

2022 Fiscal Impact Statement

1. Bill Number: SB 17

House of Origin ☒ Introduced ☐ Substitute ☐ Engrossed

Second House ☐ In Committee ☐ Substitute ☐ Enrolled

2. Patron: Hackworth

3. Committee: Senate Finance and Appropriations

4. Title: Virginia Retirement System; employment of retired law-enforcement officers.

5. Summary: Allows a retired law-enforcement officer to continue to receive their service retirement allowance during a subsequent period of employment by a state and local law-enforcement agency, so long as they have a break in service of at least 12 calendar months between retirement and reemployment, did not retire under an early retirement program, and did not retire under the Workforce Transition Act of 1995.

The bill also provides that the Director of the Department of Criminal Justice Services shall exempt a law-enforcement officer who has demonstrated sensitivity to cultural diversity issues, had previous experience and training as a law-enforcement officer, is currently receiving or is eligible to receive a service retirement allowance, and has a break in service of no longer than 60 calendar months between retirement and the new employment from the mandatory attendance of all courses which are required for the successful completion of the compulsory minimum training standards.

6. Summary of Impacts

Benefit(s) impacted: Continued retirement benefits for certain retirees who return to work as law enforcement officers with state or local law enforcement agencies. Continued benefits may include the “hazardous duty supplement” available to eligible members who have retired before their normal Social Security retirement age, in recognition of the physical and stressful nature of certain positions. May impact Line of Duty Act (LODA) benefits and state retiree health plan benefits.

Impact to unfunded liability (see Item 9 for details): Indeterminate. See discussion below for illustrative examples.

Impact to contribution rate(s) (see Item 9 for details): Indeterminate. Since hazardous duty employees are typically able to retire earlier than other covered employees, changes to retirement patterns may have a more significant impact on contribution rates. See discussion below.

Specific Agency or Political Subdivisions Affected (see Item 10): DCJS, VRS-participating state and local law enforcement agencies that hire retired law-enforcement officers.

VRS cost to implement (see Item 7 and Item 8 for details): Approximately \$148,200 in FY 2022, with minimal ongoing costs.

Employer cost to implement (see Item 7 and Item 8 for details): Indeterminate. DCJS indicates that no fiscal impact is expected on the agency.

Other VRS and employer impacts (see Item 7, Item 9, Item 11, and Item 12 for details): DCJS would have to opine on the impacts of the exemption. For VRS benefits, the bill may impact both retirement and other post-employment benefits (OPEB) plans. Since hazardous duty employees are typically able to retire earlier than other covered employees, rehiring retired hazardous duty employees may have additional impacts on workers' compensation benefits and Line of Duty Act (LODA) benefits.

GF budget impacts (see Item 8 for details): None at this time.

NGF budget impacts (see Item 8 for details): VRS will need a budget amendment to implement the changes.

7. **Budget Amendment Necessary:** Yes. Item 494. VRS estimates implementation costs for the bill at \$148,200 in FY 2022, with minimal ongoing costs in FY 2023 and beyond. This does not include the impact to current or future contribution rates or to the funded status of the plans, which are discussed below.

Some new programming will be required for employers to be able to enroll these retirees, to ensure that their retirement benefits are not suspended, and that service is not added to their records. This is similar to the current procedure for retirees in the teacher and bus driver critical shortage program and in the school security officer (SSO) retiree return-to-work program. A manual process for collecting employer contributions may need to be deployed until an automated solution can be fully developed, tested, and put into production.

8. **Fiscal Impact Estimates:** See Item 9, below for VRS impacts. DCJS indicates that no fiscal impact is expected on the agency.
9. **Fiscal Implications:** Allows a retired law-enforcement officer to continue to receive their service retirement allowance during a subsequent period of employment by a state and local law-enforcement agency, so long as they have a break in service of at least 12 calendar months between retirement and reemployment, did not retire under an early retirement program, and did not retire under the Workforce Transition Act of 1995. Requires employer contributions for these retirees.

Under the proposed change:

- A member who is a sworn law enforcement officer could elect to retire from VRS but return to work as a law enforcement officer after being retired for at least 12 months.
- The member would not receive any future benefit accruals while working and would not be making member contributions.
- Members electing the in-service distribution would be considered retired for pension, Group Life Insurance (GLI), Health Insurance Credit (HIC), and/or Virginia Sickness and Disability Program (VSDP) benefits.

- The member would be eligible to receive Cost of Living Adjustments (COLAs) on the service retirement benefit while receiving in-service distributions.

We expect that the proposed change will provide some incentive for members to take the in-service distribution and continue working, thereby receiving their pension benefit while also receiving pay. Below is an analysis of the plans that could be impacted by this legislation. Exhibit 1 provides the number of active hazardous duty members for each employer group and the number of members who meet the eligibility requirements to retire as of June 30, 2021. The target population would be the last two columns, which show the number of members who are already eligible to retire with an unreduced benefit as of the June 30, 2021, which ranges from 6% - 14% based on the employer group.

Exhibit 1 – Hazardous Duty Members Eligible to Retire as of June 30, 2021

Employer Group	Active Members	Eligible to Retire 6/30/21	% Eligible to Retire	Eligible for Unreduced Retirement 6/30/21	% Eligible for Unreduced Retirement
SPORS	1,947	408	21.0%	280	14.4%
VaLORS	7,823	1,548	19.8%	561	7.2%
Local LEO	25,579	4,247	16.6%	1,587	6.2%
Total HD	35,349	6,203	17.5%	2,428	6.9%

Projecting the population out four years from now, the number of members reaching retirement eligibility increases further. The target population of members eligible to retire with an unreduced benefit as of June 30, 2025 increases to 16% - 25% depending on the employer group.

Exhibit 2 – Hazardous Duty Members Eligible to Retire as of June 30, 2025

Employer Group	Active Members	Eligible to Retire by 6/30/25	% Eligible to Retire	Eligible for Unreduced Retirement 6/30/25	% Eligible for Unreduced Retirement
SPORS	1,947	633	32.5%	493	25.3%
VaLORS	7,823	2,580	33.0%	1,420	18.2%
Local LEO	25,579	7,191	28.1%	4,212	16.5%
Total HD	35,349	10,404	29.4%	6,125	17.3%

In order to evaluate the impact of allowing a retired law-enforcement officer to continue to receive their service retirement allowance during a subsequent period of employment by a state or local law-enforcement agency, so long as they have a break in service of at least 12 calendar months between retirement and reemployment, we modeled an increase in

retirement rates of 10% to estimate the impact of the proposed change. To the extent actual experience varies from that assumed, the costs will vary from the estimates provided herein.

The costs below assume that any impacts in employer contribution rates will not occur until the next rate-setting valuations effective for FY 2025-2026. If an adjustment to the rates is provided in the FY 2023-2024 Appropriation Act, then any changes in rates would be immediately realized in the FY 2023-2024 rates.

Exhibit 3 – Estimated Cost Impacts of SB 17

	<u>FY 2023</u>	<u>FY 2024</u>	<u>FY 2025</u>	<u>FY 2026</u>	<u>FY 2027</u>	<u>FY 2028</u>
State - General Fund	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
SPORS - General Fund	-	-	1,027,000	1,027,000	1,027,000	1,027,000
VaLORS - General Fund	-	-	667,000	667,000	667,000	667,000
JRS - General Fund	-	-	-	-	-	-
	-	-	-	-	-	-
TOTAL General Fund	\$ -	\$ -	\$ 1,694,000	\$ 1,694,000	\$ 1,694,000	\$ 1,694,000
State - Non-General Funds	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
SPORS - Non-General Funds	-	-	169,000	169,000	169,000	169,000
VaLORS - Non-General Funds	-	-	69,000	69,000	69,000	69,000
	-	-	-	-	-	-
TOTAL - Non-General Funds	\$ -	\$ -	\$ 238,000	\$ 238,000	\$ 238,000	\$ 238,000
Political Subs - In Aggregate	-	-	6,594,000	6,594,000	6,594,000	6,594,000
TOTAL Local Funds	\$ -	\$ -	\$ 6,594,000	\$ 6,594,000	\$ 6,594,000	\$ 6,594,000
Grand Totals	\$ -	\$ -	\$ 8,526,000	\$ 8,526,000	\$ 8,526,000	\$ 8,526,000

Estimated projections based on employee data and valuation results as of June 30, 2021 and assume a level population throughout projection period. Payrolls include proposed pay increases included in Governor's proposed budget for FY 2023 and 2024. Payrolls are assumed to remain level beyond 2024 through remainder of projection period.

While there were small impacts to the Group Life Insurance Plan, Health Insurance Credit Plans, and the Virginia Sickness and Disability Program, the impacts were not large enough to impact the employer rates for those plans. Below is the impact to plan liabilities and the corresponding change in employer cost.

Exhibit 4 – Impacts to Plan Liability and Employer Rates - SB 17

Plan	Change in Liability	Change in Employer Rate
SPORS	\$9,613,000	0.76%
VaLORS	\$7,975,000	0.19%
Locals in Aggregate	\$50,112,000	0.12%
GLI	(\$119,000)	0.00%
HIC State	\$644,000	0.00%
HIC Locals in Aggregate	\$55,000	0.00%
VSDP	(\$238,000)	0.00%

For the LODA fund, we assume the reemployed members would continue to be eligible to submit a claim for LODA benefits if disabled or killed in the line of duty or under a presumptive cause. The cost impact to LODA would be indeterminate although there may potentially be more claims since this population will typically be older than active employees. However, current LODA beneficiaries cannot return to active employment in positions covered by LODA without their LODA benefit ceasing.

Allowing a VRS retiree to return to work and be actively employed while continuing to receive a retirement allowance would impact both retirement and other post-employment benefits (OPEB) plans.

Return-to-work provisions have the potential to have financial impacts on VRS retirement plans due to the following implications:

- **Can incentivize members to retire earlier than originally expected.** Since members would be able to receive a retirement benefit and continue to receive compensation for working in a VRS-covered position, provisions of the bill allowing such return to work could change retirement patterns. To illustrate, if members retire earlier than anticipated, the plan pays benefits earlier than expected and for a longer period. In addition, the plan has less time in which to earn investment income on member and employer contributions, which is necessary to fund benefits. Historically, approximately 2/3 of the funding for benefits is derived from investment income. Requiring longer breaks in service, such as a year or more, would help to avoid prearrangements of subsequent reemployment (precluded by the Internal Revenue Code) and mitigate altering retirement patterns of current members.
- **Can impact allocation of cost-sharing if replacing current covered positions with retirees.** Employers filling positions with retirees under the provisions of the bill could impact cost-sharing allocations if the payroll of these members is exempt from inclusion in valuation pay. As an example, payroll of a law enforcement agency that hires retirees as law enforcement officers will be smaller than anticipated if these positions that were formerly filled by active employees will now be filled by retirees, for whom no employer contributions are being made. This impact can be avoided by requiring that the payroll of

retired members be included in the plan's covered payroll for VRS reporting, as is the case with this bill.

The implications of incentivized early retirement would impact individual political subdivision plans, SPORS, and VaLORS under the provisions of the bill, and the amount of impact would vary based on utilization of the provision within each of the plans. The additional costs of earlier than expected retirements would be borne by the local employers of the retiring members through additional pension and health insurance credit payments paid over longer periods of time, or in the case of a member in SPORS or VaLORS, the cost would be shared by the pool of employers in those plans.

Retirement eligibility provisions for hazardous duty employees (SPORS, VaLORS, and local law enforcement) allow them to retire earlier than employees in other VRS plans. As noted by the Joint Legislative Audit and Review Commission (JLARC) in its 2008 *Review of State Employee Total Compensation* report, <http://jlarc.virginia.gov/pdfs/reports/Rpt378.pdf>, these employees typically have job requirements that make them less fit for duty as they age. This has implications for their colleagues and the public. This may also lead to increased workers' compensation claims and LODA claims.

In addition, many of these members are also provided with an enhanced hazardous duty supplement, which in theory is being provided as a financial bridge for members from an earlier retirement until eligibility for Social Security and Medicare benefits.. Also, in part since hazardous duty employees are eligible to retire earlier than general employees, they were not placed in the Hybrid Retirement Plan because they were not anticipated to have enough years of service to accumulate adequate retirement savings in the Hybrid.

This legislation covers a large group of employees of both state and local employers. Due to the size of this group, the impact of this bill may have significant cost impacts. It is also another in a series of recent bills adding various categories of employees who are allowed to return to work full-time after retirement. The more categories of employees who are allowed to return to work on a full-time basis, the higher the impact will be on retirement patterns, as these bills encourage members to retire earlier than they normally would have. Earlier than anticipated retirements require payment of retirement benefits for a longer period of time than was assumed when contribution rates were set, and over time will lead to higher contribution rates.

Current Return-to-Work Options

Retirees may currently return to work part-time without losing VRS retirement benefits following a bona fide break in service of one full calendar month during a time the employee would otherwise have worked and with no prearrangement. In most cases a VRS retiree may return to work on a part-time basis with a VRS-participating employer and continue receiving retirement benefits. When working in a "non-covered" (i.e., part-time, temporary, or provisional) position, a VRS retiree is not in violation of § 51.1-155(B) and may continue to work while also collecting his or her retirement benefit. To be considered working in a non-covered position based on part-time employment, a retiree must work 80% or less of the

hours required of the comparable full-time position. For a 40-hour week, this translates to 32 hours per week or 1,664 hours per year.

Note that, under the bill, retirees who return to work under this provision forfeit the opportunity to add additional service credit to their record. Additional service credit, if earned, may result in a higher retirement benefit when the retiree re-retires at a later date. However, this bill does not permit the retiree to continue to earn service credit in the system. If the retiree remained active, or returned to active service, however, they would earn additional service credit.

10. Specific Agency or Political Subdivisions Affected: DCJS, as well as VRS and any employer, as defined in § 51.1-124.3, that is a state or local law enforcement agency and any person receiving a service retirement allowance under Title 51.1 for service as a sworn law-enforcement officer who returns to work as a law enforcement officer, as defined in § 9.1-101 under the provisions of this legislation.

11. Technical Amendment Necessary: No.

12. Other Comments: Under the bill, a member who has retired from a sworn law-enforcement officer position under Title 51.1 (SPORS, VaLORS, or local law-enforcement officers) and who, following a one-year break in service, is hired by a law enforcement agency as a law enforcement officer, may work full-time and continue to receive a retirement benefit (i.e., an in-service distribution). The bill also provides that the retiree will not be eligible to receive any cash match contributions pursuant to Chapter 6.1 (§ 51.1-607 et seq.) for which active employees are eligible. The bill also requires employer contributions, which serve to mitigate the potential impacts related to changes in retirement patterns.

The retiree would not receive any future benefit accruals while working and would, therefore, not be required to make member contributions to the plan. Retirees who return to work under this provision would be considered retired for retirement, group life, health insurance credit, VSDP and/or VLDP benefits, if applicable. The member would be eligible to receive cost-of-living increases on the service retirement benefit while receiving the in-service distribution.

Because this legislation applies to so many employees, it could have significant cost impacts. In addition, it is one in a series of recent bills adding various categories of employees who are allowed to return to work full-time after retirement. The more categories of employees who are allowed to return to work full time while receiving a retirement benefit, the higher the impact will be on retirement patterns, as these bills encourage members to retire earlier than they normally would have. Earlier than anticipated retirements require payment of retirement benefits for a longer period of time than was assumed when contribution rates were set, and over time will lead to higher contribution rates.

Outside benefits counsel has confirmed that Internal Revenue Service (IRS) guidance allows specifically for a bona fide break in service with no prearrangement for re-employment, and the IRS makes the determination of whether there is a break in service using a facts and

circumstances test. The IRS has not established a safe harbor severance period. IRS regulations under Internal Revenue Code (IRC) § 410, as cited in Private Letter Ruling 201147038, suggest that a one-year period without performing service might be considered a safe harbor. VRS uses a one-year break in service for the teacher and bus driver critical shortage program and for the SSO program. In 2001, the Joint Legislative Audit and Review Commission (JLARC) adopted a resolution concurring with VRS regarding the minimum twelve-month separation before a retiree could be rehired into a critical shortage position without loss of retirement benefits, consistent with the recommendation of the JLARC actuarial consultant. That approach was used also in the SSO program and it is applied again in this bill.

Failure to meet the facts and circumstances test for a bona fide break in service could jeopardize VRS' plan qualification status, thereby affecting all members and retirees. Typically, individual retirees who return to work at more than 80% of a full-time position or are found not to have legitimately retired by completing the bona fide break in service must un-retire, with their retirement benefit ceasing, and the retirees must repay any benefit payments received since the time they returned to work. The retiree would also need to confirm health care eligibility rules at the time he or she is contemplating a return to work.

The bill adopts a one-year break in service before a retired law-enforcement officer can return to work as a law enforcement officer. Also, under this bill, employer contributions are required while the retiree is working, although the retiree will not receive corresponding service credit and will not pay employee contributions.

VRS employer contribution rates are established as a percentage of an employer's VRS covered payroll. When a position is removed from VRS coverage by a return-to-work exception or otherwise, there is a decrease in the funding of retirement benefits. Specifically, legacy unfunded liabilities will not be paid off as expected. This bill does require that an employer include compensation paid to a retiree hired into a law enforcement officer position in its VRS covered payroll for purposes of calculating employer retirement contributions, which helps to mitigate this impact.

Allowing a VRS retiree to return to work and be actively employed while continuing to receive a retirement allowance would impact both retirement and other post-employment benefits (OPEB) plans.

Background

Currently, a VRS retiree cannot collect a VRS retirement benefit while simultaneously working full-time in a VRS-covered position absent specific statutory authority that complies with applicable Internal Revenue Code provisions. There are limited exceptions to this rule under the *Code of Virginia*, such as retirees working in statutorily defined critical shortage bus driver and teaching positions and SSO positions. Most often, however, an individual working in a full-time position for a VRS-participating employer cannot simultaneously collect a VRS retirement benefit. In the case of a VRS retiree returning to work full-time in a

VRS-covered position, the retiree must “unretire” and resume active VRS participation. When the individual chooses to subsequently retire again, VRS will recalculate the new retirement benefit to include the additional service credit earned.

One-Year Break in Service

The bill provides for a one-year break in service, consistent with the bus driver and teacher critical shortage provisions and the SSO return to work provisions.

A key reason that the critical shortage bus driver and teaching exception and the SSO exception have not resulted in major shifts in retirement patterns is because of the requirement that an individual must have been receiving a retirement allowance for at least one full year before becoming eligible to return in the critical shortage capacity and without impact to the retirement allowance. In addition, the one-year requirement reduces the risk for abuse of the rules that might otherwise result in an unlawful prearrangement, which is contrary to provisions of the Internal Revenue Code (IRC), between an employer and retiring employee to establish post-retirement employment. Ensuring that an unlawful prearrangement to return to work does not take place is critical in pension plans, because not doing so can adversely impact both the member and VRS’ qualified plan status under the IRC.

Health Insurance Impact

Health care issues related to retirees returning to work should also be considered. Some provisions may be challenging to administer since retiree pension benefits and health plan coverage are governed by different rules. Each employer’s health insurance provisions may differ, but typically if a retiree is eligible for active employee coverage, he or she would want to move to the active plan. In most cases, when a retiree comes back to active employment that provides eligibility for health insurance coverage, the retiree prefers to have the employer contribution. However, a retiree who returns to work under the provisions of this bill will still be considered a retiree by VRS and DHRM. Retirees who have coverage under the State Retiree Health Plan and who choose to cease coverage under that plan may not later restart coverage. Each locality may offer different health care insurance coverage, so it is difficult to generalize about the health care impact of a retiree returning to work for a non-state employer and whether they would be allowed to resume retiree coverage, if available.

The employer shared responsibility provisions of the Affordable Care Act (ACA) require that applicable large employers (generally, 50+ employees) offer affordable, minimum essential coverage to full-time (30 or more hours/week) employees and their dependents. The employee does not have to take the coverage, but in order to comply with ACA requirements, the employer would need to confirm through ACA reporting that the offer was made. As indicated with the State Retiree Health Plan, a retiree health plan may or may not include provisions allowing for the retiree to leave the retiree health care program in order to receive

coverage in another plan and then return to the former retiree health plan later. A retiree who mistakenly chooses to leave the State Retiree Health Plan because the employer was required to offer coverage does not have the option to return to the State Retiree Health Plan.

There may also be Medicare considerations that apply.

Additional Information Related to Disability Retirement and LODA Benefits Eligibility

A retired law enforcement officer who is receiving Line of Duty Act (LODA) benefits and who is rehired as a retiree into the same position would lose those benefits under § 9.1-401(C)(3).

Many retired officers receiving LODA benefits are also drawing a disability retirement benefit that may possibly make them ineligible for work as a law enforcement officer under the bill. VRS has communicated clearly and consistently through its publications and other outlets that a disability retiree cannot return to a position that requires the same or similar duties as those performed prior to disability retirement. Similarly, if a LODA recipient returns to an active LODA-eligible position, their LODA benefit must cease.

Lastly, DCJS would have to opine on any questions related to the implications of exemptions for training and certification requirements

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