Virginia Retirement System
2012 Fiscal Impact Statement

1. **Bill Number:** SB498

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

2. **Patron:** Watkins

3. **Committee:** Finance

4. 4. **Title:** Virginia Retirement System; optional defined contribution and defined benefit retirement program.

5. **Summary:** Virginia Retirement System; optional defined contribution and defined benefit retirement program. Creates a new hybrid retirement program, administered by the Virginia Retirement System, that contains a defined contribution and a defined benefit component. All new state and local employees commencing employment on or after the January 1, 2014 effective date of the bill would make an irrevocable election to participate in the hybrid plan or the traditional defined benefit retirement plan. Employees in-service on December 31, 2013 would be given the opportunity to make a one-time, irrevocable election to participate in the new hybrid program. The hybrid program would not be available to members of the Judicial Retirement System, Virginia Port Authority employees, political appointees, school board superintendents, employees of the Virginia Outdoors Foundation, or employees currently eligible for optional retirement plans.

6. **Budget Amendment Necessary**: Yes. While this bill does have significant costs associated with systems development, these cannot be ascertained at this time. The ability to accurately predict costs is complicated because VRS is replacing its current technology systems. As a result, legislative changes will likely need to be made to both the current and the future systems, depending on the effective date of the legislation. The introduction of significant changes at this time will likely cause a delay in the overall project schedule, resulting in additional payments to the vendor. Further, the cost for implementing a single piece of legislation cannot be calculated precisely due to economies of scale. The actual cost to implement all legislation enacted during a given session will more than likely be less than the sum of the costs attributed to individual bills. Therefore, VRS is not providing specific systems costs for this bill, but will calculate the total for all VRS bills once they have been acted upon favorably in both houses and prior to the conference committee report.

   Additional estimated costs to implement this bill that are not related to systems development are $1.3 million. These estimated costs include actuarial calculator updates, revising and reprinting all VRS publications and the web site, legal and compliance costs, additional positions for the customer contact center due to increased call volume, training and design personnel, third-party administrator costs, and RFP costs.

7. Fiscal Impact Estimates:

SB 498 creates a new optional hybrid retirement plan with a defined benefit retirement plan component and a defined contribution retirement plan component for all state employees and local employees except judges and employees currently eligible for optional retirement plans. The plan will be available beginning January 1, 2014.

Table 1 is a 10 year projection of the estimated changes to contribution rates assuming 20% of new hires during each of the first 20 years of the plan's implementation and 5% of current non-vested employees elect the hybrid plan.

Change in projected contribution rates due to addition of Hybrid Plan										
	TABLE 1									
	Effect when Contributing Minimum Contribution to DC Plan									
Fiscal Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
State	-0.01%	0.01%	-0.12%	-0.10%	-0.25%	-0.24%	-0.37%	-0.35%	-0.45%	-0.44%
Teachers	0.02%	0.04%	-0.02%	0.00%	-0.07%	-0.06%	-0.12%	-0.11%	-0.15%	-0.14%
SPORS	0.10%	0.10%	-0.10%	0.00%	-0.09%	-0.18%	-0.09%	0.00%	-0.26%	-0.25%
VALors	0.05%	0.08%	-0.02%	-0.05%	-0.14%	-0.16%	-0.20%	-0.24%	-0.30%	-0.31%
	Effect when Contributing Maximum Contribution to DC Plan									
Fiscal Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
State	0.09%	0.13%	0.03%	0.07%	-0.06%	-0.03%	-0.14%	-0.11%	-0.20%	-0.17%
Teachers	0.10%	0.14%	0.10%	0.14%	0.08%	0.11%	0.06%	0.09%	0.06%	0.08%
SPORS	0.20%	0.19%	0.00%	0.19%	0.09%	0.00%	0.09%	0.18%	-0.09%	0.00%
VALors	0.26%	0.30%	0.20%	0.19%	0.12%	0.11%	0.07%	0.07%	0.00%	0.02%

Table 2 shows the estimated savings from the General Fund over the next 20 years by biennium.

Projected Savings by Biennium - General Fund										($Millions)	
	TABLE 2										
	Assuming Minimum Contribution to DC										20 Year
	FY 15/16	FY 17/18	FY 19/20	FY 21/22	FY 23/24	FY 25/26	FY 27/28	FY 29/30	FY 31/32	FY 33/34	Total
State	$ (0.07)	$ 3.27	$ 7.51	$ 11.07	$ 13.78	$ 16.17	$ 17.85	$ 19.18	$ 20.28	$ 21.27	$ 130.30
Teachers	$ (1.69)	$ 0.51	$ 3.38	$ 5.98	$ 7.68	$ 8.97	$ 10.21	$ 11.58	$ 12.46	$ 13.32	$ 72.40
SPORS	$ (0.16)	$ 0.08	$ 0.23	$ 0.08	$ 0.44	$ 0.56	$ 0.61	$ 0.65	$ 0.68	$ 0.83	$ 3.99
VALors	$ (0.40)	$ 0.23	$ 0.94	$ 1.39	$ 1.92	$ 2.21	$ 2.47	$ 2.70	$ 2.73	$ 2.86	$ 17.06
Total	$ (0.64)	$ 3.57	$ 8.68	$ 12.53	$ 16.14	$ 18.94	$ 20.93	$ 22.52	$ 23.69	$ 24.96	$ 151.35
	Assuming Maximum Contribution to DC										20 Year
	FY 15/16	FY 17/18	FY 19/20	FY 21/22	FY 23/24	FY 25/26	FY 27/28	FY 29/30	FY 31/32	FY 33/34	Total
State	$ (3.36)	$ (1.53)	$ 1.47	$ 3.93	$ 5.68	$ 7.41	$ 8.43	$ 9.23	$ 9.84	$ 10.42	$ 51.50
Teachers	$ (6.19)	$ (6.15)	$ (5.06)	$ (3.96)	$ (3.67)	$ (3.52)	$ (3.45)	$ (3.18)	$ (3.30)	$ (3.50)	$ (41.97)
SPORS	$ (0.33)	$ (0.16)	$ (0.08)	$ (0.23)	$ 0.07	$ 0.14	$ 0.13	$ 0.13	$ 0.12	$ 0.30	$ 0.11
VALors	$ (1.75)	$ (1.22)	$ (0.73)	$ (0.42)	$ (0.07)	$ 0.13	$ 0.24	$ 0.40	$ 0.38	$ 0.47	$ (2.56)
Total	$ (5.45)	$ (2.91)	$ 0.67	$ 3.28	$ 5.68	$ 7.68	$ 8.80	$ 9.76	$ 10.35	$ 11.18	$ 49.05

Both charts contain two scenarios: the first assumes the employer match to the DC plan is based on the minimum required amount of 1.5%, while the second scenario assumes the maximum 3.5% employer match is contributed to the DC plan. Payroll growth is assumed to remain flat throughout the projection period.

8. **Fiscal Implications:** An employer's contribution rate for the defined benefit plan will be adjusted to include the annual contribution rate for the defined benefit portion of the hybrid plan for employees who enroll in that plan. The plan design changes in SB 498 are assumed to apply to only a small demographic of new hires and current members. The savings are based on the assumption that 20% of new hires during each of the first 20 years of the plan's implementation, and 5% of current employees as of January 1, 2014, will elect to participate in this plan. As a result, the reductions in costs associated with this plan design will only be realized as more members elect this new benefit structure. While initial cost savings associated with the plan design changes will be minimal, they will serve to reduce the ongoing or normal cost of the plan and help to contain employer costs for these plans going forward. Because the existing defined benefit plan is not being closed in order to implement the hybrid plan, the more significant contribution rates that would result from a complete shift to a defined contribution plan are not incurred.

9. **Specific Agency or Political Subdivisions Affected:** VRS, employers and all state and local employees, including hazardous duty and school division employees, who are eligible for and opt into the hybrid program.

10. **Technical Amendment Necessary:** No

11. **Other Comments:** This bill creates a new optional hybrid retirement plan to be administered by VRS that includes both a defined benefit and a defined contribution component. A number of other states have recently adopted hybrid retirement plans in various forms. States that administer some form of hybrid plans as a mandatory or optional

primary retirement benefit for broad classes of employees include Georgia, Indiana, Ohio, Michigan, Oregon, Utah, and Washington.[1]

Under this legislation, an employee's election to enroll in the optional hybrid program is irrevocable. Employees hired on or after January 1, 2014 will have 60 days to make an election between the VRS defined benefit program or the hybrid program. The default option for any eligible employee not making an election within the specified time will be the VRS defined benefit plan. Employees in service as of December 31, 2013 will have until April 30, 2014 to make an election to participate in the hybrid plan.

Proposed Optional Hybrid Defined Benefit and Defined Contribution Schedule:

Employer Contribution	Employee Contribution
To DB: determined actuarially	To DB: 4% (mandatory)
To DC: 1.5% (mandatory)	To DC: 3% (mandatory)
To DC: 100% of next .05%	To DC: .05% (optional)
To DC: 100% of next .05%	To DC: .05% (optional)
To DC: 100% of next .05%	To DC: .05% (optional)
To DC: 100% of next .05%	To DC: .05% (optional)
MANDATORY CONTRIBUTION TO DC: 1.5% CONTRIBUTION BASED ON OPTIONAL EMPLOYEE CONTRIBUTIONS: 2.0% TOTAL POSSIBLE EMPLOYER CONTRIBUTION: 3.5% (NOT INCLUDING ACTUARIALLY DETERMINED DB EMPLOYER CONTRIBUTION)	MANDATORY CONTRIBUTION TO DB: 4% MANDATORY CONTRIBUTION TO DC: 3% OPTIONAL CONTRIBUTIONS TO DC TO GET FULL EMPLOYER MATCH: 2% TOTAL POSSIBLE EMPLOYEE CONTRIBUTION: 9%

Vesting of the employer contributions to the defined contribution component would begin at 20% after the first year of continuous participation in the program, increasing by an additional 20% per year until full vesting at the end of the fifth year of continuous participation. If an employee terminates employment with an employer prior to achieving 100% vesting, contributions made by an employer on behalf of the employee that are not vested will be forfeited. No loans or hardship withdrawals may be made from the employer or employee contributions to the defined contribution component. The Commonwealth's Cash Match Plan (currently $20 per pay period maximum based on a $40 per pay period contribution to the 457 Plan) will only begin to provide an employer match under this program when the hybrid plan participant's contributions exceed the maximum voluntary participant contribution allowed in the defined contribution component of the hybrid plan.

[1] NASRA ISSUE BRIEF: State Hybrid Retirement Plans, November 22, 2011, http://www.nasra.org/resources/HybridBrief.pdf

The defined benefit component has a 1.0 multiplier. Members transferring to the new hybrid plan will have their creditable service as of the date of the transfer applied to the multiplier in effect prior to the transfer in calculating the DB benefit; the 1.0 multiplier will apply to all future service earned subsequent to the transfer to the hybrid plan. SPORS and VaLORS members who transfer to the new hybrid plan will not be eligible for earlier retirement provisions or for the Social Security supplement.

A new Disability Program for Political Subdivision Employees is available for local employees participating in the hybrid plan if the locality elects to participate in the program. Participants in the hybrid plan would also be eligible for group life and the health insurance credit program.

Currently the member contribution amount is 5% for the existing defined benefit retirement plan. This bill would allow employees an option to select a retirement plan that would require a different contribution amount, absent a parallel and concurrent change in the amount of the existing defined benefit plan member contribution. Allowing employees to choose between two plans with different mandatory contribution amounts could be considered a prohibited cash or deferred arrangement as there is uncertainty at this point over the Internal Revenue Service's interpretation of employee "pick-up" rules under Section 414(h) of the Internal Revenue Code.

Date: 1-25-12
Document: SB498.DOC