Virginia Retirement System
2018 Fiscal Impact Statement

1. **Bill Number:** SB 498

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

2. **Patron:** Carrico

3. **Committee:** Finance

4. **Title:** Retirement benefits for local law-enforcement officers; participation by certain political subdivisions.

5. **Summary:** Requires a locality that participates in the Virginia Retirement System and that has two or fewer public safety officers eligible for enhanced hazardous duty retirement benefits to provide such benefits for such employees. The Commonwealth would fund one-half the cost of such benefits for those localities.

6. **Budget Amendment Necessary**: Yes.

   Item 488. VRS would need a NGF appropriation for implementation costs of approximately $450,000. The costs are primarily for systems modifications and communications. This legislation would have high implementation costs as it affects complex processes, including the process by which employers report contributions. Additionally, it impacts retirements and disbursements, processes which are being developed for a systems upgrade release currently scheduled for October 2018.

   Item 474. A GF appropriation of $93,500 would also be necessary for the Commonwealth's share of the cost.

7. **Fiscal Impact Estimates:** Eighteen localities were identified that could be impacted by SB 498. Twelve of the localities currently have not elected to provide enhanced hazardous duty benefits, while six localities currently provide enhanced coverage for hazardous duty members. Table 1 provides an overview of the eighteen localities. Note that the column labeled "Total Active Employees" refers to all of the employees covered by VRS benefits in that locality. "Active Hazardous Duty Employees" is a subset of the total number of employees who may be serving in hazardous duty positions. Because their employers have not elected these additional benefits in all cases, these employees serving in hazardous duty positions are generally not currently covered by enhanced hazardous duty benefits.

Table 1

	Employer	Total Active Employees	Estimated Active Hazardous Duty Employees	Current Plan - 6/30/17 Valuation: Unfunded Actuarial Accrued Liability	Funded Status
No Enhanced Hazardous Duty Coverage Provided	55203 (Town of St. Paul)	20	2	$745,331	74.86%
	55218 (Town of Craigsville)	5	1	$189,910	65.02%
	55243 (Town of Rural Retreat)	10	1	$55,845	91.85%
	55248 (Town of Pennington Gap)	24	2	($161,211)	117.34%
	55249 (Town of La Crosse)	4	1	($125,718)	149.91%
	55252 (Town of Windsor)	12	2	($9,779)	101.08%
	55311 (Town of Brookneal)	9	1	$416,416	75.83%
	55338 (Town of Quantico)	3	1	($146,706)	128.23%
	55372 (Town of Weber City)	4	2	$175,956	80.28%
	55380 (Town of Independence)	12	2	$610,016	66.42%
	55390 (Town of Parksley)	5	1	$42,707	94.33%
	55399 (Town of Blackstone)	55	2	($760,273)	110.66%
Enhanced Hazardous Duty Coverage Provided	55228 (Town of Middletown) *	10	1	($126,208)	121.27%
	55245 (Town of Scottsville) *	4	2	$94,707	81.38%
	55250 (Town of Rich Creek) *	6	1	($18,896)	105.24%
	55254 (Town of Stephens City) **	7	2	$645,458	65.55%
	55374 (Town of Hurt) **	4	2	$322,080	65.67%
	55378 (Town of Courtland) *	2	1	($188,692)	143.95%

* Enhanced Hazardous Duty 1.70% Multiplier and Supplement

** Enhanced Hazardous Duty 1.85% Multiplier and Supplement

There is currently no systematic tracking of employees who serve in hazardous duty roles with employers that participate in VRS, but whose employers have not elected enhanced hazardous duty benefits for these employees. The localities in the table above were manually identified through a combination of reviewing employer reporting records and the VRS-administered LODA fund rosters. As this was a manual review and employers may identify these types of employees differently, additional affected localities and employees may exist.

SB 498 would require that employers provide enhanced hazardous duty coverage to eligible active hazardous duty members, which would include the 1.85% benefit multiplier and the enhanced hazardous duty supplement. The enhanced benefit provisions would apply retroactively to all hazardous duty service of eligible members. The expected annual cost to provide these benefits to the 18 localities is estimated at $187,000, with half of the amount, or approximately $93,500, payable by the Commonwealth. Under current law, employers with eligible hazardous duty employees are able to elect enhanced hazardous duty coverage under the provisions of Va. Code § 51.1-138. Employers may elect enhanced coverage, which provides the hazardous duty supplement, with either the 1.7% or 1.85% benefit multiplier. As of June 30, 2017, 222 localities had elected enhanced hazardous duty coverage with approximately 58% of the employers electing the 1.7% multiplier along with the supplement. SB 498 specifically states that the 1.85% multiplier would be provided. Table 2 provides the estimated total cost for each of the identified localities, which also includes increasing the multiplier to 1.85% for four of the six employers that had already elected enhanced hazardous duty coverage with the 1.7% multiplier. The provisions of the bill require that these estimated costs be split between the locality and the Commonwealth.

Table 2

Employer	Annual Cost Associated with SB 498
55203 (Town of St. Paul)	$6,300
55218 (Town of Craigsville)	$7,600
55243 (Town of Rural Retreat)	$10,700
55248 (Town of Pennington Gap)	$6,500
55249 (Town of La Crosse)	$18,900
55252 (Town of Windsor)	$5,700
55311 (Town of Brookneal)	$12,200
55338 (Town of Quantico)	$10,500
55372 (Town of Weber City)	$11,400
55380 (Town of Independence)	$25,400
55390 (Town of Parksley)	$4,600
55399 (Town of Blackstone)	$10,500
55228 (Town of Middletown) *	$2,200
55245 (Town of Scottsville) *	$12,200
55250 (Town of Rich Creek) *	$2,100
55254 (Town of Stephens City) **	$32,500
55374 (Town of Hurt) **	$6,500
55378 (Town of Courtland) *	$1,200
Total	$187,000

* Enhanced Hazardous Duty 1.70% Multiplier and Supplement

** Enhanced Hazardous Duty 1.85% Multiplier and Supplement

While the coverage provided is only for a small number of members, it is important to note that unexpected changes due to events such as early retirements and disabilities can have a more dramatic impact on the cost of benefits for employers with a smaller number of members. Since this benefit is applied to prior service, most employers will have additional unfunded liability associated with the enhanced benefits that will need to be paid for even after members retire.

7) **Fiscal Impact Estimates/Expenditure and Revenue Impacts:**

a. Fiscal Impact Estimates/Expenditure Impact:

Fiscal Year	***Dollars***	***Positions***	***General Fund***	***Non-General Fund & Local Funds***
2019	$637,000	0	$93,500	$543,500
2020	$187,000	0	$93,500	$93,500
2021	$187,000	0	$93,500	$93,500
2022	$187,000	0	$93,500	$93,500
2023	$187,000	0	$93,500	$93,500
2024	$187,000	0	$93,500	$93,500

VRS costs to program for and administer the bill will depend on the process used for paying the state portion of the cost. Changes to the funding mechanism will affect programming and administration and, therefore, the cost to VRS.

8. Fiscal Implications: It is unclear how the Commonwealth would fund its 50% portion of the supplemental retirement allowance for the affected public safety officers that are contemplated by this bill, but the General Fund would absorb the expenditure impact.

VRS estimated the expenditure impact using both the hazardous duty supplement and the higher 1.85% multiplier available to the locality for election under § 51.1-138(B). While the bill will require at least 12 employers to provide the benefit, the Commonwealth would also be required to pay 50% of the enhanced benefit for the six employers who have already elected the coverage.

Currently, when a locality requests to add enhanced hazardous duty benefits, an actuarial study is required, which costs the locality $1,250 to perform. If a locality is under 70% funded at the time of the request, VRS requires that in order to increase benefits for members, the plan would need to be at least 70% funded after the impacts of the enhancements, which could require a lump sum payment to prepay the benefits and avoid further decreasing the locality's funded position. The funded status threshold is 70%, with discussions to move the level to 80% in the near future. Some of the localities affected by this legislation would, under VRS' current policy, be required to prefund the benefits to increase their funded status to at least the 70% level. The additional costs associated with required prefunding would be approximately $100,000 for the two localities impacted. The source of the funding required to prefund the benefits is not set forth in the bill and therefore somewhat uncertain, but would likely rest with the locality.

The bill also does not consider the fiscal health of the employers impacted and does not contemplate employers being unable to fund additional benefits for members. The legislation could have the effect of requiring a locality to provide benefits that the locality cannot afford and did not elect.

In 2013, VRS adopted a new funding policy for VRS-administered plans. In response to new Governmental Accounting Standards Board (GASB) requirements, a cross-over calculation was added to the funding policy, which could require an additional contribution or surcharge for certain plans that have the potential for projected cash flow requirements to exceed projected assets. Three of the plans identified as being impacted already have this additional contribution/surcharge requirement, which likely will increase under this legislation.

There will be GASB implications if the Commonwealth takes on this liability, which will have to be reflected on the state's financial statements. This arrangement could qualify as a special funding situation under GASB 68, which would require the Commonwealth to include a portion of the Net Pension Liability associated with this benefit for local employers in the Commonwealth's CAFR.

All expenditure impacts are calculated under the assumption that the bill will affect only retirements that occur on or after July 1, 2018, although the 1.85% multiplier will apply to active members' prior hazardous duty service.

9. **Specific Agency or Political Subdivisions Affected:** VRS and any locality that has two or fewer employees in positions covered by § 51.1-138(B).

10. **Technical Amendment Necessary:** Yes. VRS is requesting a delayed effective date of January 1, 2020 due to the impact the changes in this legislation would have on the employer reporting system. VRS is implementing several releases of its multi-year systems upgrade during 2018 and into 2019. A delayed effective date would prevent having to make the changes necessary to implement this legislation during this time period, which would delay these releases. Since additional releases are scheduled for March of 2019, the next feasible timeframe for a project of this size and complexity would be January 2020. See Other Comments for a discussion of items that require clarification necessary to the administration of the bill.

11. **Other Comments:** SB 498 makes changes to § 51.1-138(B), under which an employer currently may elect enhanced retirement benefits for certain public safety officers. The election involves choosing between a 1.7% multiplier and a 1.85% multiplier for the retirement benefit, plus a hazardous duty supplement currently equal to $1,132 per month and continuing until normal retirement age under Social Security. The employer may make an irrevocable election to provide either or both of these enhancements. By making either election, the normal retirement age for employees eligible for enhanced hazardous duty coverage becomes age 60 rather than 65, and employees are eligible for an unreduced benefit at age 60 with at least five years of service credit or at age 50 with at least 25 years of service credit.

    Hazardous duty employees in a locality that has elected enhanced benefits are not eligible for the Hybrid plan; those whose employers have not elected enhanced benefits and who are hired on or after January 1, 2014 are enrolled in the Hybrid retirement plan. This legislation could therefore require some employees to be moved from the Hybrid plan to Plan 2.

The bill provides that, beginning July 1, 2018, any locality participating in the Virginia Retirement System that has two or fewer employees who are employed in a position eligible for enhanced benefits under § 51.1-138 shall provide both of the enhancements to such employees. The locality and the Commonwealth are each required to fund 50 percent of the "supplemental retirement allowance" for such officers. The bill eliminates the election of the enhanced retirement benefit for any affected locality and would require them to provide the coverage and pay 50 percent of the cost.

The bill would make the Commonwealth responsible for funding half the cost of coverage for any locality with two or fewer employees eligible for enhanced hazardous duty coverage, including those that have already elected and are funding enhanced hazardous duty coverage. A portion of the costs of the coverage would shift from that locality to the General Fund of the Commonwealth. In addition and as noted above, this arrangement could qualify as a special funding situation under GASB 68, which would require the Commonwealth to include a portion of the Net Pension Liability associated with this benefit for local employers in the Commonwealth's CAFR. Further, the bill does not consider the fiscal health of the employers impacted and does not contemplate employers being unable to fund additional benefits for members.

Finally, the bill does not address whether an affected locality is required to continue providing enhanced hazardous duty coverage if there comes a time when it no longer has two or fewer affected employees (i.e., it hires a third or fourth employee eligible for enhanced hazardous duty benefits). This issue is especially important for any locality with employees who would be entitled to enhanced hazardous duty coverage under the bill but are currently in the hybrid retirement program under § 51.1-169, given the different plan structures (e.g., vesting schedules for employer contributions to the defined contribution component of the hybrid retirement program).

One approach to the implementation challenges would be to make this provision applicable only to those localities that have two or fewer employees who would be eligible for enhanced hazardous duty benefits as of July 1, 2018. If an affected locality later hired additional eligible employees, the employer would be required to provide the enhanced benefits but the Commonwealth would not be required to fund a portion of those costs. This would, however, create funding challenges for some of the localities that had not independently elected enhanced benefits for their hazardous duty employees.

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