

**SENATE OF VIRGINIA**

**Senate Finance Committee**

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**Funding of the  
Virginia Retirement  
System**

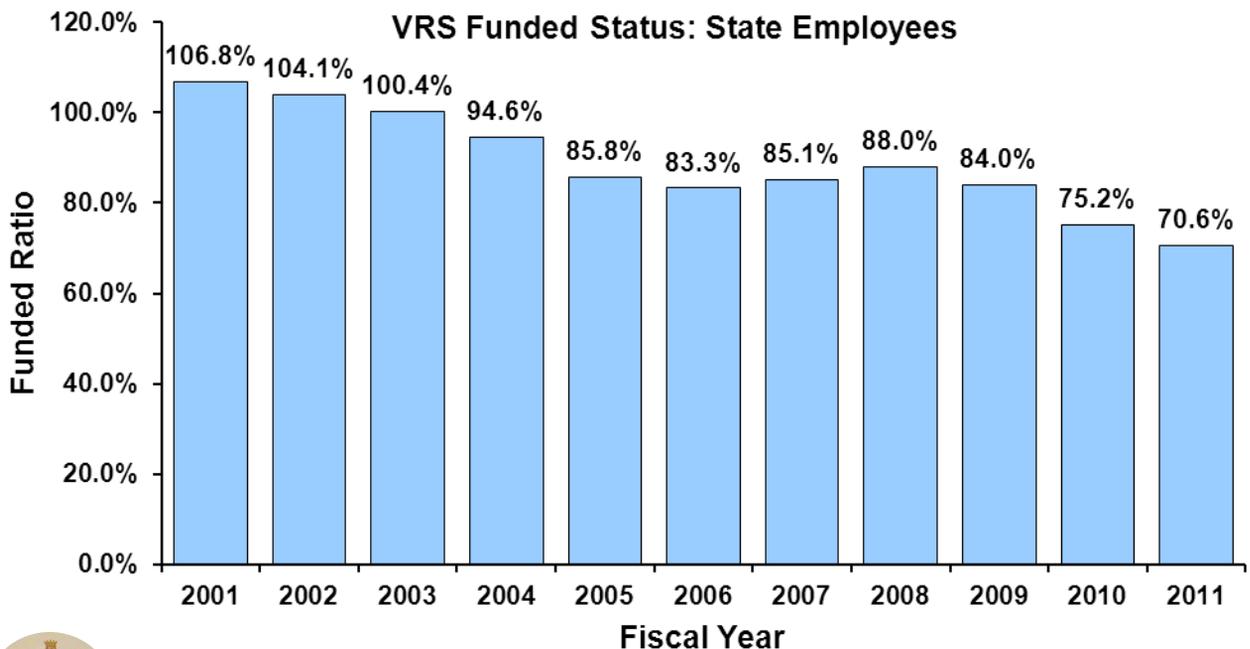
November 18, 2011



SENATE FINANCE COMMITTEE

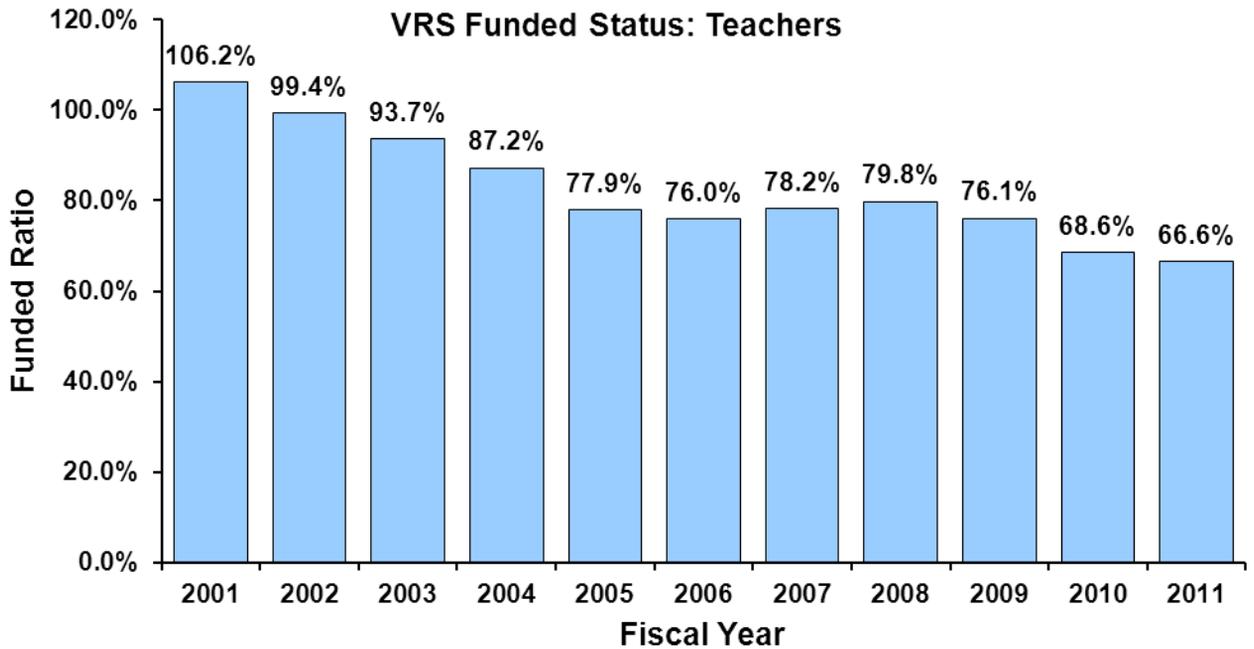
# VRS Retirement: 2012-14 Biennium

- Employer contribution rates for the Virginia Retirement System will be a major issue for the 2012 General Assembly session.
  - Increases in the board-approved rates for the five defined benefit pension programs have a combined cost of about \$990 million GF.
    - VRS: State Employees
    - VALORS: Virginia Law Officers Retirement System
    - VRS: Teachers
    - JRS: Judicial Retirement System
    - SPORS: State Police Officers Retirement System
  - The unfunded liability of these five programs has risen to about \$19.9 billion.
- The funded status of the state employee retirement pool has declined to 70.6 percent.



# VRS Retirement: 2012-14 Biennium

- The funded status of the teachers retirement pool has declined to 66.6 percent.



# VRS Retirement: 2012-14 Biennium

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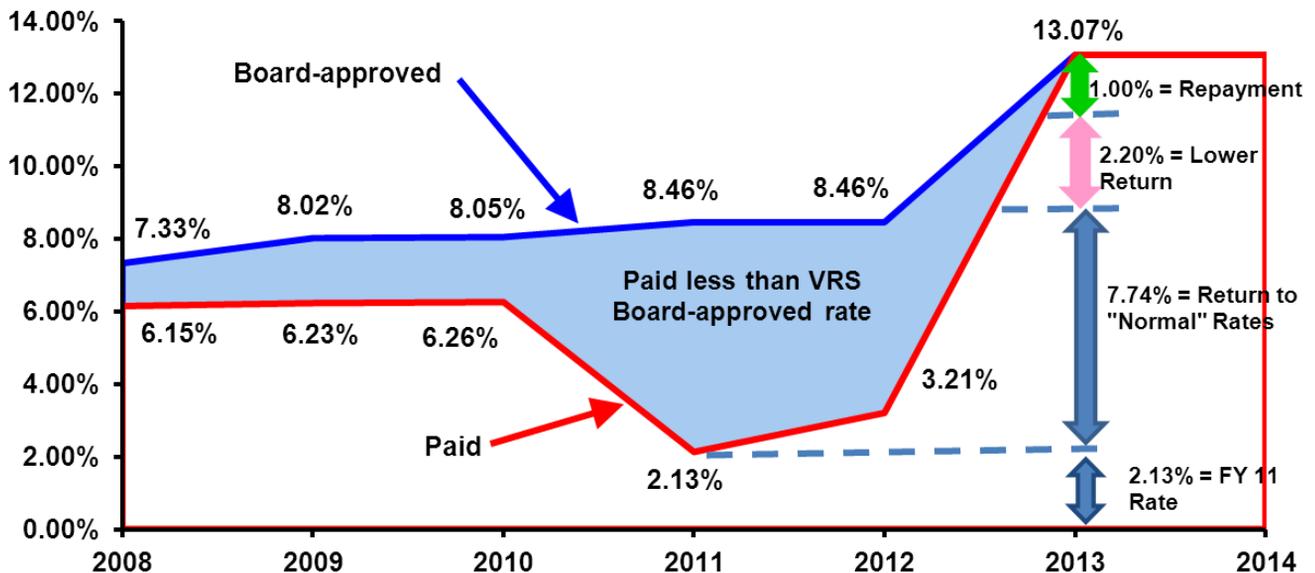
- The 2012-14 contribution rates and the unfunded liability are two separate issues and require different approaches:
  - **2012-14 contribution rates:** Short-term issue that will require immediate solutions.
  - **The unfunded liability:** Long-term issue that will require long-term solutions.
- About 86 percent of the costs are driven by two major programs: Teacher Retirement (59%) and State Employee Retirement (27%).
- Short-term actions to lower the 2012-14 rates **may increase** the unfunded liability.
- Long-term actions to lower the unfunded liability will have **no impact** on the 2012-14 contribution rates.



# VRS Retirement Rates: State Employees

- The board-approved VRS employer contribution rate for the 2012-14 biennium for state employees is 13.07 percent of salary.
  - 10.94 percent higher than the artificially low rate paid in FY 2011.
  - 7.74 percent is attributable to the return to payment of more normal contribution rates.
  - 1.00 percent is repayment of the 2010-12 deferral.
- The employer contribution rate would be 9.26 percent had the board-approved rates been paid over the last twenty years.

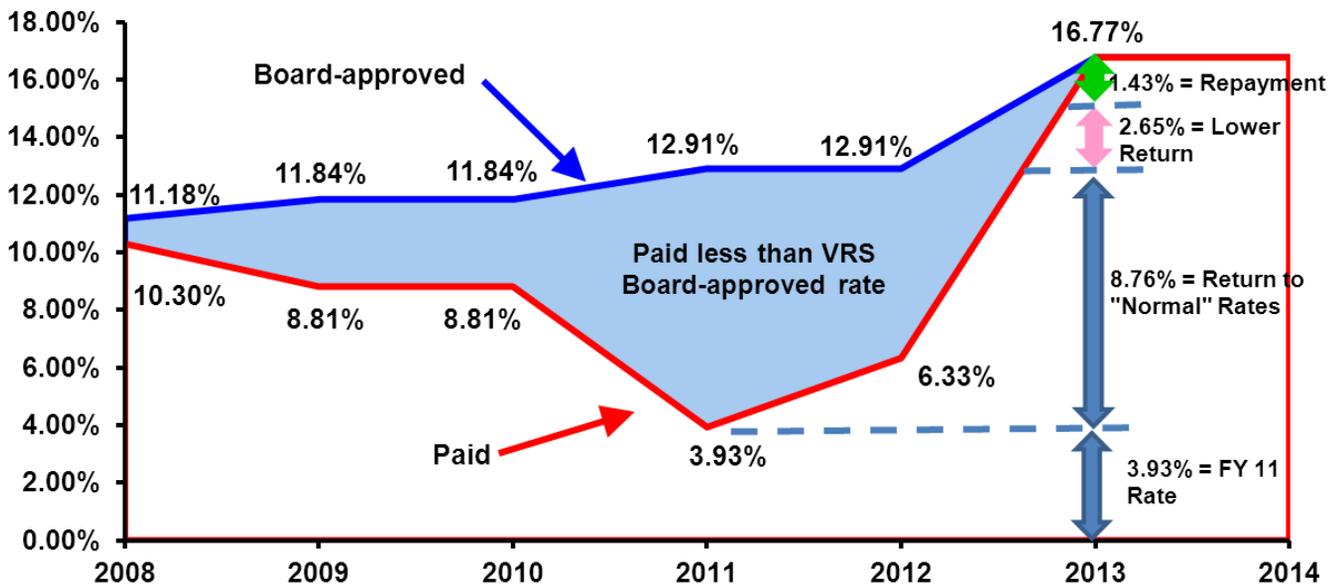
**Comparison of VRS Board-Approved to Actually Paid Employer Contribution Rates for State Employees**



# VRS Retirement Rates: Teachers

- The board-approved VRS employer contribution rate for the 2012-14 biennium for teachers is 16.77 percent of salary.
  - 12.84 percent higher than the artificially low rate paid in FY 2011.
  - 8.76 percent is attributable to the return to payment of more normal contribution rates.
  - 1.43 percent is repayment of the 2010-12 deferral.
- The employer contribution rate would be 12.28 percent had the board-approved rates been paid over the last twenty years.

Comparison of VRS Board-Approved to Actually Paid Employer Contribution Rates for Teachers



# VRS Retirement Rates: 2012–14 Options

- Three options for addressing the 2012-14 VRS contribution rates:

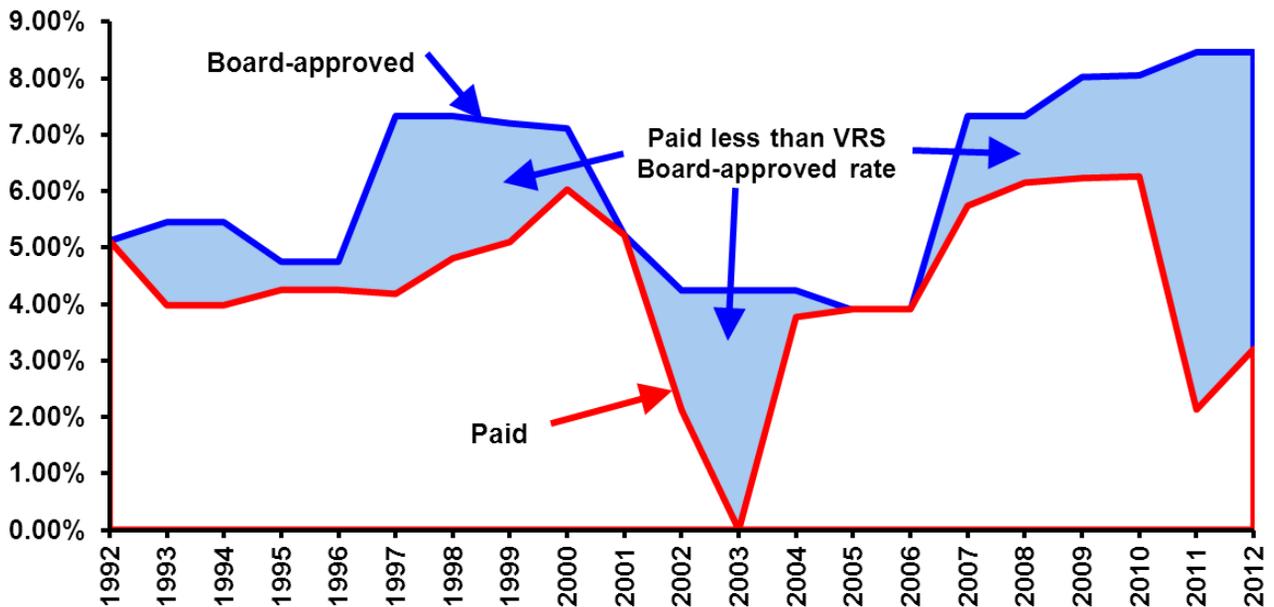
<b>VRS Funding Scenarios</b> (\$ GF in millions)			
	<b>FY 2013</b>	<b>FY 2014</b>	<b>2012-14</b>
<b>Board-Approved Rate (7%)</b>			
State Employees	\$200.7	\$205.0	\$405.7
Teachers	<u>\$289.7</u>	<u>\$290.5</u>	<u>\$580.3</u>
<b>Total</b>	<b>\$490.4</b>	<b>\$495.5</b>	<b>\$986.0</b>
<b>Phase-In</b>			
State Employees	\$127.4	\$130.1	\$257.5
Teachers	\$173.5	\$173.9	\$347.4
<b>Total</b>	<b>\$300.8</b>	<b>\$304.1</b>	<b>\$604.9</b>
<b>Alternate Rate of Return (8%)</b>			
State Employees	\$117.0	\$119.5	\$236.5
Teachers	<u>\$147.9</u>	<u>\$148.4</u>	<u>\$296.3</u>
<b>Total</b>	<b>\$264.9</b>	<b>\$267.9</b>	<b>\$532.8</b>



# VRS Unfunded Liability

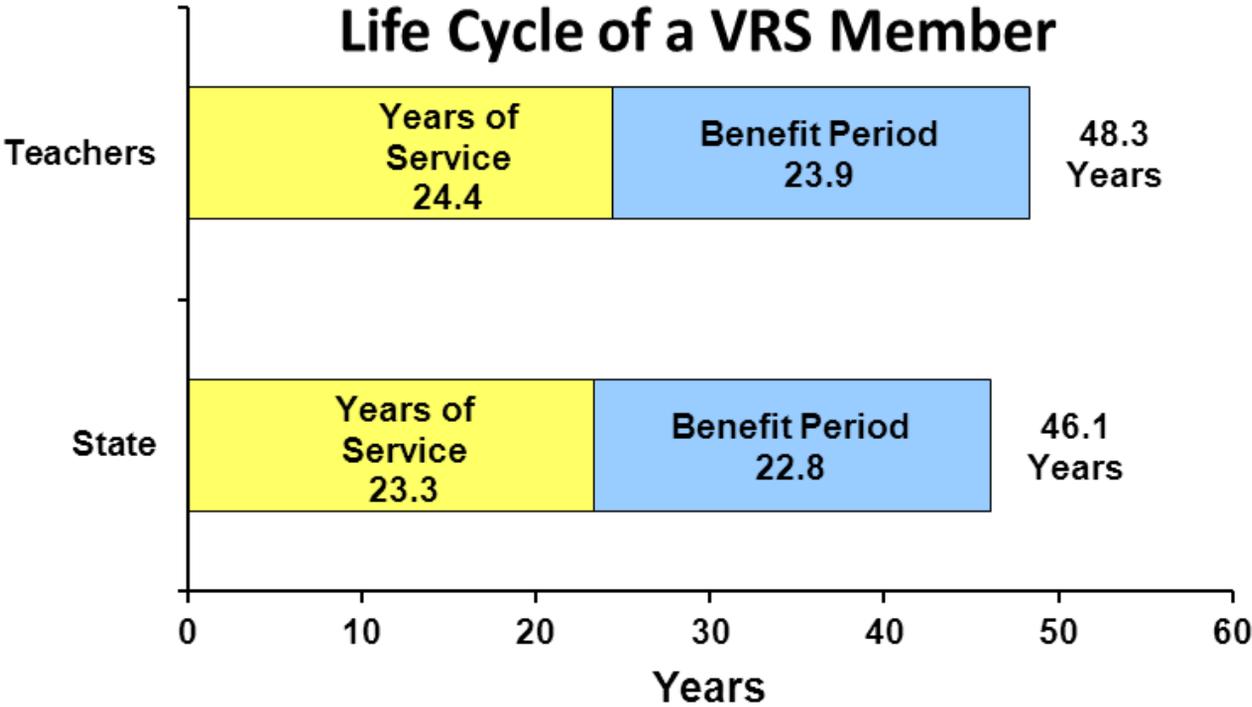
- The VRS unfunded liability reached \$19.9 billion in 2011.
  - Under Governmental Accounting Standards Board (GASB) rules the unfunded liability is **always** measured using the actuarial assumptions adopted by the VRS board.
- The two largest factors affecting the VRS unfunded liability are:
  - Investment losses since 2002, and
  - Chronic underfunding of the employer contribution rates.

Comparison of VRS Board-Approved to Actually Paid Employer Contribution Rates for State Employees



# VRS Unfunded Liability

- The VRS time horizon is very long.



# Addressing the Unfunded Liability

- Retirement rates are calculated to “pay off” the unfunded liability (UL) over a set period of time.
  - For 2011 the VRS board used 30 years.
  - The goal is 100 percent funding (No Unfunded Liability).
- Retirement plans with a funded status of 80 percent or more are considered adequately funded.
  - Greater unfunded liabilities can be acceptable if the pension program’s funded status is improving.
  - State Employees funded status is 70.6 percent. (UAAL= 29.4%)
  - Teachers funded status is 66.6 percent. (UL= 33.4%)
  - Both were moving in the wrong direction
- There are three ways to address the unfunded liability:
  - Cut retirement benefits,
  - Shift the cost to someone else, or
  - Pay the bill.
- The Commonwealth has already done the first two.
  - Reduced retirement benefits for employees hired after July 1, 2010, and
  - Required employees to contribute to their retirement costs.
- The Senate passed a constitutional amendment in 2011 to require a phase-in toward payment of the board-approved retirement rates.



# Addressing the Unfunded Liability: Next Steps

- Numerous proposals have been put forward to address the issue of VRS funding;
  - Defined Contribution retirement plans,
  - Hybrid retirement plans,
  - Further reduce the defined benefit plan benefits, and
  - Shift additional costs to employees.
- Reliable information on the costs and benefits of these proposals was unavailable in 2011.
- Given the magnitude of the program, any changes will have significant implications.
  - Almost 601,000 members of the five VRS defined benefit retirement programs.
  - Over \$52 billion in assets.
- The Senate requested that JLARC undertake a comprehensive study of the VRS retirement programs for state and local employees.
  - Report before the 2012 session – December 2011.
  - Provide a basis of information and recommendations for further action.



# Summary

- There will be two separate retirement issues before the 2012 General Assembly.
  - **Short-term:** 2012-14 VRS employer contribution rates.
  - **Long-term:** The VRS unfunded liability.
- Defined benefit retirement programs are long-term in nature.
- **Short-term actions to lower the 2012-14 rates may increase the unfunded liability .**
- **Long-term actions to lower the unfunded liability will have no impact on the 2012-14 contribution rates.**
- Long-term structural changes to the VRS defined benefit retirement programs will affect hundreds of thousands of Virginians and billions of dollars.
- The JLARC study of public employee retirement programs will provide a base of information and recommendations for future action.



# Appendix: 2010 and 2011 Retirement Changes

- 2010 session changes to the public employee retirement programs.

Provision	Current	HB 1189 and SB 232 (New Employees after July 1, 2010)
<b>Benefit Formula</b>	AFC x YRS Service x .0170	AFC x YRS Service x .0170
<b>AFC Calculation</b>	3 Highest years	5 Highest years
<b>Early Retirement</b>	50 years old/30 Years service	Age + Service = 90 Minimum Age = 60 No change for SPORS, VALORS, or JRS
<b>Normal Retirement</b>	65 years old/5 Years service	Conform to Social Security (VRS) No change for SPORS, VALORS, or JRS
<b>COLA</b>	First 3% of CPI + Next 4% of CPI x 0.5 Cap of 5%	First 2% of CPI + Next 8% of CPI x 0.5 Cap of 6%
<b>JRS Years of Service</b>	Years of Service x 2.5 Max Age 70	Age < 45 = Years Service x 1.5 Age 45 to 55 = Years Service x 2.0 Age 55+ = Years Service x 2.5 Max Age 70
<b>Employee Contribution:</b>		
<b>Current Employees</b>	0.0%	0.0%
<b>New Employees</b>	0.0%	5.0%
<b>Optional Retirement Plans (ORP)</b>	10.4% Employer Rate 0.0% Employee Rate	8.5% Employer Rate (Option for an additional 0.4%) 5.0% Employee Rate (New Employees)
<b>Purchase of Service</b>	Within first 3 years = 5.0% 3+ years = Actuarial cost (Details vary by type of service)	Within first year = Normal Cost 1 year + = Actuarial Cost (Details vary by type of service)

- 2011 session reinstated the 5 percent employee retirement contribution for state employees hired before July 1, 2010.

