and/or interest rate and (ii) the updated factors must be derived exclusively from an applicable interest rate and mortality

table. Appellant's Op. Br. at 16-18, 19. Again, these arguments must be rejected for the reasons that follow.

a. Actuarial Factors Are Updated on a Regular Six-Year Cycle Rather Than Upon *Changes* in Mortality and/or Interest

Contrary to Mr. Lenander's suggestion, nothing in the plain language of RCW 43.43.278 and RCW 43.43.120 conditions the adoption of updated Option B factors on a change in mortality tables and/or interest rates. As discussed above, RCW 43.43.278 and RCW 43.43.120 must and can be harmonized with the requirements of RCW 41.45.090 to produce a unified actuarial framework for WSPRS. RCW 41.45.090 establishes that the factors must be updated on the established six-year cycle. And, when the Option B equivalence factors are updated according to this schedule, RCW 43.43.278 and RCW 43.43.120 establish how they should be updated—with appropriate consideration of mortality and interest to produce benefit options of equal value.

But even if Mr. Lenander were correct that the Option B equivalence factors may be updated only when mortality tables and/or interest rates change, his challenge to the rule would still fail because the interest rate *has* changed since the flat 3% factor was adopted. When the

3% factor was adopted in May 2000, the statutory interest rate was 7.5%.¹² CP 660. Presumably, the State Actuary used this rate in developing the 3% reduction factor. *See Smith v. Hollenbeck*, 48 Wn.2d 461, 294 P.2d 921 (1956) (public officers are presumed to perform their duties in compliance with controlling statutory provisions). By the time the Option B factors were updated in 2010, the statutory interest rate had been increased to 8%. Final B. Rep., ESSB 6167 (Wash. 2001). Under Mr. Lenander's own argument, nothing more is required to authorize the Department to update the Option B factor.

b. In Updating the Option B Equivalence Factors, the State Actuary Must Consider All Relevant Factors, Not Simply Mortality and Interest

As set forth above, RCW 43.43.278 provides that the Department “shall adopt rules that allow a member to select an actuarially equivalent retirement option [i.e., Option B],” and RCW 43.43.120, defines “actuarial equivalent” as “a benefit of equal value when computed upon the basis of such mortality table as may be adopted and such interest rate as may be determined by the [Department's] director.” Mr. Lenander argues that the new Option B factors should be rejected because the State Actuary

¹² Counsel for the Department found evidence of the May 2000 rate in a Final Bill Report while drafting the Department's brief to the superior court. In 1997, the Economic and Revenue Forecast Council set the interest rate to 7.5%. This rate remained unchanged until 2001, when the interest rate was statutorily increased to 8% per year. Final B. Rep., ESSB 6167 (Wash. 2001) (CP 667-89).

considered variables in addition to mortality and interest, but the statute “only allows” consideration of mortality and interest rates. Appellant’s Op. Br. at 16-17. This argument ignores the fundamental requirement in RCW 43.43.120 that to be “actuarially equivalent” benefits must have equal value.

A statute must be construed by reading it in its entirety and considering its relation with the statutory scheme as a whole. *Dep’t of Ecology v. Campbell & Gwinn, L.L.C.*, 146 Wn.2d 1, 11, 43 P.3d 4 (2002). All statutory language should be given effect, and no portion should be rendered meaningless or superfluous. *Kilian*, 147 Wn.2d at 21.

Mr. Lenander’s argument fails to give effect to the statutory language that Options A and B be “actuarially equivalent,” RCW 43.43.278, and have “equal value,” RCW 43.43.120. Only a professional actuary knows which economic and demographic variables and which actuarial formulas and other tools of the trade are necessary to the calculation of an actuarial factor that will produce equal value. The State Actuary is such a professional, “qualified by education and experience in the field of actuarial science” and “a member of the American academy of actuaries.” RCW 44.44.010(2), .030(2). To calculate the updated Option B equivalence factor, the Actuary, applying his professional expertise, used all relevant variables, including the

relevant mortality tables and interest rates, to derive factors that would produce benefit options of equal value.

In the actuarial communication setting out his findings and recommendations for each of the factors updated in the 2008-2009 Project, the State Actuary listed the variables that he had deemed relevant and necessary to his calculations. CP 544-47. To update the Option B factor, he of course used the most recent definitions of Options A and B.¹³ He used statutorily required economic assumptions (e.g., 8% interest, 3% annual cost-of-living adjustment) and statutorily required demographic data from the 2006 Experience Study Report (e.g., normal retirement age, 53; service at retirement, 29 years). CAR1 267. *See* RCW 41.45.035, .090. And, as appropriate within the requirements of actuarial science, he incorporated policy decisions by the Department, including the Department's decision to use the "mortality rates developed in the 2001-2006 OSA Experience Study Report . . . , without additional mortality improvement trends." CAR1 266.

Contrary to Mr. Lenander's assertion, RCW 43.43.120 cannot be construed to compel the State Actuary to disregard his professional

¹³ Between 2000 and 2010, Option A had changed from a 2% automatic cost-of-living adjustment (COLA) for the member and a lesser automatic COLA for the member's spouse to a variable cost-of-living adjustment for each. Option B had changed from a 2% automatic COLA for both member and spouse to a variable COLA for each. These changes necessarily affected the total value of each benefit option over the joint lives of member and spouse and must, therefore, be considered in the update.

expertise and standards by requiring him to use less data or fewer tools than are necessary to produce true actuarial equivalence. To construe the statute in its entirety, giving effect to all its terms, RCW 43.43.120 must authorize the Actuary to consider the variables he knows to be necessary and employ the methodology he knows to be required to produce benefit options of actuarially equal value, while allowing the Department appropriate input regarding mortality and interest.

3. The Department Had Appropriate Input Into the Development of the Amended Option B Factors

RCW 43.43.120(1) (emphasis added) defines “actuarial equivalent” as “a benefit of equal value when computed upon the basis of such mortality table as *may be adopted* and such interest rate as *may be determined* by the [Department’s] director.” Mr. Lenander argues that the Department did not have sufficient input into the mortality table and interest rate used by the State Actuary in updating the Option B equivalence factors. Appellant’s Op. Br. at 19-20. His argument should be rejected: the definition in RCW 43.43.120(1) does not require the Department to have had more input than it did in the adoption of the Option B factors. Without question, the Department did adopt a mortality table. CAR 246-49, 257, 265-66. And, the Department had appropriate

input in the determination of an interest rate pursuant to RCW 43.43.120(1).

First, in RCW 43.43.120(1), the Legislature did not require the Department to adopt a mortality table by rule. Although nothing in RCW 43.43.120(1) expressly required the Department to adopt a mortality table by rule, in effect the Department did so when it adopted the Option B Equivalence Rules. Before making a final recommendation regarding the updated Option B equivalence factors, the State Actuary presented the Department with a range of reasonable options for the mortality table to be used in calculating the new factors and sought the Department's input. CAR1 243, 246. The Department's Director chose the mortality table the Actuary had recommended, and this table was then used in the Actuary's calculations. CAR1 246-49, 257, 265-66. When the Department adopted the Option B factors predicated on the mortality table it had requested, it implicitly adopted the underlying mortality table itself by rule.

Second, the Department's Director had appropriate input in the determination of an interest rate pursuant to RCW 43.43.120. RCW 43.43.120(1) was originally adopted in 1951, at a time when WSPRS was administered by a retirement board, and this definition of

“actuarially equivalent” has since remained virtually unchanged.¹⁴ However, the context for the implementation of the definition in RCW 43.43.120(1) has changed considerably since it was enacted. During the 1950s, the WSPRS Board was required to retain a private actuary at least once every five years to perform the services now performed by the State Actuary. CP 674-75. The private actuary’s only access to the economic and demographic data necessary to perform its work was through the WSPRS Board. Accordingly, the Board was required to collect the necessary data and provide it to the retained actuary, including the current rate of return (interest rate) in the WSPRS fund. The retained actuary could have no knowledge of this rate independent of the WSPRS Board.

After the State’s actuarial services were consolidated in the Office of the State Actuary in 1976 and RCW 41.45 was enacted in 1989, the process for determining the economic assumptions, including the interest rate, required to be used by the Actuary in calculations for all the pension systems evolved. By 2010 (when the Department amended the challenged rules), economic assumptions, including interest rate, were set in statute, subject to revision by the Pension Funding Council. At that time, the

¹⁴ RCW 43.43.120(1) was previously codified at RCW 43.43.120(15) in 1951. In a housekeeping statute in 1982, all references to the former boards were changed to references to the Department. Laws of 1982, 1st Ex. Sess. ch. 52, § 24.

Department's Director was (and continues to be) a statutory member of the Pension Funding Council with input into revisions of the interest rate. RCW 41.45.100.

Consistent with the principle of reading statutes in *pari materia*, the definition in RCW 43.43.120(1) and the provisions of RCW 41.45 can and should be harmonized to create a "unified whole." See *Hallauer*, 143 Wn.2d at 146. To harmonize RCW 43.43.120(1) (WSPRS actuarial factors are based on such "interest rate as may be determined" by the Department) with RCW 41.45 (setting the interest rate to be used in all actuarial calculations at 8%), this Court should find that the Director, through his role on the Pension Funding Council, did "determine" the 8% statutory interest rate used in calculating the Option B factor in 2010.

In the alternative, this Court should find that the modern statutory framework for actuarial services provided to the Department, enacted in 1989 in RCW 41.45, supersedes the requirements of the 1951 statute. Indeed, it is a well-recognized rule of statutory construction that "where a law is amended and a material change is made in the wording, it is presumed that the legislature intended a change in the law." *City of Seattle v. Fuller*, 177 Wn.2d 263, 282, 300 P.3d 340 (2013) (citation omitted). By 2010, whatever authority RCW 43.43.120(1) may have delegated (to the WSPRS Board in 1951 or to the Department in 1977) to

“determine” a WSPRS interest rate had been superseded by RCW 41.45, which now sets the interest rate to be used in all actuarial calculations related to the state retirement systems.

4. The Evolution of the Department’s Rules Regarding Actuarial Equivalence in Other Systems Have No Relevance to the Department’s Statutory Authority to Amend the Option B Rules

Admitting he is arguing for a unique interpretation of actuarial equivalence, Mr. Lenander claims that the “Washington State Patrol Plan 1 System Was Always Understood To Be Different From Other Systems.” Appellant’s Op. Br. at 19-23. He claims (i) that the rules containing the actuarial factors for other retirement systems contain “reservation language;” (ii) the WSPRS Option B Equivalence Rules do not; and (iii) without “reservation language,” the WSPRS Option B rules cannot be amended.

As a preliminary matter, Mr. Lenander’s factual assertion is flawed: since 2003, the WSPRS Option B rules have incorporated the same “reservation language” applicable to the Department’s other rules containing actuarial factors. The initial Option B Equivalence Rule was adopted in 2000. In 2002, on the six-year cycle set forth RCW 41.45, the Department updated the actuarial tables, schedules, and factors used in the other retirement systems it administers, consolidating them in WAC 415-

02, containing “general rules affecting multiple plans and systems [including WSPRS].” WAC 415-02 (internal heading). WAC 415-02-300(3) provided that the tables “may be amended from time to time, based upon subsequent actuarial investigations.” Although the WSPRS Option B factor (then 3%) was not incorporated in these general rules in 2002, the following year the Option B Equivalence Rule (WAC 415-103-215) was amended and that amendment incorporated the provisions in the general rule for periodic updating of actuarial tables, schedules, and factors into the Option B rule. WAC 415-103-215(6). Thus, the Department’s rules reflect its statutory authority to amend the Option B rule “from time to time based on subsequent actuarial investigation.” WAC 415-02-300(3).

Second, to the extent Mr. Lenander’s argument is intended to address the Department’s *statutory authority* to amend the Option B Equivalence Rule in 2010 (one of the only two issues in this appeal), his argument about the agency rules for other systems has little relevance. The Department’s statutory authority can only be determined from the statutes themselves, not by reference to the provisions of administrative rules governing actuarial factors in other systems.

In conclusion, the amendment of the Option B Equivalence Rules did not exceed the Department’s statutory authority. The Department had express statutory authority to adopt rules to maintain the actuarial

equivalence of Options A and B. Consistent with RCW 43.43.120(1), as harmonized with more recent provisions regarding actuarial factors in RCW 41.45, the updated rules were promulgated on the appropriate schedule, based on the necessary underlying variables and the statutorily required input from the Department.

B. Updating the Actuarial Factors in the Option B Equivalence Rules Did Not Unconstitutionally Impair Mr. Lenander's Pension

A court will invalidate a rule if it “violates constitutional provisions.” RCW 34.05.570(2)(c). The party alleging that a rule is unconstitutional must prove unconstitutionality beyond a reasonable doubt. *Longview Fibre Co. v. Dep't of Ecology*, 89 Wn. App. 627, 632-33, 949 P.2d 851 (1998). Mr. Lenander has not sustained his burden to prove (i) that, under the traditional test for contract impairment, his pension benefit was substantially impaired; or (ii) that, under the pension-specific *Bakenhus* test, he had a constitutional right to an Option B benefit based on the reduction factor in use when he initially became employed. Accordingly, the Option B Equivalence Rules are constitutional as applied to Mr. Lenander.

1. The Traditional Test for Contract Impairment Is the “Backbone” of This Court's Analysis

Recently, the Supreme Court announced that “when analyzing whether a law impairs public pension contracts [the court] will apply the

same three-part test governing all public contracts.” *Wash. Educ. Ass’n v. Dep’t of Ret. Sys.*, 181 Wn.2d 233, 244, 332 P.3d 439 (2014) (*WEA I*); see also *Wash. Educ. Ass’n v. Dep’t of Ret. Sys.*, 181 Wn.2d 212, 222, 332 P.3d 428 (2014) (*WEA II*). “[T]his test provides that [state action] will unconstitutionally impair a public contract only if it substantially impairs an existing contractual relationship and is not reasonable and necessary to serve a legitimate public purpose.” *WEA I*, 181 Wn.2d at 243. The test addresses three distinct questions: (1) does a contractual relationship exist; (2) does the action substantially impair the contractual relationship; and (3) if so, was the impairment reasonable and necessary to serve a legitimate public purpose? *WEA II*, 181 Wn.2d at 222.

In both *WEA I* and *WEA II*, the Court was required to consider the interrelationship between this traditional test and the “*Bakenhus* test,” specifically developed to analyze contract impairment in the pension context. *WEA I*, 181 Wn.2d at 243; *WEA II*, 181 Wn.2d at 222. The Court held that the traditional test was the “overarching framework” for the analysis of impairment in the pension context—that the *Bakenhus* factors may supplement the traditional test, but their use must be “properly confine[d] . . . within the three-prong backbone of” the traditional test. *WEA II*, 181 Wn.2d at 223. Mr. Lenander’s claim must be analyzed within the overarching framework of the traditional test.

2. Exercising a Statutory Provision Cannot Create Substantial Impairment

Under the traditional test, the contours of a contractual relationship are determined by the language of the statute taken in its totality. Both *WEA I* and *WEA II* involved statutes that contained a pension provision coupled with express language in which the Legislature reserved the right to repeal the provision. In both cases, the Legislature had exercised its reserved right to repeal the provision, and plaintiffs sued, claiming that, under *Bakenhus*, they had vested contractual rights in the benefit provided by statute notwithstanding the reservation clauses.

Using the traditional test, the Court refused to find unconstitutional impairment in either case—it held that “the repeal legislation did not substantially impair the contractual relationship as reflected in the . . . statute”:

The [plaintiffs’] contract rights are defined by the language of the statute creating those rights. Here, that language includes a right to amend or repeal. . . . The . . . repeal merely executed a provision of the established contract.

WEA I, 181 Wn.2d at 244. “[T]he repeal of [the benefit] cannot impair any existing contractual right because the express language of the . . . statute provided for its repeal.” *WEA II*, 181 Wn.2d at 223. In short, the exercise of a provision expressly contained in a statute could not possibly be a “substantial impairment” of the contractual relationship.

3. Updating the Three Percent Reduction Was Not a Substantial Impairment

Mr. Lenander claims that he has a contractual right to the continuation of the 3% reduction factor contained in the Department's 2000 rule. He claims that the 5.3% reduction of his Option B benefit under the updated rules constituted an unconstitutional impairment of contract. Appellant's Op. Br. at 23-31. Mr. Lenander's claim must be analyzed using the traditional test by asking: (i) whether there was a contractual relationship between Mr. Lenander and the State, and if so, (ii) whether that relationship was substantially impaired by the amendment of the Option B factors. Just as the contractual relationship in the *WEA I* and *WEA II* cases was wholly defined by the language of the statutes creating the relationship, Mr. Lenander's relationship with the State is defined by the statutes creating it.

RCW 43.43.278 provides that the Department "shall adopt rules that allow a member to select an actuarially equivalent retirement option" RCW 43.43.278 must be understood in the context of the statutory framework governing actuarially equivalent benefits that requires that actuarial factors be updated periodically based on recommendations from the State Actuary. RCW 43.43.278 never provided that WSPRS members had a right to receive an Option B benefit that was exactly 3%

less than an Option A benefit; it provided only that they had the right to select an Option B benefit that was *actuarially equivalent* to Option A. The 2010 rules maintain the actuarial equivalence between Options A and B by updating the factors that create equivalence. As in *WEA I* and *WEA II*, the exercise of the provision for periodic updates expressly contained in the statute could not substantially impair the statutorily defined contractual relationship. When the State acts on authority contained in a statute, it does not alter and, *ipso facto*, does not impair the essential statutory relationship. *See WEA I*, 181 Wn.2d at 244.

Mr. Lenander suggests that because the Legislature did not more expressly “reserve the right” to change the Option B factor in RCW 43.43.278, the factor could not be changed once set. Appellant’s Op. Br. at 8. But, as the superior court recognized, the Legislature did not need to articulate an express reservation of the Department’s right to change the Option B equivalence factor. Rather, by using language requiring ongoing actuarial equivalence, the Legislature effectively reserved the Department’s right to amend the factor to preserve actuarial equivalence.

The foregoing result is identical to the result reached under the *Bakenhus* test in *King County Employees’ Association v. State Employees’ Retirement Board*, 54 Wn.2d 1, 336 P.2d 387 (1959). Like this case, *King*

County involved the election between two actuarially equivalent options. Initially, the actuarial factors used to convert between the two options were based on mortality tables for male lives. Six years later, new factors were adopted for women based on mortality tables for female lives. The new factors caused women's annuities to be reduced more than they had been previously. Female employees claimed that the adoption of the new factors was an unconstitutional impairment of contract under *Bakenhus*.

The Supreme Court disagreed, holding that women did not have a contractual right to the continuation of the factors that had been in existence when they began employment. Rather, as in *WEA I* and *WEA II*, their benefits were determined by the language of the statute:

[O]ne must look to the statute to determine what [the] annuity is. . . . The member, under the plain wording of the statute, does not acquire a vested contractual right to an annuity based on the mortality table in use when the employee became a member of the retirement system; rather, the employee acquires a vested right to 'a benefit of equal value' to his or her accumulated contributions

King Cnty., 54 Wn.2d at 9. The Court found no impairment of contract under *Bakenhus*.

Consistent with *King County*, even if the *Bakenhus* test is used in the present case to supplement the three-prong backbone of the traditional text, there is no basis for this Court to find that the updated Option B factors impaired Mr. Lenander's pension.

4. Periodically Updated Actuarial Factors Do Not Create Rights Through Administrative Practice

Citing *Bowles v. Department of Retirement Systems*, 121 Wn.2d 52, 847 P.2d 440 (1993), Mr. Lenander argues that because the original Option B Equivalence Rules did not expressly state that the factor could be amended and because the factor was used for approximately ten years, members acquired, through “administrative practice,” a contractual right to the 3% reduction in perpetuity. Appellant’s Op. Br. at 19-23, 27-30. This argument misinterprets the *Bowles* decision.

Bowles involved the Department’s interpretation of an ambiguous statute. After interpreting the statute one way for up to ten years, the Department subsequently sought to reinterpret the statute. The *Bowles* Court held that the Department’s long-standing administrative interpretation of the statute had created in the affected employees a contractual right to the original interpretation. Once the Department established a permissible interpretation and so administered the statute for a number of years, employees developed expectations in the continuation of the interpretation.

This case is entirely different. Unlike *Bowles*, it does not involve the interpretation of an ambiguous statute through administrative practice, but rather the exercise of delegated legislative authority on a statutory

schedule. When the Department initially adopted the 3% reduction factor it was not interpreting an ambiguous statute (i.e., the definition of “actuarial equivalence”); it was simply exercising its statutory duty to adopt a rate that would provide actuarial equivalence, to be effective until updated according to the statutory cycle. Thus, *Bowles* is not applicable here; its ruling must be limited to the unique facts of that case.

C. Mr. Lenander Is Not Entitled to Fees Under RCW 49.48.030, RCW 4.84.350, or the Common Fund Doctrine

If this Court rules in favor of Mr. Lenander, he nonetheless will not be entitled to attorneys’ fees. RCW 49.48.030 provides no authority for the assessment of fees against a defendant that is not the person’s employer or former employer. *City of Kennewick v. Bd. for Volunteer Firefighters (BVFF)*, 85 Wn. App. 366, 370, 933 P.2d 423 (1997).¹⁵ In *City of Kennewick*, the City and five former volunteer firefighters prevailed in an action for retirement benefits against BVFF and sought attorneys’ fees under RCW 49.48.030. Because BVFF was not plaintiffs’ “employer,” but merely administered retirement benefits, the Court unequivocally denied fees, stating:

¹⁵ Mr. Lenander’s reliance on *Bates v. City of Richland*, 112 Wn. App. 919, 51 P.3d 816 (2002), and *Merino v. State*, 179 Wn. App. 889, 320 P.3d 153 (2014), is misplaced. In both cases, fees were awarded against the employer, *not* the Department. CP 671-72.

The statute [RCW 49.48.030] does not authorize an assessment of attorney fees against a party who is not an employer. The attorney fee request is denied.

City of Kennewick, 85 Wn. App. at 370. Similarly, RCW 49.48.030 provides no basis for Mr. Lenander's attorneys' fees from the Department because the Department was not his employer.

Nor are fees available under RCW 4.84.350, which provides "a court shall award a qualified party that prevails in a judicial review of an agency action . . . reasonable attorneys' fees, unless the court finds that the agency action was substantially justified" To show that its action was "substantially justified," an agency must demonstrate that its action had a reasonable basis in law and fact. *Constr. Indus. Training Coun. v. Wash. State Apprenticeship & Training Coun.*, 96 Wn. App. 59, 68, 977 P.2d 655 (1999).

When a case involves an issue of first impression or a close question of statutory interpretation, courts have regularly found an agency's carefully considered action to be reasonable and "substantially justified"—even when ultimately found by the court to be incorrect. *See Honesty in Env'tl. Analysis & Legislation v. Cent. Puget Sound Growth Mgmt. Hearings Bd.*, 96 Wn. App. 522, 535-36, 979 P.2d 864 (1999).

Under this standard, the Department's rule amendments, updating the Option B factors, were substantially justified. The amendments were

made following the modern statutory process in RCW 41.45, upon the recommendation of the State Actuary. Any complaint regarding the constitutionality of such amendment had been decided in the Department's favor years ago in *King County*. Because Mr. Lenander cannot prove that the Department's interpretation of the issue was not substantially justified, he is not entitled to fees under RCW 4.84.350.

Finally, Mr. Lenander's claim for common fund fees must be rejected. He did not seek common fund fees in his Petition for Review or in his briefing before the superior court. If this Court determines that attorneys' fees should be awarded under the common fund theory, additional briefing will be required to determine the source of the common funds to be paid. If Mr. Lenander suggests that fees be paid as a loan from the WSPRS trust, briefing will be required to address federal tax law barring such approach. Common fund fees cannot be granted until an adequate payment scheme is vetted.

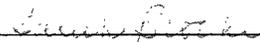
V. CONCLUSION

This Court should affirm the Superior Court, holding that the 2010 amendment to the Option B Equivalence Rules was within the

Department's statutory authority and did not violate Mr. Lenander's constitutional rights.

RESPECTFULLY SUBMITTED this 14th day of September, 2015.

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CERTIFICATE OF SERVICE

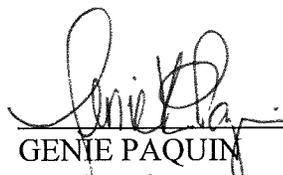
I hereby certify under penalty of perjury according to the laws of the State of Washington that on September 14, 2015, I caused true and correct copies of the foregoing *BRIEF OF RESPONDENT WASHINGTON DEPARTMENT OF RETIREMENT SYSTEMS* to be filed with the Washington State Court of Appeals Division II and be served as follows:

U.S. Mail Postage Prepaid via Consolidated Mail Service:

Wayne Williams
Williams, Wyckoff & Ostrander, PLLC
P.O. Box 316
Olympia, WA 98507

I certify under penalty of perjury under the laws of the state of Washington that the foregoing is true and correct.

DATED this 14th day of September, 2015, at Olympia, Washington.



GENIE PAQUIN
Legal Assistant

WASHINGTON STATE ATTORNEY GENERAL

September 14, 2015 - 10:29 AM

Transmittal Letter

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