

Virginia Retirement System 2007 Fiscal Impact Statement

1. Bill Number HB 1941

House of Origin ☒ Introduced ☐ Substitute ☐ Engrossed

Second House ☐ In Committee ☐ Substitute ☐ Enrolled

2. Patron Purkey

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 retirement plan for all employees who begin employment on or after July 1, 2008, in lieu of participating in any other retirement plan administered by the Virginia Retirement System. Other employees already enrolled in a VRS plan would be allowed to switch to the new plan immediately upon passage of the bill.

6. 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: The contribution rates for the defined contribution (DC) plan will be set by the General Assembly. In other DC plans, the General Assembly has set the contribution rate at 10.4% of pay. The ultimate impact on total costs to the Commonwealth will be a function of the employer contribution rate for the new plan as established by the General Assembly 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.

Limitations on Election to Join a Retirement Plan and Switching Between Plans:

For members hired before July 1, 2008, the General Assembly may wish to consider additional language that would allow for a plan to plan transfer of a member's Defined Benefit assets to the member's Defined Contribution account.

The election to move to the Defined Contribution Plan for member's hired prior to July 1, 2008 should provide for a specific open enrollment period and should be irrevocable.

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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.

Date: 01/19/07/pas
Document: HB1941