

# Major Changes To Act 600 Enacted By The Legislature



By William C. Asay, CEBS  
President  
(412) 394-9332  
wcasay@ebds.com

The General Assembly has passed and the Governor has signed legislation that significantly changes the provisions of Act 600 of 1956, the Municipal Police Pension Law. This amendment will affect all Act 600 plans and the changes will become a part of your collective bargaining process in the near future. The law became effective immediately upon the signature of the Governor. He signed the legislation on April 17, 2002, which is now Act 30 of 2002.

The following article reflects our initial interpretation of the benefit changes enacted by the legislature and the potential effect on the funding of the plans. The governing body should seek the interpretation and advice of the Solicitor prior to making any changes to the pension plan. In addition, as every pension plan will be affected differently, your municipality should contact the pension plan actuary to determine how these benefit changes may affect the funding of your plan (as required by section 305 of Act 205 of 1984).

This amendment has made multiple changes to five benefits of an Act 600 police pension plan:

1. **Surviving Spouse Benefits** (after retirement eligibility)
2. **Pre-Retirement Surviving Spouse Benefits**
3. **Disability Benefits**
4. **Killed-in-Service Benefits**
5. **Employee Contributions**

## Surviving Spouse Benefits

Prior to this amendment, the surviving spouse benefits could be paid to the spouse of

a deceased police officer who had reached the age and service requirement for normal retirement, early retirement or was actually receiving a disability or vested benefit. The benefit payable to the spouse was 50 percent of the amount the officer was eligible to receive or actually receiving at the time of his death. This benefit was payable to the surviving spouse until she subsequently dies or remarries. If she dies or remarries and there were any children under 18, they would receive payments until their 18th birthday.

The amendment changed this provision in three ways:

1. Removes the word "remarries"
2. Alters the ending age of the children payments to 23 if they are attending a college if the spouse dies
3. Mandates a surviving spouses benefit for all police officers with a minimum benefit level of 50 percent

## Remarries

By removing the word "remarries" from the statute, the Legislature will allow the spouse to remarry and continue receiving surviving spouses benefits from the police pension plan until her death. Over the years, very few municipalities have actually tracked the marital status of the spouse of a deceased retiree.

## Age 23 If Attending College

The change in the children's age will allow a participant's child who is "attending college" to receive the benefit until they are 23 if the spouse dies. The amendment defines "attending college" as being registered at an accredited institution of higher learning and carrying a minimum course load of seven credits per semester.

Neither of the first two changes to this section will have much of an impact on the funding requirements of the pension plan.

However, the third change could have a larger impact.

## 50 Percent Surviving Spouses Benefit Minimum

This change alters the prior surviving spouses benefit from being an optional benefit to being a mandatory benefit. The mandatory benefit will be payable at a minimum rate of 50 percent of the monthly benefit. This change appears to allow the surviving spouses benefit to be paid at any level above 50 percent. Although the legislation does not dictate a maximum benefit level, in most other pension plans 100 percent is the maximum. It also appears that this benefit will be an unreduced benefit rather than an actuarially reduced benefit.

Depending on whether the pension plan already includes a surviving spouses benefit and the actual percentage adopted, this provision may have a moderate impact on the cost of the plan.

## Grandfathering of Spouses Currently Receiving Surviving Spouses Benefits

Any widow whose spouse died prior to the effective date of this Act and has not remarried will be affected by this amendment. It would appear that if the pension plan did not include a surviving spouse's benefit at the time the retiree began receiving monthly benefits, it must do so now. So long as the spouse has not remarried, it would appear that the spouse must now begin to receive benefits. (It makes no reference to those spouses who were covered by an optional form of benefits elected from the provisions of prior plans.) The application of the benefit may be retroactive but whether the actual benefit payments must be made payable to the date of the retiree's death is currently not determinable from this legislation. The cost implication of this benefit modification will be entirely dependent on the specifics of each plan.

# SPECIAL UPDATE

## Pre-Retirement Surviving Spouse Benefit

Prior to the passage of this amendment, in order for a widow to be eligible to receive a benefit for a deceased member, the member would have been required to survive to his normal or early retirement date. If he did not survive to that date, Act 600 required that the beneficiary receive a refund of his employee contributions, plus interest. (53 P.S. 775) This amendment specifies a procedure for refunding employee contributions for members that die prior to becoming vested. The change in legislation isn't specific, however, it may be inferred that since this revision is part of the section on survivor benefits (*Section 1(a)(5)*) and it specifies how pre-vesting contributions are to be distributed, any spouse of a member who dies after becoming vested is entitled to receive a monthly benefit payable at the earliest retirement date and at a rate specified by the plan. The governing body should seek advice from the Solicitor prior to making any changes to this section.

The effect of this change on the annual funding of the plan will depend on the percentage rate of the surviving spouse's benefit. The change should have a minimal effect on the annual cost.

## Disability Benefit

Act 600, mainly through judicial interpretations, mandates that a police pension plan must provide a disability provision. However, to qualify, the disability must be Service-Connected and the disability must render the police officer Totally and Permanently disabled. The definition for Total and Permanent disability is that the police officer is unable to perform the usual and customary duties of a police officer.

The definition, as interpreted, is very broad in nature. Because of the expansive definition, this provision has been used for many different purposes, other than paying disability benefits to truly disabled participants. The courts determined that the amount of the benefit was to be determined by the governing body or through negotiations. The amendment has made major changes to the disability provision and it could have a dramatic effect on your pension plan.

First, the amendment has set a floor level of **no less than 50 percent of the member's salary** at the time the disability occurs. (*The Act refers to "salary" and not "monthly average salary" as used in the normal retirement benefit section. This may allow the salary to be used in the disability calculation to be different from the normal retirement calculation.*) Until recently, federal law restricted the maximum benefit allowable in a qualified pension plan to the 100 percent of the highest three years salary (*IRC Section 415*). However, this maximum benefit level no longer applies to governmental pension plans. It now appears that any benefit level, over 50 percent, may be negotiated, arbitrated and/or granted.

This benefit, depending on the benefit level adopted and the number of members retiring under this provision could have a dramatic effect on the annual funding of the plan. Before adopting a specific benefit level above 50 percent, you should have the plan actuary study various benefit percentages and he should study various scenarios assuming that an actual disability benefit will be paid. When you combine a very broad definition of Total and

Permanent disability with a benefit level that exceeds the normal retirement benefit (*50 percent*), the probability of an occurrence increases. Don't be shocked at the change in liability and the increase in annual cost when a disability occurs.

Secondly, the amendment includes a mandatory offset for any member who qualifies for benefits under the Social Security Act because of the same injuries that qualified him for a pension under the pension plan. Since no percentage is enumerated, it is assumed to be 100 percent. This means that the entire Social Security entitlement would be used to reduce the disability payment from the pension plan. However, my experience has been that the member qualifying for a disability pension according to the provisions of the pension plan rarely qualifies for a Social Security Disability because of the same injuries. If a participant were to qualify for a Social Security Disability benefit there are often times other contributing factors which could eliminate any offset. Also, since the amendment specifically refers to Social Security Act and no other, all other cost controlling offsets may no longer apply. I believe that the offset added to this section will rarely occur. Therefore, I believe the offset will seldom help to control costs.

## Killed-in-Service

Prior to the passage of this amendment, Act 600 allowed for the voluntary adoption of a killed-in-service provision whose benefit level was to be set by the governing body. It stated the *"...amount and commencement of the payments shall be fixed by regulations of the governing body of the borough, town, township or regional police department."* (53 P.S. 771) This meant that if the municipality adopted this provision the governing body, through negotiations or through arbitration determined the benefit level. This amendment now **mandates** that the benefit be included in the pension plan and the benefit is calculated at **100 percent of the member's salary**. (*As with disability, it says "salary" and not "average monthly salary."*)

The probability of a police officer being killed-in-service is, thankfully, low. Since the probability is low, the pre-funding effect on the annual cost would typically be minimal. However, at the levels mandated by this act, if a married police officer were killed-in-service, it could have a devastating effect on the funding levels of the plan, especially if the plan is small or not extremely well funded. The actuary would determine the actual monthly benefit payable and could determine the actual change in liability to the plan. In these cases, I have seen the actuarial accrued liability range from \$300,000 - \$600,000 for just one individual. As payroll increases, the benefit level will increase and actuarial accrued liability will increase accordingly. Again, have your actuary run a few "what if" scenarios and don't be surprised at the dramatic increases in annual costs. I would strongly suggest that the governing body investigate the possibility of insuring this risk. The premium for such coverage should be very low and will help to protect the plan. However, we would note the insurer would expect a tight, objective interpretation for an insurable killed-in-service death benefit in order to control their own risk exposure.

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# CHANGES

## Employee Contributions

The prior law incorporated municipal general fund protections whenever the employee contribution rate was reduced or eliminated. The prior law allowed for employee contributions to be reduced from the mandatory levels (5 percent for plans covered by Social Security with no offset and 5 - 8 percent for plans not covered by Social Security) if the following occurred on an annual basis:

1. An actuarial study shows that the contributions will not be required to keep the fund actuarially sound,
2. A resolution is passed by the governing body, and
3. If contributions are reduced or eliminated, no contribution will be required from the municipality's general fund.

Previously, in order to comply with Act 600, the Minimum Municipal Obligation was funded in the following order (53 P.S.772(c)).

1. State Aid
2. Employee Contributions
3. Municipal Contributions

The amendment eliminates the requirement for the employee to contribute at his/her mandatory level if municipal contributions are required to keep the fund actuarially sound. It eliminates the requirement for an actuarial study to determine the actuarial need for employee contributions, but the governing body will continue to be required to pass an annual ordinance or resolution. (*Your solicitor will need to determine if this amendment will supercede Section 305 of Act 205 of 1984 and the recent court interpretation that the study is required under Act 205.*)

This amendment eliminates the statutory protection the municipality enjoyed when dealing with employee contributions. The employees will no longer be required to contribute to the plan before the municipality is required contribute. The municipality could be required to contribute while the employee contributions are eliminated. If employee contributions are eliminated, there will be a minimal effect on the annual funding of the plan. As the employee contribution rate is reduced in plans across the state and the State Aid annual contribution is increased to offset the employees' annual contributions, I believe it will have a negative effect on future unit values. The effect on the budget for municipalities receiving the maximum amount of State Aid, would be a dollar for dollar increase. I would urge the municipality to review the reduction or elimination of employee contributions with the plan actuary.

## Documentation and Formal Adoption

Changes resulting from the passage of this Act will constitute a formal change to the pension plan provisions. You may need to incorporate them in your collective bargaining agreements. You will be required to include any changes made to you pension plan in your municipal pension plan document and/or your plan ordinance or plan resolution. This will help to ensure benefit provision consistency throughout the plan and hopefully limit litigation. In addition, this will allow the plan actuary to value the cor-

rect set of benefit when completing the biennial actuarial valuation and the administrator to calculate the correct benefit amounts for affected retirees. Finally, by formalizing the new plan provisions, it will help to avoid future audit findings by the Department of the Auditor General.

## Summary

This amendment provides many ancillary benefit enhancements, both mandatory and optional, which benefit the members. It has been many years since Act 600 has undergone such extensive changes. With the potential magnitude of changes imposed, comes fiduciary responsibility. It is the fiduciary responsibility of the governing body to understand the implication these changes may have on your plan. From the layman's point of view, these changes would be thought to have little impact on the plan. After all, the state reviewed the bill and there were actuarial studies (*footnotes*) completed showing the potential increases in annual costs. Unfortunately, the study reflects the potential cost implications on a statewide basis. The actuarial cost implications should be reviewed at the plan level. After all, the governing body of the municipality is responsible by law to fund the pension plan appropriately. You should determine the effect these changes will have on collective bargaining, State Aid revenues and general fund revenues. If municipal officials do not evaluate and understand the potential cost implications of this amendment, they may find themselves unprepared for future increases.

*You will be hearing from your Mockenhaupt Benefit Group consultant in the near future to discuss the effect the changes Act 30 will have on your plan. If you are currently in contract negotiations, please contact us immediately.*

**Mockenhaupt Benefits Group is committed to making a difference for you.**



## Contact Information

### Mockenhaupt Benefits Group

Suite 1225  
One Gateway Center  
420 Fort Duquesne Blvd.  
Pittsburgh, PA 15222

**Toll Free Phone 1-800-405-3620**

**Local Phone (412) 394-9660**

**Fax (412) 394-6339**

## SPECIAL UPDATE

# SUMMARY

### Summary of Act 30 of 2002 - Changes to Act 600

<u>Prior Law</u>	<u>Act 30 (SB 16)</u>
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#### Surviving Spouse Benefit - After Retirement or Retirement Eligibility

Benefit is optional. Benefits are paid to the widow until death or remarriage. Benefits are then paid to the children under the age of 18.	Three primary benefit changes occurred. <ul style="list-style-type: none"> <li>Makes the surviving spouses benefit mandatory</li> <li>It removed the term “remarries” so the surviving spouse can continue to receive a benefit if they remarry.</li> <li>Allows a college student to receive benefits until age 23</li> </ul>
The amount of surviving spouses benefit is 50% of the pension the retiree was receiving or would have been receiving at the time of his death.	The benefit level has been revised to be “no less than” 50%.
	<b>Note:</b> The above section of the legislation mandates that the survivor benefit also be paid to spouses of retirees who died before this act was signed and had not remarried by the effective date of the Act.

#### Surviving Spouse Benefit - Before Retirement Eligibility

For the spouse to receive a monthly benefit the member had to be either eligible to receive a monthly benefit or actually receiving the monthly benefit on the day of his death.	The spouse of any member who dies after reaching the service requirement for vesting would be eligible to receive a benefit starting at what would have been the officer’s earliest retirement date, based on the plan provisions in effect at the time of his death.
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#### Disability Benefits - Service-Connected and Total and Permanent

Mandatory for police officers who were “unable to perform the usual and customary duties of a police officer”. The amount of the benefit was determined at the local level.	The benefit level will be “...no less than 50 percent of the members salary at the time the disability.” It also includes a Social security offset under certain conditions.
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#### Killed-in-Service Death Benefit

The benefit is optional and the amount of the benefit is determined at the local level.	The benefit is mandatory and the benefit level shall be calculated at 100 percent of the member’s salary at the time of death.
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#### Employee Contributions

Annually, a municipality could reduce or eliminate employee contributions if an actuarial study showed that contributions by the governing body were not necessary to keep the plan actuarially sound. This meant that if the municipality was required to contribute to the plan from the general fund, employee contributions could not be reduced or eliminated.	The requirement that employee contributions could not be reduced or eliminated if the municipality made contributions to the plan from the general fund has been removed. Language requiring an annual study was eliminated.
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