

Virginia Retirement System 2015 Fiscal Impact Statement

1. Bill Number: SB977

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

2. Patron: Ruff

3. Committee: Finance

4. Title: Virginia Sickness and Disability Program; open enrollment period.

5. Summary: Opens the enrollment into the Virginia Sickness and Disability Program from October 1, 2015, through January 1, 2016 for eligible employees not currently participating in the program. Any employee electing to participate in the program would convert his sick leave balances to (i) additional retirement service credit on the basis of one month of service for each 173 hours of sick leave or (ii) disability credits on the basis of one hour of disability credit for each hour of sick leave. An election to participate in the program must be in writing and is irrevocable.

6. Budget Amendment Necessary: Yes. VRS estimates that one-time implementation costs of approximately \$89,000 will be necessary for systems changes and testing.

7. Fiscal Impact Estimates: This bill provides eligible employees the opportunity to elect participation in the Virginia Sickness and Disability Program (VSDP) if not already participating. Eligible employees are defined pursuant to § 51.1-1100 and include state employees, members of the State Police Officers' Retirement Plan, members of the Virginia Law Officers' Retirement Plan and certain employees of institutions of higher education who are not participants in an optional retirement plan for higher education. The bill would allow an electing member to convert accumulated sick leave to VRS service credit at a rate of one month for every 173 hours of sick leave or to convert sick leave balances to disability credits. There are approximately 13,000 employees not currently participating in VSDP who would be eligible to make the election. Exhibit 1 below shows the average age and service of these employees by employer group.

Exhibit 1

Employer	Count	Average Age	Average Service	Average Sick Leave Balance
State	10,795	56	26.4	1,400
SPORS	593	51	27.0	1,757
VaLORS	1,176	51	22.9	1,450
Total	12,564	56	26.1	1,422

VRS is unable to predict how many of the eligible employees would elect to enroll in VSDP and convert accumulated sick leave, but we would expect some adverse selection, particularly with those members who have large sick leave balances and who are already eligible to retire with unreduced benefits. Some members may also elect to move to VSDP due to the long-term disability benefit. Approximately 43% of the employees who would be eligible for the election will already meet the service requirements for an unreduced retirement at the proposed election date, even before adding the additional service converted from sick leave. Nearly 75% of the eligible employees already meet the requirements for a reduced retirement.

Although the proposed bill would provide an actuarial gain in disability coverage for any member who elected to convert to VSDP under the proposed bill, the increase in liability associated with converting the sick leave balance to pension service would erase any savings and ultimately increase costs by generating additional unfunded liability. Pre-funding assumes that contributions along with investment income will be used to pay for future retirement benefits. Since nearly 75% of these eligible employees are already eligible for retirement, there is not enough time to accumulate investment income to pay for the increased benefits. Without an immediate contribution to cover the increase in plan liability, the new unfunded liability will need to be paid by the next generation of taxpayers.

VRS also expects that there would be minor impacts to costs associated with the Health Insurance Credit (HIC) Program and Group Life Insurance (GLI) Program due to the accelerated retirement eligibility of some members, but we expect these impacts to be less significant than the conversion of sick leave to pension service.

The average sick leave balance for all those impacted is approximately 1,400 hours for employees who opted out of VSDP, which would equate to about 8 months of additional service if converted to service credit.

Below, VRS provides cost estimates under two scenarios. The first scenario assumes that 50% of all eligible employees elect to enroll in VSDP, while the second scenario assumes a 100% election rate. The cost estimates are based on data, actuarial assumptions, and methods from the June 30, 2014 actuarial valuation.

50% Election Rate

	<u>FY15 Cost</u>	<u>FY16 Cost</u>	<u>FY17 Cost</u>	<u>FY18 Cost</u>	<u>FY19 Cost</u>	<u>FY20 Cost</u>
State - General Fund	\$ -	\$ 2,844,000	\$ 2,844,000	\$ 2,844,000	\$ 2,844,000	\$ 2,844,000
SPORS - General Fund	-	670,000	670,000	670,000	670,000	670,000
VaLORS - General Fund	-	1,094,000	1,094,000	1,094,000	1,094,000	1,094,000
JRS - General Fund	-	-	-	-	-	-
Teacher - General Fund	-	-	-	-	-	-
TOTAL General Fund	<u>\$ -</u>	<u>\$ 4,608,000</u>				
State - Non-General Funds	\$ -	\$ 3,709,000	\$ 3,709,000	\$ 3,709,000	\$ 3,709,000	\$ 3,709,000
SPORS - Non-General Funds	-	116,000	116,000	116,000	116,000	116,000
VaLORS - Non-General Funds	-	106,000	106,000	106,000	106,000	106,000
TOTAL - Non-General Funds	<u>\$ -</u>	<u>\$ 3,931,000</u>				
Teacher - Local Funds	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Political Subdivisions - Local Funds	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
TOTAL Local Funds	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Grand Totals	<u>\$ -</u>	<u>\$ 8,539,000</u>				

Estimated projections based on employee data and valuation results as of June 30, 2014 and assume a level population throughout projection period.

Payroll projections are assumed to remain level throughout projection period.

The immediate increase in unfunded liability that would result from this legislation, assuming a 50% election rate, is expected to be approximately \$72.8 million.

100% Election Rate

	<u>FY15 Cost</u>	<u>FY16 Cost</u>	<u>FY17 Cost</u>	<u>FY18 Cost</u>	<u>FY19 Cost</u>	<u>FY20 Cost</u>
State - General Fund	\$ -	\$ 4,182,000	\$ 4,182,000	\$ 4,182,000	\$ 4,182,000	\$ 4,182,000
SPORS - General Fund	-	996,000	996,000	996,000	996,000	996,000
VaLORS - General Fund	-	1,640,000	1,640,000	1,640,000	1,640,000	1,640,000
JRS - General Fund	-	-	-	-	-	-
Teacher - General Fund	-	-	-	-	-	-
TOTAL General Fund	\$ -	\$ 6,818,000				
State - Non-General Funds	\$ -	\$ 5,455,000	\$ 5,455,000	\$ 5,455,000	\$ 5,455,000	\$ 5,455,000
SPORS - Non-General Funds	-	172,000	172,000	172,000	172,000	172,000
VaLORS - Non-General Funds	-	158,000	158,000	158,000	158,000	158,000
TOTAL - Non-General Funds	\$ -	\$ 5,785,000				
Teacher - Local Funds	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Political Subdivisions - Local Funds	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
TOTAL Local Funds	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Grand Totals	\$ -	\$ 12,603,000				

Estimated projections based on employee data and valuation results as of June 30, 2014 and assume a level population throughout projection period.

Payroll projections are assumed to remain level throughout projection period.

The immediate increase in unfunded liability that would result from 100% of the eligible members converting their sick leave to service credit is expected to be approximately \$108.6 million.

The above costs do not take into account any offset of potential payout by employers for unused sick leave at time of retirement. This payout is for up to 25% of sick leave and is capped at \$5,000.

- 8. Fiscal Implications:** Allowing the conversion of accumulated sick leave to retirement service credit would enable eligible employees who take advantage of the opportunity to retire earlier. In some cases, long-term employees have accrued several years of sick leave. Any employee with at least 15 years of service who retires earlier than expected will also begin to receive a health insurance credit (HIC) earlier than expected. All eligible members will have at least 15 years of service. Accelerated retirement eligibility generally increases the unfunded liabilities since contributions were not collected for the relevant period of service credit.

9. Specific Agency or Political Subdivisions Affected: VRS and all VRS participating employers with eligible employees.

10. Technical Amendment Necessary: Yes. VRS suggests that for administrative simplicity the effective date for all members who opt into VSDP be the same date instead of staggered dates based on the actual date of the member's election.

Line 24, after "before" change "January 1, 2016" to December 1, 2015.

Lines 28 and 29, delete "the first day of the pay period following the delivery of the notice of election to the Retirement System."

Line 28, after "shall be" insert January 1, 2016.

11. Other Comments: To date there have been two election periods related to VSDP participation. The initial election was an opt-in period from January 1, 1999 through March 31, 1999. The second election period, which gave non-participating employees an opportunity to opt out of VSDP, was from October 1, 2002 through January 1, 2003. This legislation would allow any eligible employee who is not a VSDP participant as of September 30, 2015, to elect to participate in VSDP. The election must be in writing, would be irrevocable, and must be received by VRS between October 1, 2015, and January 1, 2016. The effective date of participation for any eligible employee electing participation pursuant to this bill will be the first day of the first pay period following the delivery of the election notice to VRS. (Please see suggested amendments.) Upon election, a member may convert his or her accumulated sick leave to retirement service credit at a rate of one month of service credit for 173 hours of sick leave or convert his or her sick leave balance to disability credits. SB 977 does not limit the amount of sick leave that can be converted. However, any conversion must take place as of a member's effective date of VSDP participation.

Current law (§ 51.1-142.2(D)) allows any member in service to purchase service credit for accumulated sick leave upon retirement but only in the amount the employer may provide as payment for unused sick leave. The member is required to pay the actuarial equivalent of the cost of any service purchased under this provision. DHRM policy 4.55 allows eligible employees with at least five years of continuous salaried state service who separate from state service to be paid for up to 25% of their accrued sick leave balance up to a maximum of \$5,000.

Below are two examples of the cost impact to the VRS under the proposed bill.

The first example shows the impact for a SPORS member already eligible for retirement who has 1,200 hours of accumulated sick leave. The 1,200 hours of sick leave converts to 6 additional months of service:

Employee Age at Retirement	50		
Years of Benefit Service	25		
Average Final Compensation	\$85,000		
Accumulated Sick Leave Balance	1200 Hours		
Current Value of Retirement Benefit and Unused Sick Leave at Retirement Date			
Annual Retirement Benefit	Payout of Unused Sick Leave	Present Value of Retirement Benefit at Retirement	Total Value Retirement and Sick Leave Payout
\$ 27,625	\$ 5,000	\$ 458,800	\$ 463,800
Value of Retirement Benefit and Unused Sick Leave under proposed legislation at Retirement Date - Accumulated Sick Leave is converted to 6 months of additional benefit service			
Annual Retirement Benefit	Payout of Unused Sick Leave	Present Value of Retirement Benefit at Retirement	Total Value Retirement and Sick Leave Payout
\$ 28,178	\$ -	\$ 467,800	\$ 467,800
The net increase in payout is approximately \$4,200			

The second example shows the impact for a SPORS member who has 3,600 hours of accumulated sick leave. The 3,600 hours of sick leave converts to 1 year and 8 months of additional service:

Employee Age at Retirement	50		
Years of Benefit Service	25		
Average Final Compensation	\$85,000		
Accumulated Sick Leave Balance	3600 Hours		
Current Value of Retirement Benefit and Unused Sick Leave at Retirement Date			
Annual Retirement Benefit	Payout of Unused Sick Leave	Present Value of Retirement Benefit at Retirement	Total Value Retirement and Sick Leave Payout
\$ 27,625	\$ 5,000	\$ 458,800	\$ 463,800
Value of Retirement Benefit and Unused Sick Leave under proposed legislation at Retirement Date - Accumulated Sick Leave is converted to 1 year 8 months of additional benefit service			
Annual Retirement Benefit	Payout of Unused Sick Leave	Present Value of Retirement Benefit at Retirement	Total Value Retirement and Sick Leave Payout
\$ 29,487	\$ -	\$ 489,200	\$ 489,200
The net increase in payout is approximately \$26,600			

SB 738 and HB 1883 are similar to this bill, but both restrict open enrollment into VSDP to members of the State Police Officers' Retirement Plan and do not provide for the conversion of sick leave to disability credits.

Date: 1-20-15

Document: SB977.DOC