

Report to the General Assembly and VSERS and VSTRS Boards of Trustees on Recommendations to Reduce Pensions and OPEB Liabilities



February 4, 2021

Presented to Senate Committee on Finance

Funding Progress of the VSERS Retirement System - (Amounts in Thousands)

Year ending June 30	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a) (in thousands)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2020	\$ 2,054,826	\$ 3,095,291	\$ 1,040,465	66.4%	\$ 551,981	188.5%
2019	1,964,501	2,779,966	815,465	70.7%	\$ 527,571	154.6%
2018	1,881,805	2,661,609	779,804	70.7%	521,671	149.5%
2017	1,793,795	2,511,373	717,578	71.4%	504,553	142.2%
2016	1,707,268	2,289,452	582,184	74.6%	471,268	123.5%
2015	1,636,268	2,178,827	542,559	75.1%	462,057	117.4%
2014	1,566,076	2,010,090	444,014	77.9%	437,676	101.4%
2013	1,469,170	1,914,300	445,130	76.8%	416,766	106.8%
2012	1,400,779	1,802,604	401,825	77.7%	385,526	104.2%
2011	1,348,763	1,695,301	346,538	79.6%	398,264	87.0%
2010	1,265,404	1,559,324	293,920	81.2%	393,829	74.6%
2009	1,217,638	1,544,144	326,506	78.9%	404,516	80.7%
2008	1,377,101	1,464,202	87,101	94.1%	404,593	21.5%
2007	1,318,687	1,307,643	(11,044)	100.8%	386,917	-2.9%
2006	1,223,323	1,232,367	9,044	99.3%	369,310	2.4%
2005	1,148,908	1,174,796	25,888	97.8%	349,258	7.4%
2004	1,081,359	1,107,634	26,275	97.6%	336,615	7.8%
2003	1,025,469	1,052,004	26,535	97.5%	319,855	8.3%
2002	990,450	1,017,129	26,679	97.4%	300,994	8.9%
2001	954,821	1,026,993	72,172	93.0%	278,507	25.9%
2000	895,151	967,064	71,913	92.6%	266,519	27.0%
1999	804,970	876,412	71,442	91.8%	238,281	30.0%
1998	733,716	804,501	70,785	91.2%	235,956	30.0%
1997	639,128	753,883	114,755	84.8%	227,000	50.6%

Funding Progress of the VSTRS Retirement System - (Amounts in Thousands)

Year ending June 30	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a) (in thousands)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2020	\$ 2,035,714	3,969,003	1,933,289	51.3%	\$ 645,903	299.3%
2019	1,950,860	3,505,319	1,554,459	55.7%	\$ 624,908	248.8%
2018	1,866,121	3,379,554	1,513,433	55.2%	612,899	246.9%
2017	1,779,592	3,282,045	1,502,453	54.2%	607,355	247.4%
2016	1,716,296	2,942,024	1,225,728	58.3%	586,397	209.0%
2015	1,662,346	2,837,375	1,175,029	58.6%	557,708	210.7%
2014	1,610,286	2,687,049	1,076,764	59.9%	567,074	189.9%
2013	1,552,924	2,566,834	1,013,910	60.5%	563,623	179.9%
2012	1,517,410	2,462,913	945,503	61.6%	561,179	168.5%
2011	1,486,698	2,331,806	845,108	63.8%	547,748	154.3%
2010	1,410,368	2,122,191	711,823	66.5%	562,150	126.6%
2009	1,374,079	2,101,838	727,759	65.4%	561,588	129.6%
2008	1,605,462	1,984,967	379,505	80.9%	535,807	70.8%
2007	1,541,860	1,816,650	274,790	84.9%	515,573	53.3%
2006	1,427,393	1,686,502	259,109	84.6%	499,044	51.9%
2005	1,354,006	1,492,150	138,144	90.7%	468,858	29.5%
2004	1,284,833	1,424,661	139,828	90.2%	453,517	30.8%
2003	1,218,001	1,358,822	140,821	89.6%	437,239	32.2%
2002	1,169,294	1,307,202	137,908	89.5%	418,904	32.9%
2001	1,116,846	1,254,341	137,495	89.0%	403,258	34.1%
2000	1,037,466	1,174,087	136,621	88.4%	387,999	35.2%
1999	931,056	1,065,754	134,698	87.4%	372,299	36.2%
1998	821,977	955,694	133,717	86.0%	357,899	37.4%
1997	717,396	849,179	131,783	84.5%	364,695	36.1%

State Employees Pension (VSERS)

Scope of the Challenge (Dollars in Millions)			
	2019 Valuation*	Estimated Results based on Experience Study	2020 Valuation**
	2021 budget		2022 budget
Unfunded Liability change	\$815.5	\$1,032.3 \$216.8	\$1,040.5 \$225.0
ADEC change	\$83.9	\$113.6 \$29.7	\$119.9 \$36.0

* Used to develop FY2021 budget
 ** Impacts the FY2022 budget

Teachers' Pension (VSTRS)

Scope of the Challenge (Dollars in Millions)			
	2019 Valuation* 2021 budget	Estimated Results based on Experience Study	2020 Valuation** 2022 budget
Unfunded Liability change	\$1,554.0	\$1,880.0 \$326.0	\$1,933.0 \$379.0
ADEC change	\$135.6	\$186.4 \$50.8	\$196.2 \$60.6

* Used to develop FY2021 budget

** Impacts the FY2022 budget

What We Reviewed

- Increased Employee contributions (various scenarios)
- Various Changes to reduce or eliminate COLAs for ACTIVE members upon retirement
 - Not recommending any changes to current retirees
 - **COLA revisions have the largest single impact on reductions to the unfunded liability and employer contributions and are the core of the recommendations.**
- Increase Average Final Compensation (AFC) years
- Revisions to Vesting
- Rule of 87 or 90 (age and years of service provisions for normal retirement)
- Early retirement Factors Using Actuarial Equivalents
- Changes to Maximum Benefit Percentage
- Dedicated revenue sources
 - Revenue Projections/Creation of a Reserve Fund
 - Additional Federal COVID \$
- What are some offsetting options?

Direction from the Trustee Boards

- Each Board of Trustees passed a motion directing the Treasurer to work with stakeholder groups to identify and review recommendations to lower the unfunded liability and the Actuarially Determined Employer Contribution (ADEC) to at least the previous FY2021 projections and to present those recommendations to the Governor and the General Assembly by January 15, 2021.
- Report was completed and submitted on January 15th and is available on Treasurer's web page.
- General Recommendations
 - Maintain define benefit plans
 - No changes to benefits for current retirees
 - Continue to fund the actuarial determined employer contribution (ADEC)
 - Access additional COVID monies if they become available
 - Consider using excess revenues or federal Cares Act monies to establish a reserve
 - Specific recommendations to State (VSERS) and Teacher (VSTRS) pension and other post employment benefits (OPEB)
 - Create prefunding mechanism for OPEB plans

State System (VSERS) Options to Meet Targets (in \$ millions)

	UAAL	ADEC:	Comments:
Target:	225	36	
1 All Actives, eliminate COLA upon Retirement	-238	-35.3	ADEC off target by \$700 K, UAAL estimate exceeded by \$13 million
2 Eliminate COLA for actives upon retirement except those within 5 years normal retirement as of implementation date	-116.7	-20.3	
Add 4 years to AFC	-81.5	-12.4	
Decrease Due to Combination of elements	8.15	2.108	
Rule of 90	-66.2	-9.1	Likely will decrease AFC savings because of longer working time
Estimated Savings/Preliminary	-256.25	-39.692	

State System (VSERS) Options to Meet Targets (in \$ millions)

	UAAL	ADEC:	Comments:
3 Eliminate COLA for actives upon retirement except those within 5 years normal retirement as of implementation date	-116.7	-20.3	
Add 2 years to AFC	-39.2	-6	
Decrease Due to Combination of elements	3.92	1.02	
Rule of 90	-66.2	-9.1	Likely will decrease AFC savings because of longer working time
Estimated Savings/Preliminary	-218.18	-34.38	Need to identify \$15.9 additional savings to UAAL Mid ground on AFC, add 3 years?
4 COLA threshold \$24K for all actives upon retirement	-134.5	-18.8	
AFC add 2 years	-31.9	-5	
Rule of 90	-53.5	-7.3	
Contribution increase by .35%		-2.1	
Estimated Savings	-219.9	-33.2	After adjusting for impact of combined elements, just shy of target.

Note: For Options #2 and #3 estimates will vary and likely be lowered because of interactions between various elements. The actuary will adjust for these interactions if these remain under consideration.

Preliminary Recommendation- Subject to further discussion

Teacher System (VSTRS) - Options to Meet Targets (in \$ millions)

	UAAL	ADEC:
Target:	379.0	60.6
1 Eliminate all COLAs for active members upon retirement	-165.1	-22.5
Revise AFC to 7 Years	-81.8	-11.5
Update Rule of 90*	-7.2	-0.6
Contribution increase to 8%		-17.6
Estimated Savings	-254.1	-52.2

Preliminary Recommendation- Subject to further discussion

Trustee Board Action- Subsequent Motions

- State (VSERS) and Teachers (VSTRS) Boards:
- Each Trustee Board voted to note that that “it had received the Treasurer’s Report and recognizes that the ADEC for FY22 and beyond may not be sustainable and as a result recognizes that changes in benefit levels to reduce the unfunded liability may be required.”
- “...the Board directed the Treasurer to: (1) identify and review strategies to reduce pressure on and increase the stability of ADEC contributions and lower the unfunded liability in future years, including risk/gain sharing models, establishment of a reserve fund, and separate or rolling amortization schedules (2) cost the options for benefit changes by group per member; (3) assess, to the extent possible, the potential for the options to affect assumed actuarial retirement projections and estimate the effect on the financial condition of the system, and supplement any prior report with this addition information by February 22nd.”
- VSTRS Board directed the Treasurer’s Office to research a range of COLA options for those in retirement with a lower benefit amount.
- The VSTRS Board voted to accept the Treasurer’s recommendation on employee contribution rates with the caveat that a possible phase-in is examined at either 7 or 8 percent

History of Disciplined Incremental Steps to Reduce Pension And Retiree Health Care Liabilities

2010 VSTRS: Lengthened age for normal retirement, contribution increases, and other changes, effective in FY2011, resulting in **\$15 million in annual pension savings. In addition to pension costs, additional health care savings accrued.**

2011 VSERS: Employee contribution rate increases beginning FY2012, initially generating **\$5 million in savings per year, increasing each year.**

2011-2012 VSTRS: Secured **one-time revenues in excess of \$5 million for VSERS and VSTRS** under the Federal Early Retirement Reinsurance Program.

2012 - 2015: Incremental increases in employee and employer contributions to municipal system (VMERS), demonstrating shared responsibility by all parties. These changes put VMERS on a stronger financial track.

2014 VSTRS: additional contribution increases for new and non-vested members, effective FY2015, generating **\$1 million initial annual savings, increasing each year.**

History of Disciplined Incremental Steps to Reduce Pension And Retiree Health Care Liabilities (ctd.)

- **2015:** Created Retired Teachers' Health and Medical Benefits Fund starting FY2015
 - From the 1980s to 2014, teacher health care premiums for teachers were paid out of a sub-trust of teachers pension fund but with no appropriations to cover expenses: by 2014 this arrangement was costing over \$20 million per year in interest costs.
 - Created a separate fund with federal, state and local resources instead of putting it on the credit card.
 - A new health care assessment for LEAs was implemented, linking local employment decisions to the benefit costs.
 - **Projected to save taxpayers \$480 million in unfunded liability interest costs through FY2038.**
- **2016:** Changes to the amortization financing schedule for VSERS and VSTRS **will result in saving \$165 million in interest from present to 2038.**
- **2016:** Increased employee contributions resulting in **\$1.2 million in annual savings, with savings growing larger in future years.**

At the same time creating additional Transparency and Accountability

2013: Pension forfeiture statute adopted for all three systems (VSERS, VSTRS, VMERS)

Created benchmarks for excluding hours/income to preclude spiking

2015: VSERS Disability retirement reform permitting wage verification of disability pensioners.

2015-2017: Additional disability reforms for all three systems (state, teacher, municipal).