Virginia Retirement System
2007 Fiscal Impact Statement

1. **Bill Number** HB 2956

House of Origin	☒ Introduced	☐ Substitute	☐ Engrossed
Second House	☐ In Committee	☐ Substitute	☐ Enrolled

2. **Patron** Bell

3. **Committee** Appropriations

4. **Title** Virginia Retirement Plan; defined contribution plan.

5. **Summary/Purpose:**

Virginia Retirement System; defined contribution plan. Creates a new defined contribution plan for all employees who enter on or after July 1, 2007, into any position covered by any retirement plan administered by the Virginia Retirement System. New employees would have 90 days after entering into such a position to elect to participate in the defined contribution plan or the retirement plan for which he is otherwise eligible.

6. **No Fiscal Impact (or)**
Fiscal Impact Estimates are: Start-up and ongoing costs of this bill will include the procurement and monitoring of third party administrators, legal expenses for developing and maintaining plan documents, educational materials for new members, training of employers, and other costs associated with the establishment and maintenance of a DC plan. However, depending upon certain plan design features and whether the Board is given authority to assess fees to employer/employees, these costs could be covered from various sources including reversions of nonvested contributions, membership fees charged to employers, and recordkeeping fees charged to employee accounts.
Estimated Administrative Costs:
FY08 Start-up Costs: $418,000 NGF 1 FTE
FY09 Ongoing Costs $400,000 NGF 4 FTE

7. **Budget amendment necessary:** Yes. Initial establishment of a defined contribution plan requires significant administrative costs. Assuming that start-up and ongoing costs could be covered as described above, they could be funded by DC plan reversions and administrative fees. An increase in the VRS Maximum Employment Level (MEL) would also be necessary to hire staff to manage the program and oversee the third party administrator.

8. **Fiscal implications:** This Bill allows the VRS Board of Trustees to set the level of contributions into the defined contribution (DC) plan. In other DC plans, the General Assembly has set the contribution rate at 10.4% of pay. This bill leaves the employer contribution rate to be set by the Board, meaning that a rate of less than 10.4% would be allowable. The ultimate impact on total costs to the Commonwealth will be a function of the employer contribution rates for the new plan as established by the Board and the proportion of new employees that elect the plan.

According to the VRS actuary at Wachovia Retirement Services, the normal cost rate for the DB plan is likely to rise in the first few years of the plan because of "adverse selection" by younger employees who are most likely to select the DC plan. If new and younger entrants (new hires) tend to select the DC plan and older new entrants tend to select the DB plan, then future DB rates will increase as the DB plan is left to serve older members and its future liabilities are spread over a shrinking payroll base.

The actuary estimates that the impact on contribution rates for localities will be similar to the impact upon the state funded plans.

9. **Specific agency or political subdivisions affected:** VRS and participating employers

10. **Technical amendment necessary: Yes**. In order for the Board of Trustees of the Virginia Retirement System to establish a Defined Contribution Plan (DCP) the following areas should be addressed in the bill:

Eligibility to Participate:
Current language stipulates that "any position" is eligible for DC Plan coverage. Clarification of whether employees who currently have a DC Plan choice (college faculty, political appointees, and school superintendents) should be allowed another DC Plan choice is necessary.

Vesting Schedule and Reversions of Forfeited Funds:
Current language does not provide for a vesting provision or the reversion of forfeited contributions upon termination prior to the vesting date. A vesting schedule, coupled with reversion of a portion of contributions, should be considered to reduce cost of new DC plan.

Administrative Fees:
VRS will need a revenue source to cover administrative costs of monitoring third party administrators, legal expense of maintaining plan documents, educational materials for new members, training of employers and other costs directly related to the development and maintenance of this new program. Typically, DC plans allow charges to employers and to members for covering administrative costs. Reversions can also be used to defray administrative costs or to reduce future employer contributions but may not be sufficient to fully cover the costs.

Employer Contributions:
Current language requires contributions to a DC Plan to be made from the "Commonwealth". However, local governments, school boards, and other political subdivisions should make contributions on behalf of their own employees. Language should be broadened to allow contributions from all employers.

Restrictions on Dual Coverage:
Current language does not preclude a member from earning a benefit from a DC plan while also receiving a benefit from another plan administered by the VRS other than a survivor benefit.

Limitations on Election to Join a Retirement Plan and Switching Between Plans:
Current language does not require an employee's election of a retirement plan to be irrevocable. Some limit on "switchbacks" should be included to avoid adverse selection.

Current language allows 90 days for new hires to choose a retirement plan, during which time no coverage is provided. Perhaps new hires should be allowed to make a choice or be defaulted in a plan immediately upon employment with a one-year window of opportunity to switch to the other plan. This would avoid any gap in initial coverage.

Current language does not provide for automatic enrollment in a default plan should an employee fail to make an election. Perhaps the DB plan should be the default plan if a new hire fails to make an election. Allowing a transfer from a DB plan to a DC plan is administratively simpler and less costly.

Language should provide for transferring funds and service credits between plans when a member chooses to switch. Switching from a DC plan to a DB plan should be actuarially cost neutral.

Enactment Clause:
The VRS is requesting an enactment clause that would delay implementation of this legislation for at least one year to allow sufficient time to develop the plan design, plan documents, education and training materials for employers and employees, procurement of a third party administrator and the selection of investment options.

Such a delayed implementation date would allow the VRS to plan and implement the consolidation of similar VRS DC plans under one consolidated plan document for ease of administration and reduction of administrative costs.

11. **Other comments:** The Joint Legislative Audit and Review Commission (JLARC) recently initiated a comprehensive study of employee compensation and will address the types of retirement plans that should be available to public employees.

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