**Benefits and Actuarial Committee (B&A) Meeting**
**VRS, 1111 E. Main St., 3rd Floor Board Room**
**Wednesday, 10/18/2023**
**1:00 - 3:30 PM ET**

**I. Welcome and Introductions**

**II. Approve Minutes**

*B&A Minutes 6.14.2023 - Page 2*

**III. GRS 2023 Actuarial Valuation Results for Five Statewide Retirement Plans, Group Life Insurance, State and Teacher Retiree Health Insurance Credit, and the Virginia Sickness and Disability Program (includes self-funded LTC) and Funding Policy Amendments**

*GRS Actuarial Valuation Results as of 6.30.23 - Page 5*

*VRS Funding Policy 2023 Redline - Page 62*

- **RBA - Amend VRS Funding Policy Statement to Allow for Resetting of Total Unfunded Accrued Liability as of June 30, 2023 Over 20 Years**
  *RBA - Amendments to Funding Policy Statement - Page 108*
- **RBA - Certify the Contribution Rates for the Five Statewide Retirement Plans and Associated OPEBs Effective for FY 2023 and FY 2024**
  *RBA - Approve Rates For Five Statewide Plans and Associated OPEBs - Page 110*

**IV. Information Item**

- **Stress Test and Sensitivity Analysis Report will be Provided to Legislature**
- **Upcoming B&A Committee Meeting:**
  **-. November 16, 2023 at 10:00 a.m. (Local Valuations and Line of Duty Act)**

**V. Other Business**

# Minutes

A regular meeting of the Benefits and Actuarial Committee was held on June 14, 2023, in Richmond, Virginia with the following members participating:

John M. Bennett, Chair
Lindsey K. Pantele
Jessica L. Hood

Board members present:
Hon. J. Brandon Bell, II *(remotely under § 2.2-3708.3(B)(3))*

VRS Staff:

Patricia Bishop, Jennifer Schreck, Rory Badura, Judy Bolt, Ty Bowers, Jessica Budd, Jeanne Chenault, Cassandra Coles, Michael Cooper, David Cotter, Sara Denson, Valerie Disanto, Antonio Fisher, Josh Fox, Krystal Groff, Robert Irving, Angela Payne, Scott Weaver, Leslie Weldon and Cindy Wilkinson.

Guests:

Emily Grimes, Department of Planning and Budget; Natosha Palmer, Securian Financial; and Bea Snidow, Virginia Education Association.

The meeting convened at 1:00 p.m.

**Opening Remarks**

Mr. Bennett called the meeting to order and welcomed everyone to the June 14, 2023, meeting of the Benefits and Actuarial Committee.

After noting that the meeting was being held in accordance with § 2.2-3708.3(B)(3) of the *Code of Virginia* and the VRS Remote Meeting Attendance Policy, Mr. Bennett took a roll call for attendance:

Ms. Hood: Here
Ms. Pantele: Here
Mr. Bell: Here
Mr. Bennett: Here

**Approval of Minutes**

Upon a motion by Ms. Pantele, with a second by Ms. Hood, the Committee approved the minutes of its February 7, 2023, meeting upon the following roll call vote:

Ms. Hood: Aye
Ms. Pantele: Aye
Mr. Bell: Aye
Mr. Bennett: Aye

**Election of Committee Vice Chair**

Upon a motion by Mr. Bennett, with a second by Ms. Hood, the Committee approved the nomination of Lindsey K. Pantele to serve as Vice Chair of the Benefits and Actuarial Committee upon the following roll call vote:

Ms. Hood: Aye
Ms. Pantele: Aye
Mr. Bell: Aye
Mr. Bennett: Aye

**Information Items**

Actuarial Principles 101

Rory Badura, Senior Staff Actuary, provided an overview of the actuarial principles, which included the actuarial valuation process, actuarial assumptions and terminology, rate-setting and funded ratios as a measure of the health of the plans. In addition, an overview of the VRS Funding Policy, including its purpose and objectives, was also provided.

Ms. Bishop noted a brown bag session will be held to review this information with the full Board of Trustees in September.

Mr. Bennett thanked Mr. Badura for his presentation.

Group Life Insurance

Robert Irving, Customer Services Director, presented an administrative update regarding recommendations for the Group Life Insurance premium rate to the Committee. Mr. Irving advised VRS' third-party administrator, Securian Financial, manages and administers the life insurance program which provides members opportunities to purchase optional life insurance coverage. Reviews on premium rates are conducted annually and recommendations to maintain, increase or reduce rates are provided to VRS. Mr. Irving advised that the recommendation, effective July 1, 2023, is an overall reduction of 5% in the optional life insurance premiums for certain age groups. In addition, Mr. Irving noted staff will provide an update in August on the enhanced open enrollment period that provided additional opportunities for individuals to make changes to their optional life insurance regarding enrollment or purchase amount.

Mr. Bennett thanked Mr. Irving for his presentation.

B&A Committee Meeting Schedule:

Lastly, the Committee reviewed its meeting schedule:

- October 18 at 1:00 p.m.
- November 16 10:00 a.m.

Mr. Bennett advised the full Board of Trustees will meet Thursday, June 15 at 1:00 p.m.

**Adjournment**

Upon a motion by Ms. Pantele, with a second by Ms. Hood, the Committee agreed to adjourn the meeting upon the following roll call vote:

Ms. Hood: Aye
Ms. Pantele: Aye
Mr. Bell: Aye
Mr. Bennett: Aye

There being no further business, the meeting concluded at 2:31 p.m.

__________________________ __________________________

Date

John M. Bennett, Chair
Benefits and Actuarial Committee

Virginia Retirement System

# June 30, 2023 Annual Actuarial Valuation Results

Presenters: Becky Stouffer, ASA, MAAA, FCA,
Kurt Dosson, ASA, MAAA & Jim Anderson, FSA, EA, MAAA, FCA

October 18, 2023

# Agenda

- Big Picture – Pension & OPEB
- Highlights of 2023 Pension Valuations
- Highlights of 2023 OPEB Valuations
- Looking Ahead
- Appendix

AGENDA

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# BIG PICTURE – PENSION/OPEB

# Big Picture: October Meeting Content

| Pension Valuations | Other Post-Employment Benefits (OPEB) Valuations |
|---|---|
| Virginia Retirement System<br>• State Employees<br>• Teachers | Health Insurance Credit (HIC)<br>• State Employees<br>• Teachers |
| Virginia Law Officers (VaLORS) | Group Life Insurance |
| State Police Officers (SPORS) | Virginia Sickness and Disability Program |
| Judicial (JRS) | |

<u>November Meeting Content</u>: Political Sub. Pension and OPEB; VLDP Results
HIC – Constitutional Officers, Social Service Employees, Registrars;
Line of Duty Act Fund

# Big Picture: Actuarial Valuation Results

- Purposes of Actuarial Valuations of VRS Pension and OPEB plans
  - Measure funding progress as of June 30, 2023
  - Develop contribution rates for FYE 2025 and 2026

Odd year valuations determine contribution rates for 2 years

# Big Picture: General Funding Objectives

- Intergenerational equity with respect to plan costs
- Stable or increasing ratio of assets to liabilities
- Stable pattern of contribution rates


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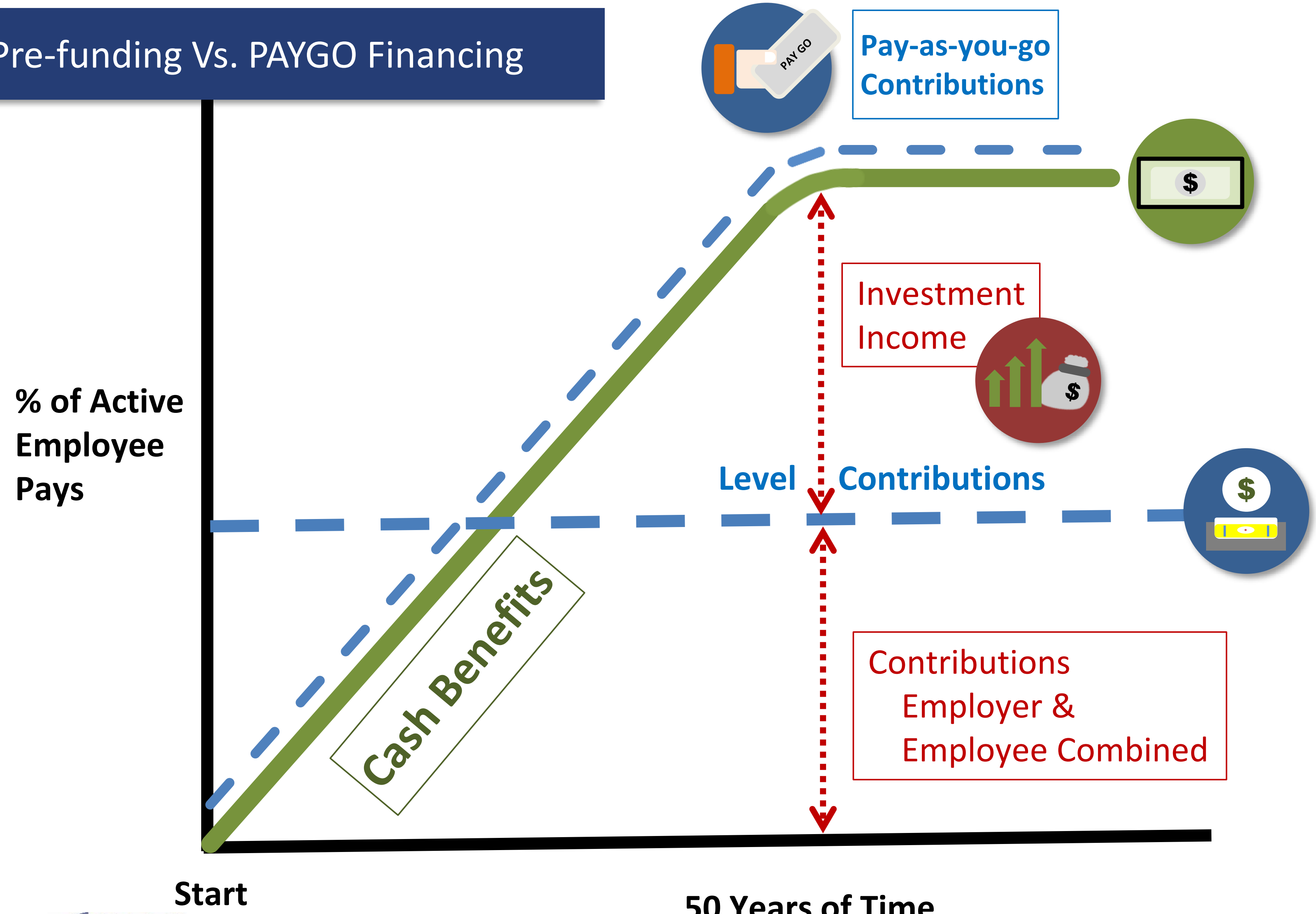
# Pre-funding Vs. PAYGO Financing



# Big Picture: Actuarial Valuation Process – (Statewide Pension Excluding Political Subdivisions)

**Member Data**

**600,237 Members**

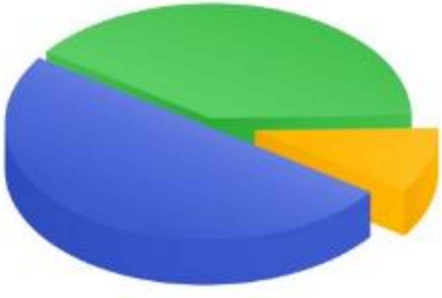
**Financial Data**


**$74.5 Billion**
**Market Value**

**Actuarial Valuation**

**Plan Provisions**


**Actuarial Cost Method**



**Actuarial Assumptions**

# JUNE 30, 2023
# VALUATION RESULTS HIGHLIGHTS

# Active Participants at June 30, 2023

| System | Plan 1 | Plan 2 | Hybrid | Total 2023 | Total 2022 | Percent Change |
|---|---|---|---|---|---|---|
| State | 24,764 | 12,620 | 39,492 | 76,876 | 74,048 | 3.8% |
| Teachers | 54,810 | 26,797 | 71,500 | 153,107 | 153,356 | -0.2% |
| SPORS | 922 | 960 | - | 1,882 | 1,885 | -0.2% |
| VaLORS | 1,843 | 5,635 | - | 7,478 | 7,289 | 2.6% |
| JRS | 136 | 42 | 280 | 458 | 461 | -0.7% |
| Pol. Sub. | TBD | TBD | TBD | TBD | 109,906 | TBD |
| Total | TBD | TBD | TBD | TBD | 346,945 | TBD |

GRS

# Actives: Changes in Average Salary

| System | 2022 | 2023 | Percent Change |
|---|---|---|---|
| State | $ 66,799 | $ 70,880 | 6.1% |
| Teachers | 60,405 | 63,137 | 4.5% |
| SPORS | 84,463 | 89,591 | 6.1% |
| VaLORS | 51,103 | 53,238 | 4.2% |
| JRS | 175,152 | 192,994 | 10.2% |

Note: Return to Work Payroll for 39 School Security Officers and Teachers = $2 million

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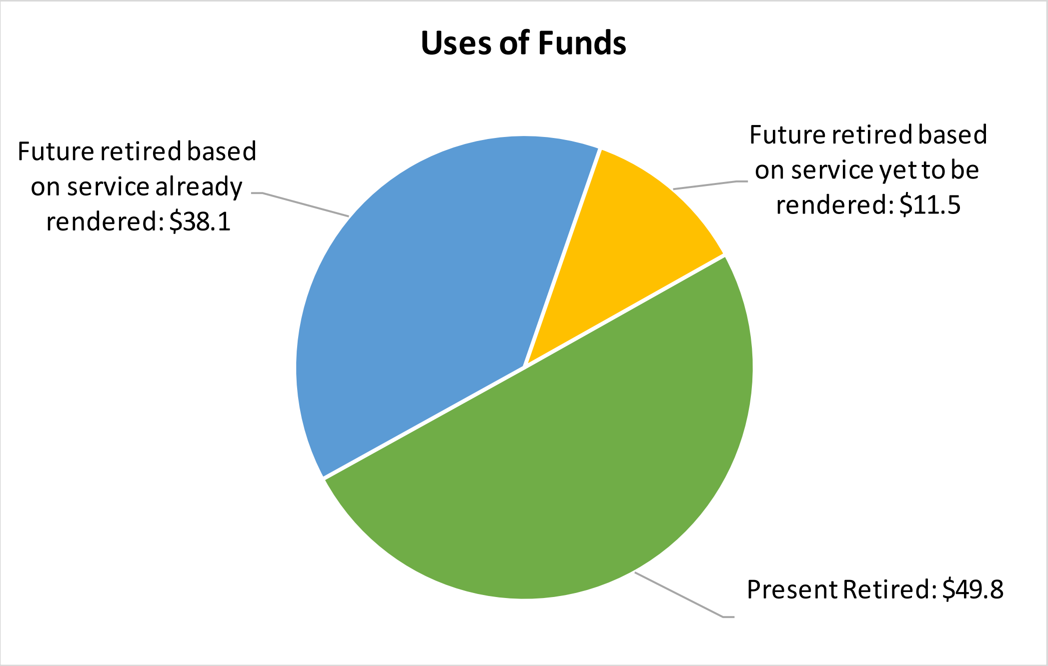
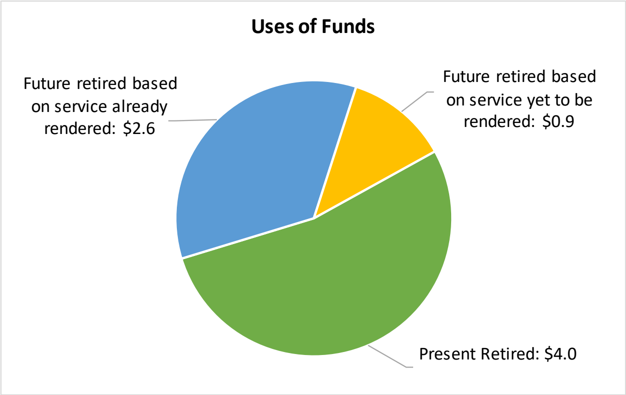
# $106.9 Billion of Benefit Promises to Present State EEs & Teacher Active and Inactive Members

**PENSION*** : $99.4 Billion




**OPEB^** (GLI+HIC): $7.5 Billion




*** Excludes SPORS, VaLORS, JRS, & Pol. Subs.**

**^ Excludes HIC (Pol. Subs. & Special Coverage Groups), VS(L)DP, & LODA**

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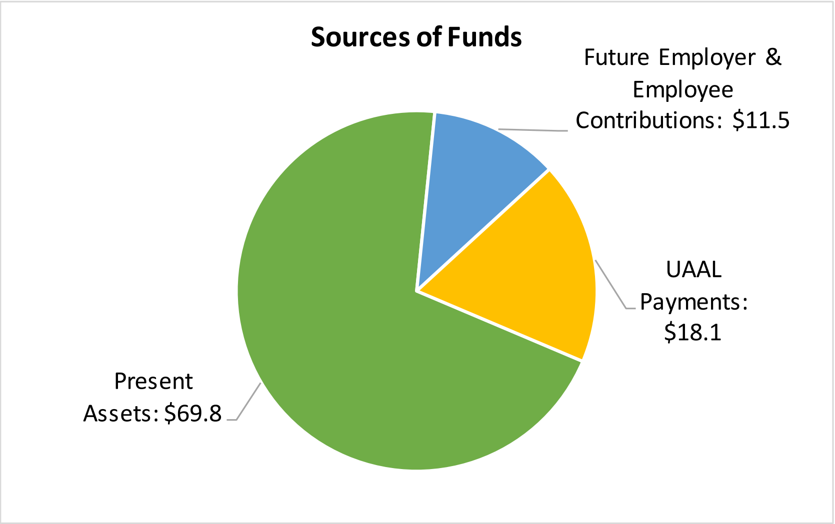
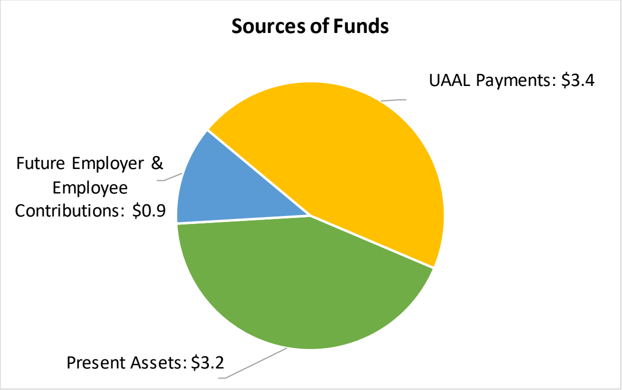
# Sources of Funds for Financing $106.9 Billion of Benefit Promises to State EEs & Teacher Members

**PENSION***: $99.4 Billion




**OPEB^** (GLI+HIC): $7.5 Billion




*** Excludes SPORS, VaLORS, JRS, & Pol. Subs.**

**^ Excludes HIC (Pol. Subs. & Special Coverage Groups), VS(L)DP, & LODA**

# VRS Additional Funding Provisions – Pension

- Additional $931+ million contributed from the General Fund to the Trust in June 2022 & 2023

| System | Add'l Contrib. 2022 | Add'l Contrib. 2023 | Total Additional 2022-2023 | Funded Status Impact | Contrib. Rate Impact |
|---|---|---|---|---|---|
| State | $219,156,316 | $73,052,105 | **$292,208,421** | **+1.08%** | **-0.4%** |
| Teachers | $442,371,087 | $147,457,029 | **$589,828,116** | **+1.08%** | **-0.4%** |
| SPORS | $10,957,816 | $3,652,605 | **$14,610,421** | **+1.10%** | **-0.7%** |
| VaLORS | $19,886,407 | $6,628,802 | **$26,515,209** | **+1.03%** | **-0.5%** |
| JRS | $6,250,014 | $2,083,338 | **$8,333,352** | **+1.13%** | **-0.7%** |
| TOTAL | **$698,621,640** | **$232,873,879** | **$931,495,519** | **+1.08%** | **-0.4%** |

Important to get additional funds into Retirement System when possible

# VRS Additional Funding Provisions – OPEB

- Additional $93+ million contributed from the General Fund to the Trust in June 2022 & 2023

| OPEB Group | Add'l Contrib. 2022 | Add'l Contrib. 2023 | Total Additional 2022-2023 | Funded Status Impact | Contrib. Rate Impact |
|---|---|---|---|---|---|
| HIC: State | $8,522,746 | $27,159,085 | **$35,681,831** | **+3.60%** | **-0.04%** |
| HIC: Teachers | $12,013,013 | $4,004,338 | **$16,017,351** | **+1.14%** | **-0.01%** |
| GLI | $30,438,378 | $10,146,126 | **$40,584,504** | **+1.13%** | **-0.01%** |
| HIC: C. Off. | $275,975 | $91,992 | **$367,967** | **TBD** | **TBD** |
| HIC: S. Svcs. | $121,754 | $1,031,416 | **$1,153,170** | **TBD** | **TBD** |
| HIC: Regis. | $6,494 | $2,165 | **$8,659** | **TBD** | **TBD** |
| TOTAL | **$51,378,360** | **$42,435,122** | **$93,813,482** | **TBD** | **TBD** |

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Important to get additional funds into OPEB Plans when possible

# Actuarial Value Assets 2023: 6.1% MVA Return
# State Employees Pension – $ Millions

| | 2023 | 2024 | 2025 | 2026 | 2027 |
|---|---|---|---|---|---|
| Actual Investment Return | 1438 | | | | |
| Assumed Investment Return | 1502 | | | | |
| Gain/(Loss) to be Phased-in | (64) | | | | |
| Phased-in Recognition<br>-Current year | (13) | ? | ? | ? | ? |
| -1st prior year | (313) | (13) | ? | ? | ? |
| -2nd prior year | 762 | (313) | (13) | ? | ? |
| -3rd prior year | (181) | 762 | (313) | (13) | ? |
| -4th prior year | (13) | (181) | 762 | (313) | (13) |
| Total Recognized Gain/(Loss) | 242 | 255 | 436 | (326) | (13) |

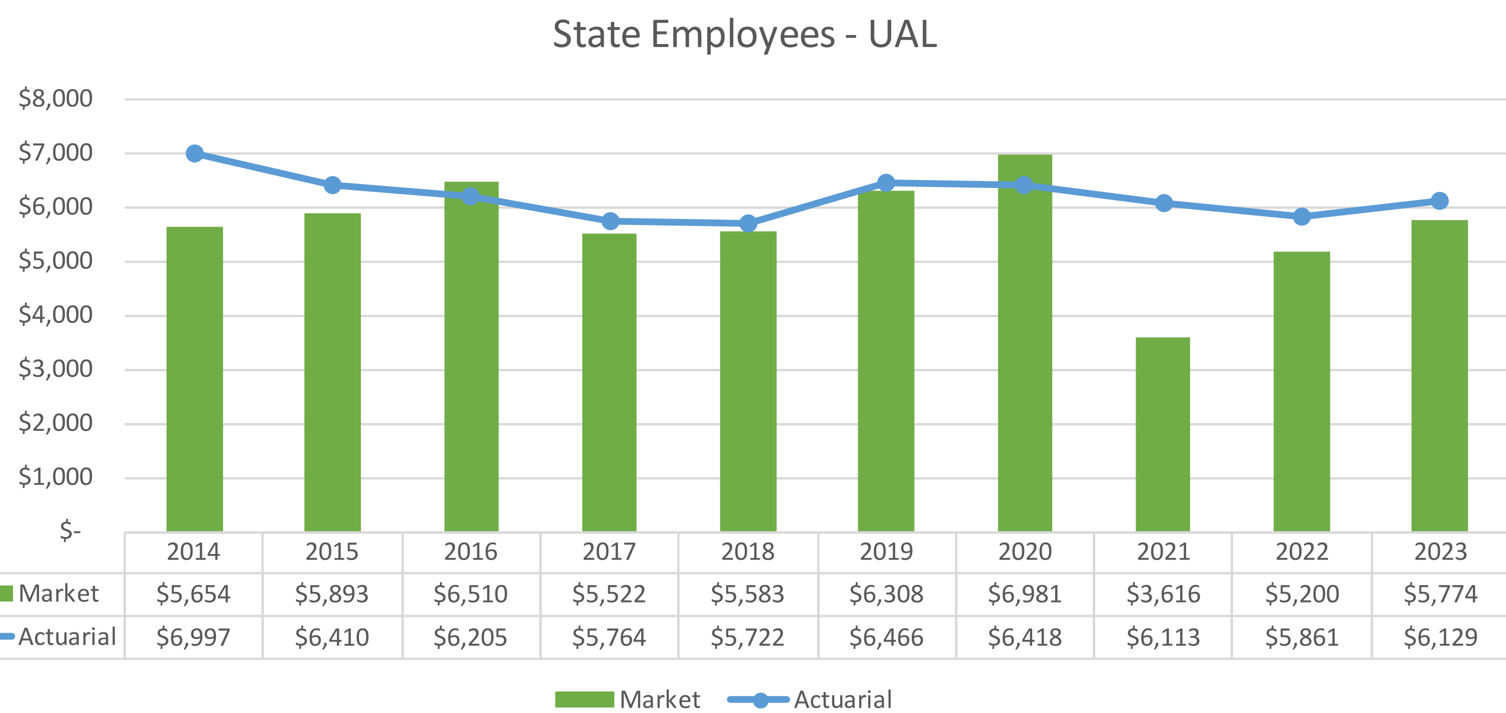
**2024-2027: Expect <u>$352 million</u> in deferred asset <u>*GAINS*</u>**
**Other VRS Plans had similar asset experience**

# Why We Smooth Asset Returns

*VRS Code Section 51.1-145:*

- *The total annual defined benefit employer contribution for each employer, expressed as a percentage of the annual membership payroll, shall be determined in a manner so as to remain relatively level from year to year.*

# Why We Smooth Asset Returns




| | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|---|---|---|---|
| Market | $5,654 | $5,893 | $6,510 | $5,522 | $5,583 | $6,308 | $6,981 | $3,616 | $5,200 | $5,774 |
| Actuarial | $6,997 | $6,410 | $6,205 | $5,764 | $5,722 | $6,466 | $6,418 | $6,113 | $5,861 | $6,129 |

Unfunded liabilities will trend to Market Value basis over time.
Other VRS Retirement Plans have similar patterns.

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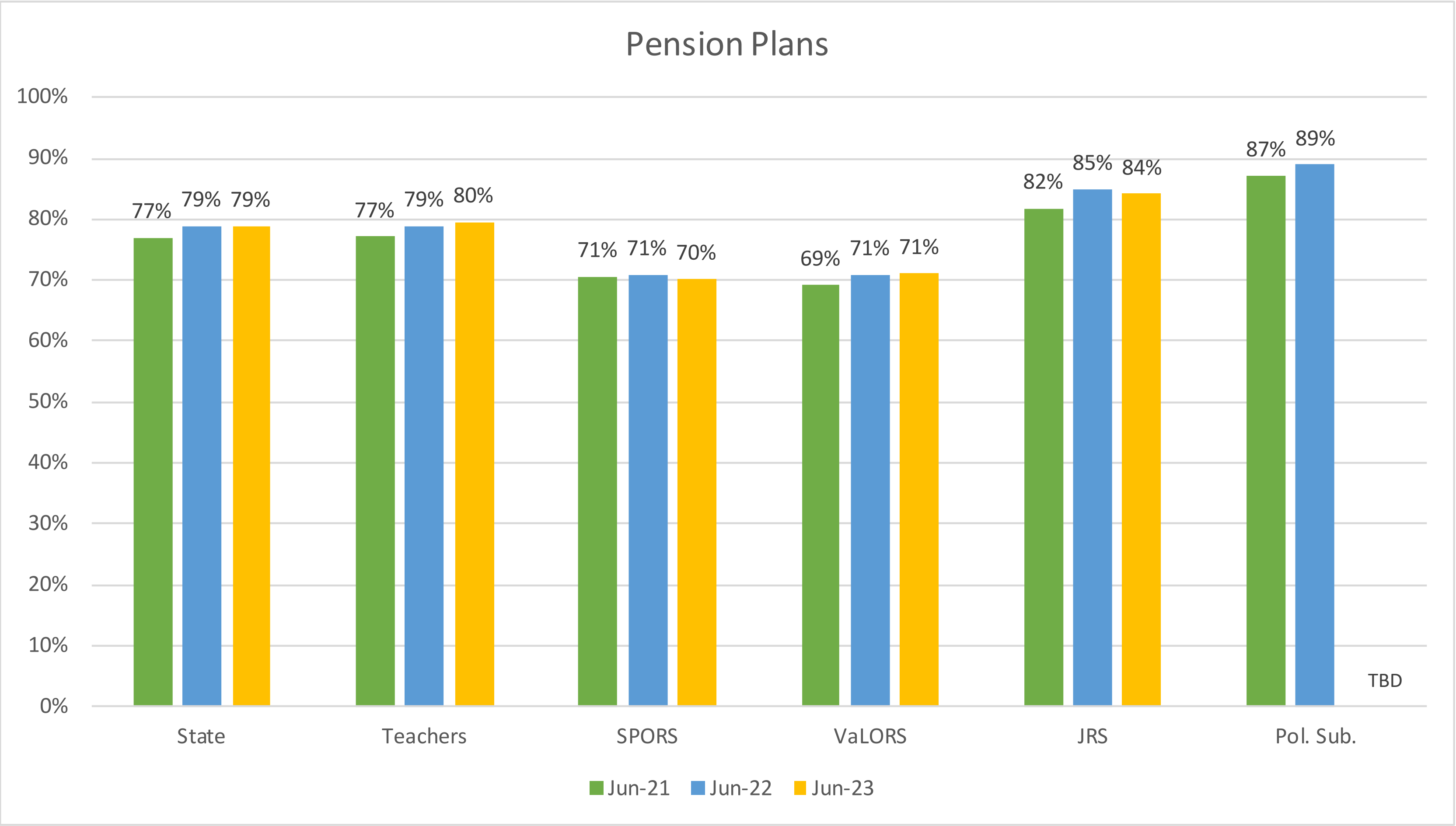
# Funded Status (AVA) – Pension Plans



# Calculated Employer Contributions

- Will vary significantly for System, Plan, and Employer based on:

  - Benefit Features
  - Demographics
  - Funded Status

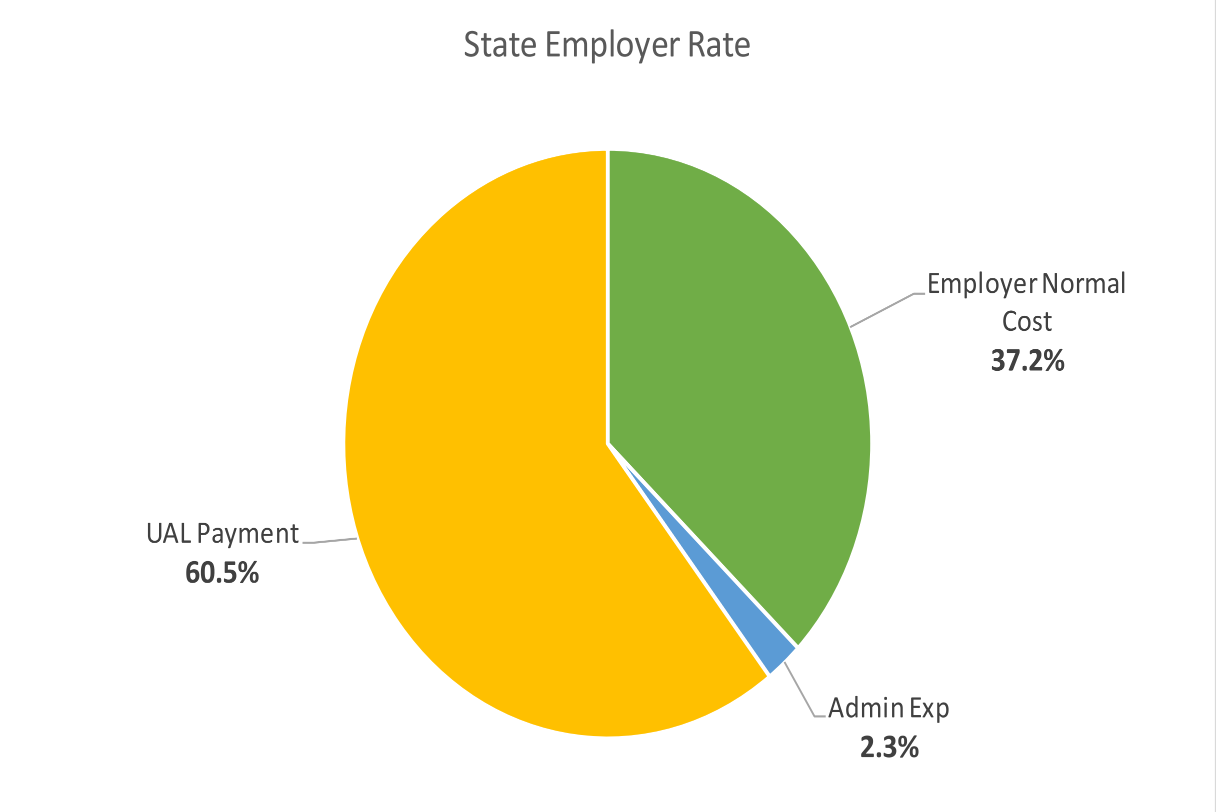
- Two Main Components:

  - Normal Cost – this represents the cost of the current year benefit earned by each active member
  - Amortization of Unfunded Liability – uses a systematic method (funding policy) to pay off the unfunded liability for each employer

# Legislative Updates

- HB 473 and SB 70 separate the employer contribution into Defined Benefit and Defined Contribution components effective for contribution rates beginning July 1, 2024
- HB 1630, SB 1289, SB 1479: Return to work
  - Required break in service reduced from 12 to 6 months for certain teacher groups
  - Specifies that the employer shall include such employees' compensation in membership payroll for purposes of the employer contributions to VRS

# Calculated Defined Benefit Employer Pension Contributions –State Employees




Normal Cost ultimately decreases to Plan 2/Hybrid level

| Component | % of Pay |
|---|---|
| Employer NC | 4.38% |
| Admin Exp | 0.27% |
| UAL Payment | 7.13% |
| Total | 11.78% |

UAL amortization payment = majority of the contribution for pension plans (other than JRS)

# Contribution Alternative

Managing unfunded accrued liabilities = Actuarial Value of Assets – Accrued Liability

- VRS uses “Layered amortization”
  - Amortized initial June 30, 2013 unfunded liability over a 30-year closed amortization period, but
  - 2014-2022 annual gains and losses, assumption changes amortized over separate closed 20-year periods
  - This methodology maintains steady progress toward eliminating the unfunded liability

# Contribution Alternative

## State EEs Pension Amortization Bases (2023)

| Description | | Original Amount | Outstanding Balance as of June 30, 2023 | Years Remaining June 30, 2023 |
|---|---|---|---|---|
| 2013 | Original Unfunded | $ 7,117,727,223 | $ 7,463,278,416 | 20 years |
| 2014 | Experience (Gain)/Loss | (414,716,278) | (346,031,947) | 11 years |
| 2015 | Experience (Gain)/Loss | (637,505,432) | (553,545,959) | 12 years |
| 2016 | Experience (Gain)/Loss | (87,589,562) | (78,605,380) | 13 years |
| 2017 | Assumption Change | 62,300,692 | 57,450,959 | 14 years |
| 2017 | Experience (Gain)/Loss | (570,456,389) | (526,049,801) | 14 years |
| 2018 | Experience (Gain)/Loss | (104,169,714) | (98,215,632) | 15 years |
| 2019 | Experience (Gain)/Loss | 15,231,288 | 14,619,334 | 16 years |
| 2019 | Assumption Change | 671,335,725 | 644,363,164 | 16 years |
| 2020 | Experience (Gain)/Loss | (90,660,484) | (88,327,231) | 17 years |
| 2021 | Experience (Gain)/Loss | (740,623,129) | (729,960,879) | 18 years |
| 2021 | Assumption Change | 401,835,129 | 396,050,180 | 18 years |
| 2022 | Experience (Gain)/Loss | (277,443,138) | (275,806,743) | 19 years |
| 2023 | Experience (Gain)/Loss | 249,375,746 | 249,375,746 | 20 years |
| **Total** | | | **$ 6,128,594,227** | |

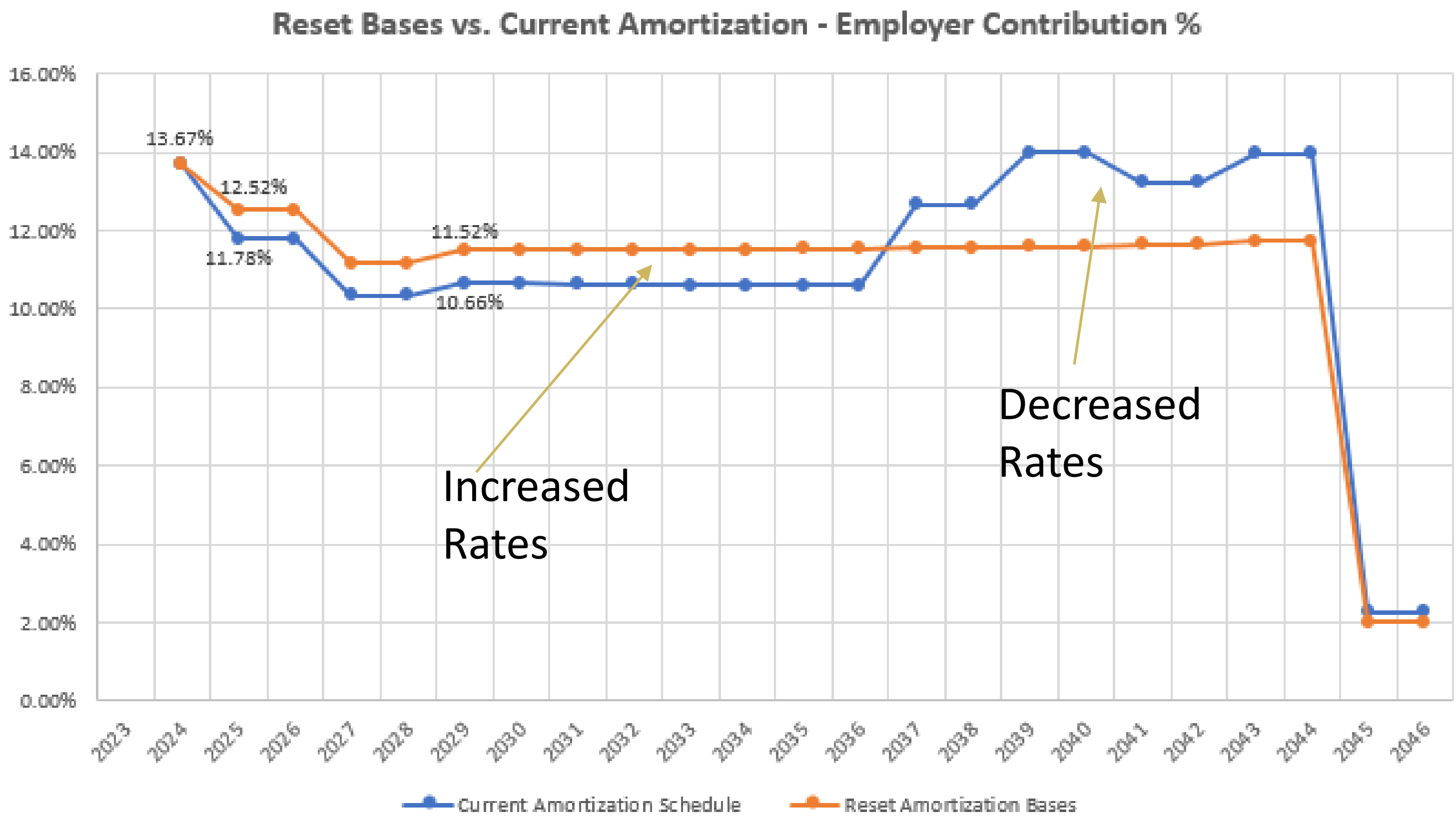
What if VRS “resets” all bases to 20 years?

# Contribution Alternative

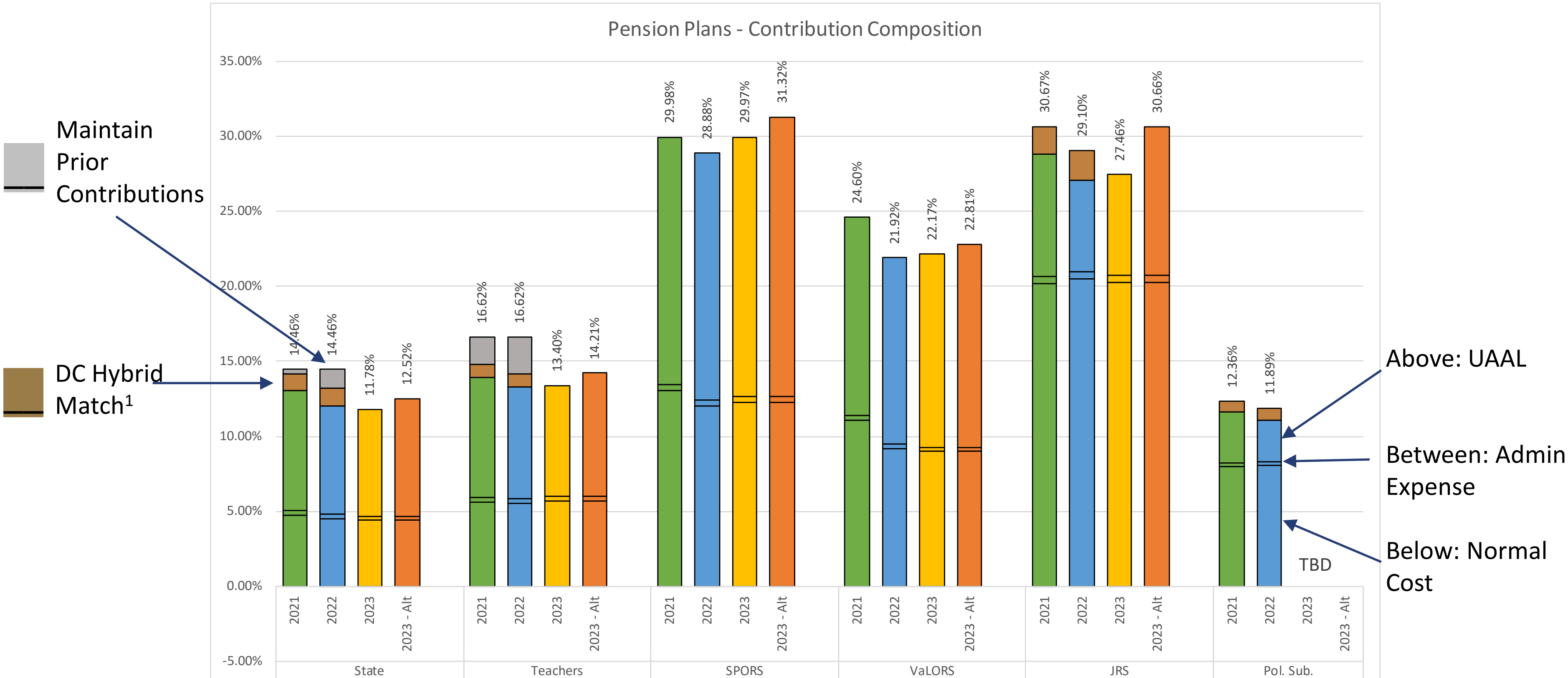
- If all assumptions are met
  - Projected contribution rates increase initially
    - But remain below current rates for State Employees and Teachers
    - Remain level, and well below out years projected rates
  - Projected contribution dollar savings of >~$1 billion over 20 years for State Employees and Teachers Systems

# Current and Alternate Projected Employer Contribution Rates (Fiscal Year)

## State Employees



# Actuarially Determined Employer Contribution Rates – Pension Plans




| | State | | | | Teachers | | | | SPORS | | | | VaLORS | | | | JRS | | | | Pol. Sub. | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2021 | 2022 | 2023 | 2023 - Alt | 2021 | 2022 | 2023 | 2023 - Alt | 2021 | 2022 | 2023 | 2023 - Alt | 2021 | 2022 | 2023 | 2023 - Alt | 2021 | 2022 | 2023 | 2023 - Alt | 2021 | 2022 | 2023 | 2023 - Alt |
| Normal Cost* | 5.05% | 4.77% | 4.65% | 4.65% | 5.91% | 5.82% | 5.96% | 5.96% | 13.43% | 12.45% | 12.64% | 12.64% | 11.38% | 9.49% | 9.27% | 9.27% | 20.67% | 20.98% | 20.74% | 20.74% | 8.23% | 8.30% | | |
| Accrued Liability | 8.02% | 7.28% | 7.13% | 7.87% | 8.04% | 7.45% | 7.44% | 8.25% | 16.55% | 16.43% | 17.33% | 18.68% | 13.22% | 12.43% | 12.90% | 13.54% | 8.14% | 6.13% | 6.72% | 9.92% | 3.39% | 2.77% | | |
| Total DB Portion | 13.07% | 12.05% | 11.78% | 12.52% | 13.95% | 13.27% | 13.40% | 14.21% | 29.98% | 28.88% | 29.97% | 31.32% | 24.60% | 21.92% | 22.17% | 22.81% | 28.81% | 27.11% | 27.46% | 30.66% | 11.62% | 11.07% | TBD | TBD |

* Includes Administrative Expense

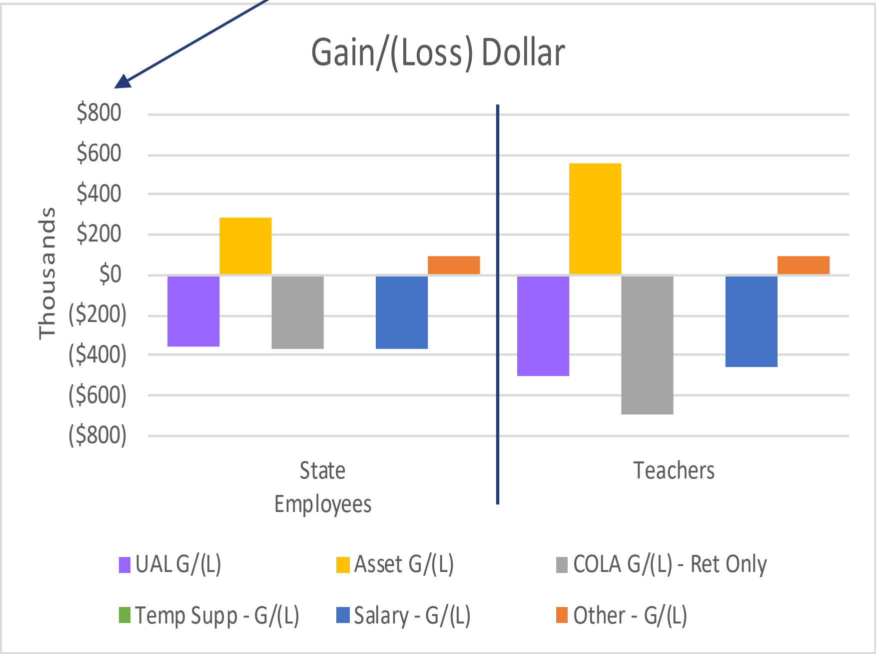
[1] Hybrid DC Match decoupled beginning 2023

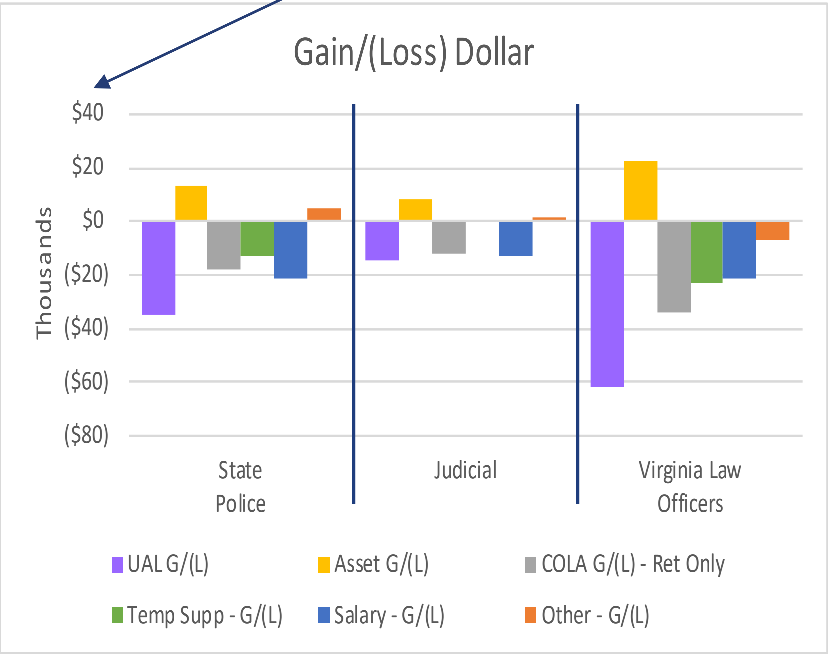
# Experience 2022-2023: Pension Plans (in $millions)

| | State | Teachers | SPORS | VaLORS | JRS |
|---|---|---|---|---|---|
| UAL Last Valuation | $ 5,861.3 | $ 11,792.1 | $ 416.6 | $ 718.0 | $ 110.9 |
| Prior Year (PY) Normal Cost | 488.8 | 1,024.6 | 28.8 | 56.5 | 21.9 |
| Actual PY ER Contributions | (903.1) | (2,013.4) | (54.2) | (108.2) | (27.6) |
| Extra Contributions | (73.1) | (147.5) | (3.7) | (6.6) | (2.1) |
| Interest | 395.7 | 792.2 | 28.1 | 48.4 | 8.0 |
| Expected UAL | 5,769.6 | 11,447.9 | 415.6 | 708.2 | 111.0 |
| UAL This Valuation | 6,128.6 | 11,950.8 | 450.0 | 770.2 | 125.2 |
| **Total (Gain)/Loss** | **$ 359.0** | **$ 502.9** | **$ 34.4** | **$ 62.0** | **$ 14.2** |
| – Asset (Gain)/Loss | $ (288.0) | $ (552.2) | $ (12.9) | $ (22.8) | $ (8.4) |
| – Liability (Gain)/Loss | $ 647.0 | $ 1,055.1 | $ 47.3 | $ 84.8 | $ 22.6 |

# Pension Gain/Loss Commentary ($000)

Scale for large plans is 5X-10X scale for small plans




Actual COLA/Assumption: Plan 1 = 5.0%/2.5%
Plan 2/Hybrid = 3.0%/2.25%
Actual Temp Supp/Assumption: 15.11%/5.1%

GRS

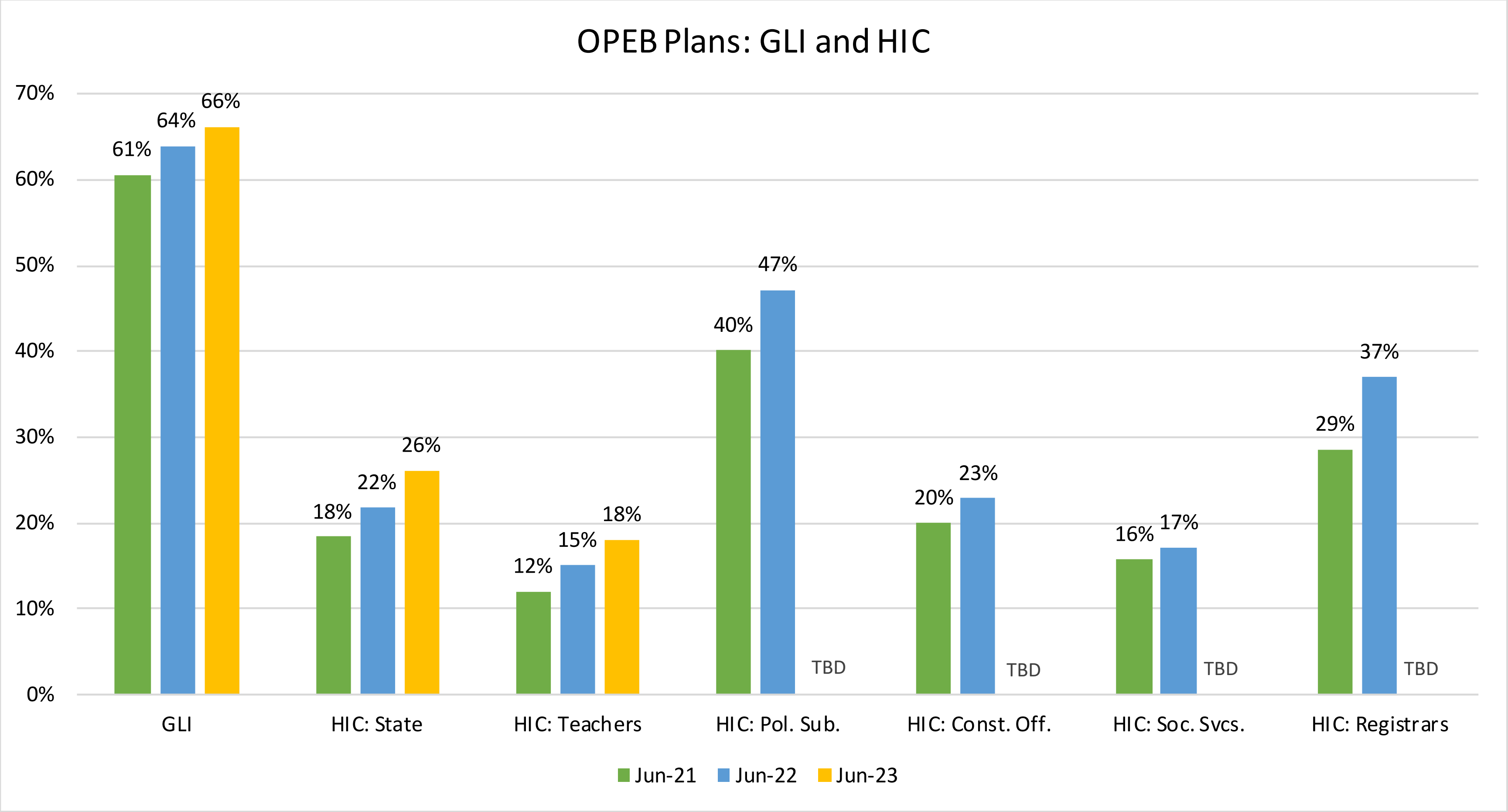
# OPEB: HIC Legislative Changes

- Increases the amount of monthly health insurance credits for certain retirees beginning July 1, 2024

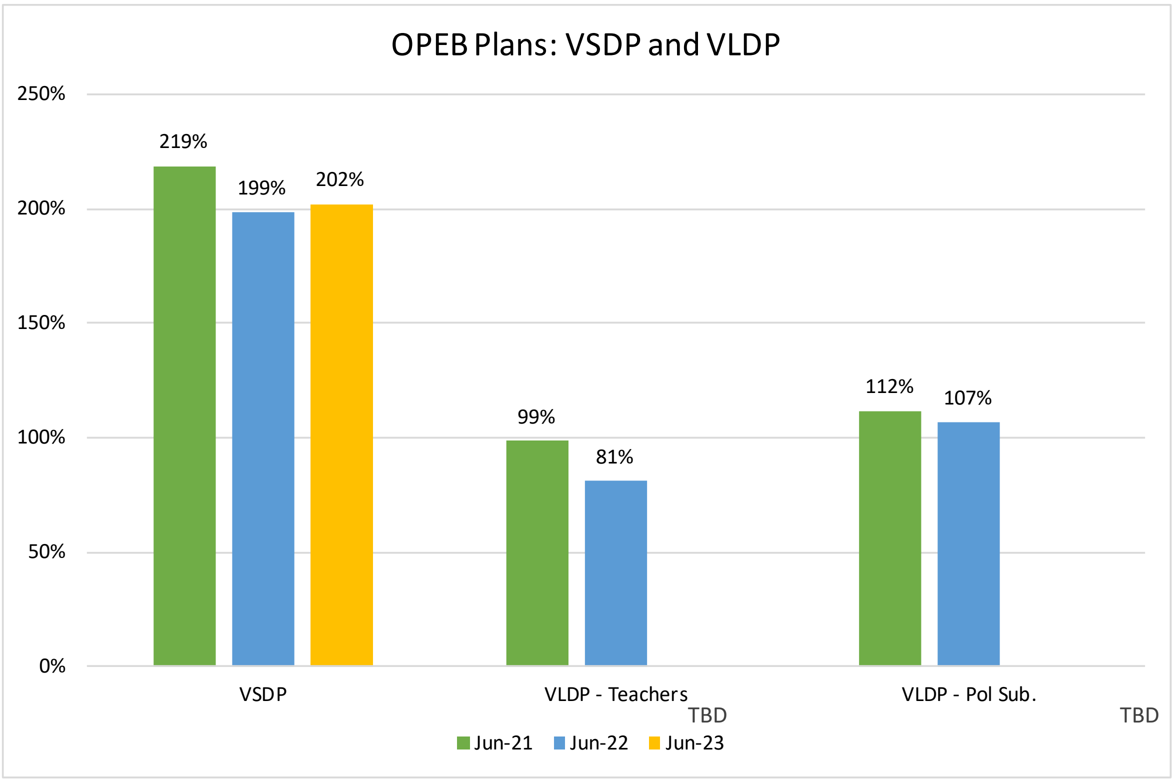
| Retired Group | Monthly Credit Increase | Maximum |
|---|---|---|
| Constitutional Officers | $1.50 to $1.75 | $52.50 |
| State Employees | $4.00 to $4.25 | No change |

GRS

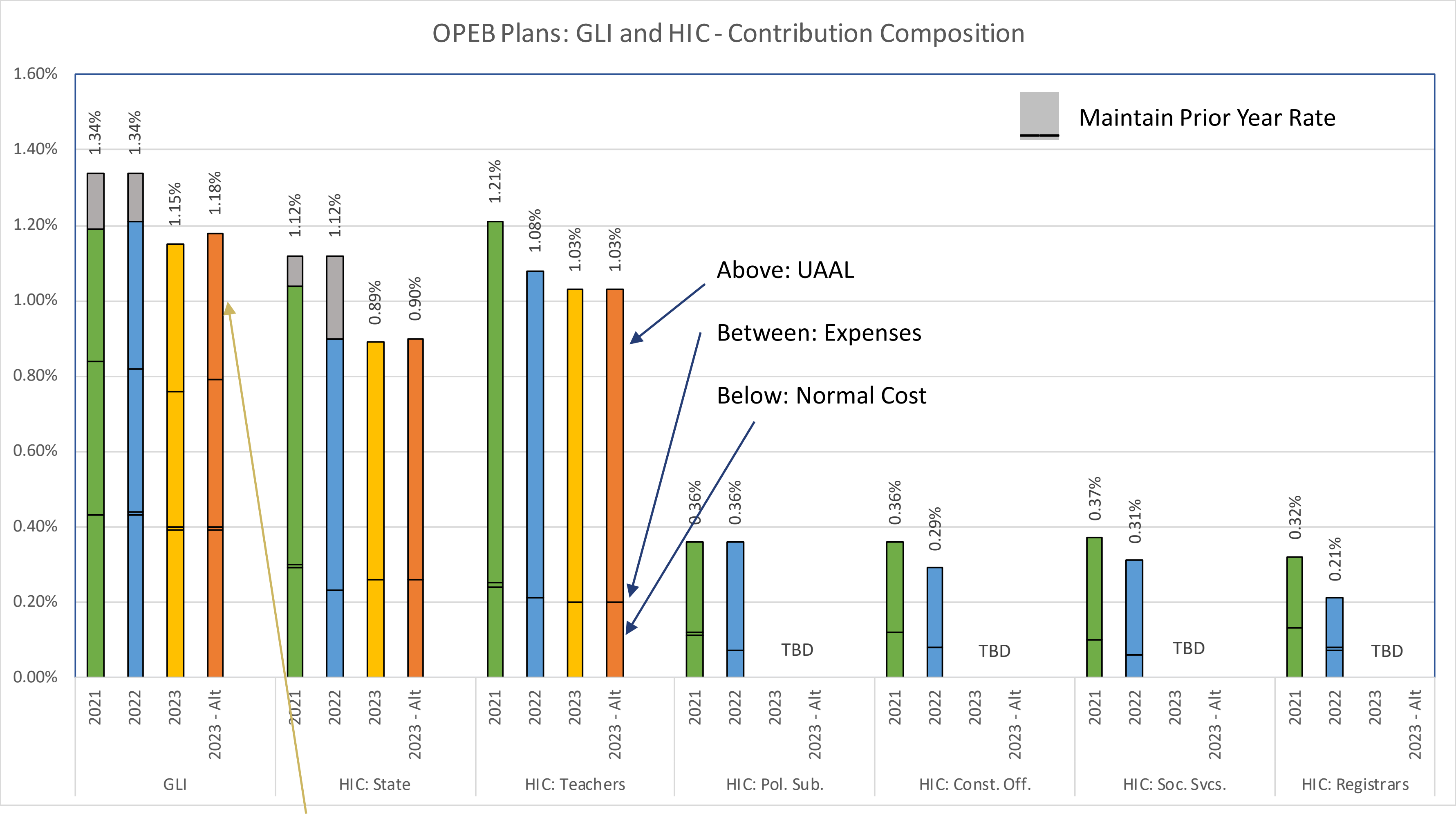
# Funded Status (AVA) – OPEB Plans



# Funded Status (AVA) – OPEB Plans

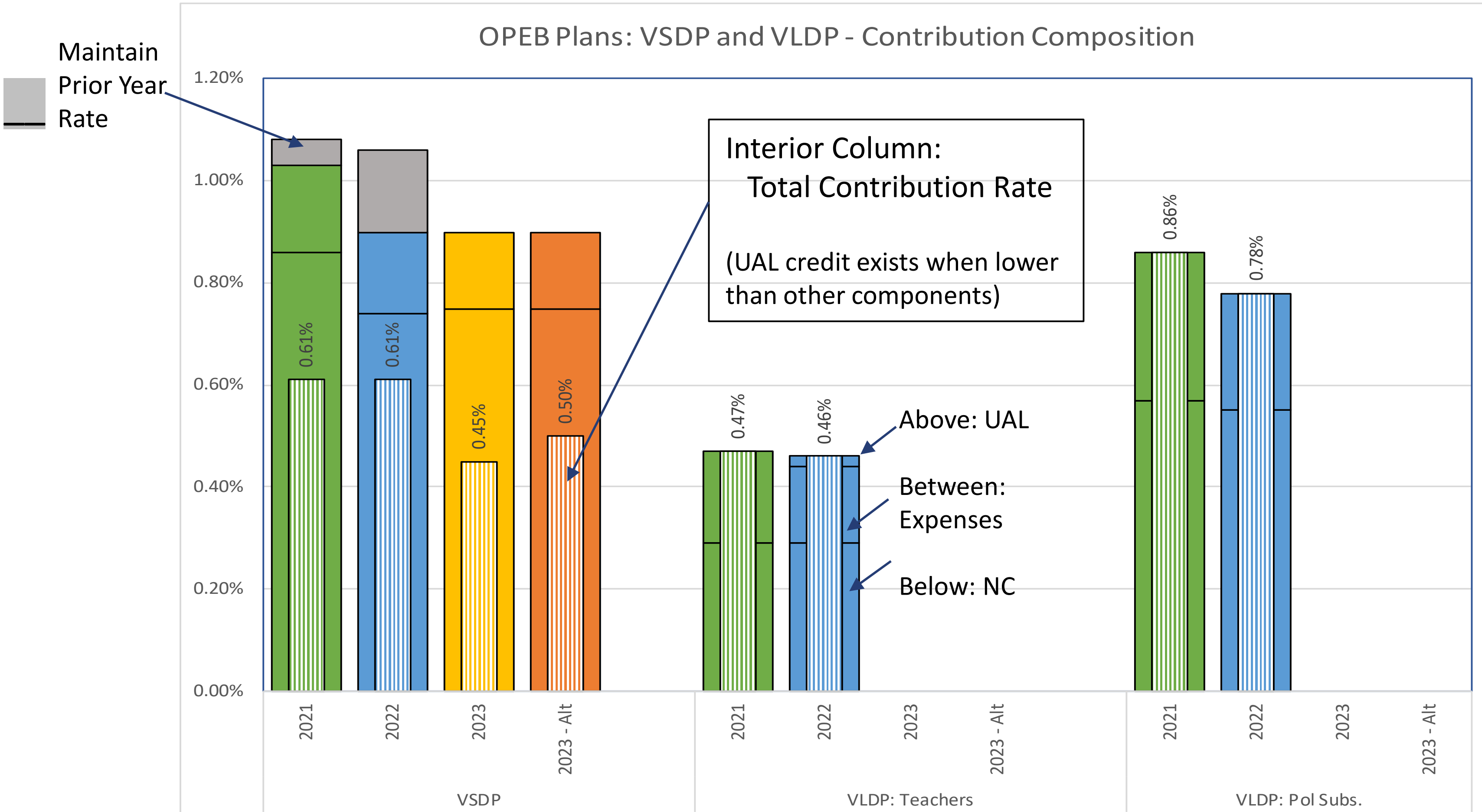


# Actuarially Determined Employer Contribution Rates – OPEB Plans




Note top 1/3 of GLI rate reflects active Life Insurance contribution

# Actuarially Determined Employer Contribution Rates – OPEB Plans



# Experience 2022-2023: OPEB (in $millions)

| | GLI | HIC: State | HIC: Teachers | VSDP |
|---|---|---|---|---|
| UAL Last Valuation | $ 1,349.0 | $ 802.2 | $ 1,237.0 | $ (291.2) |
| Prior Year (PY) Normal Cost | 88.5 | 17.1 | 18.2 | 33.3 |
| Actual PY ER Contributions | (235.5) | (92.0) | (120.3) | (24.1) |
| Extra Contributions | (10.1) | (27.2) | (4.0) | - |
| Interest | 157.9 | 100.1 | 101.0 | (5.8) |
| Expected UAL | 1,349.8 | 800.2 | 1,231.9 | (287.8) |
| UAL This Valuation | 1,357.7 | 797.4 | 1,196.3 | (316.5) |
| **Total (Gain)/Loss** | **7.9** | **(2.8)** | **(35.6)** | **(28.7)** |
| -- Asset (Gain)/Loss | (102.3) | (49.1) | (21.1) | (19.4) |
| -- Plan Change (Gain)/Loss | - | 68.3 | - | - |
| -- Liability (Gain)/Loss | 110.2 | (22.1) | (14.5) | (9.3) |

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# Pension Projections

## State Employees and Teachers

The following pages show projected pension contributions & funded status

- Liabilities are calculated at 6.75%
- Investment returns shown at assumed 6.75% rate, and 5.75%/7.75% for sensitivity
- Alternate Contribution rates (resets amortization bases) include Defined Benefit only
  - Defined Contribution decoupled from Employer Rate for 2023 valuation and going forward

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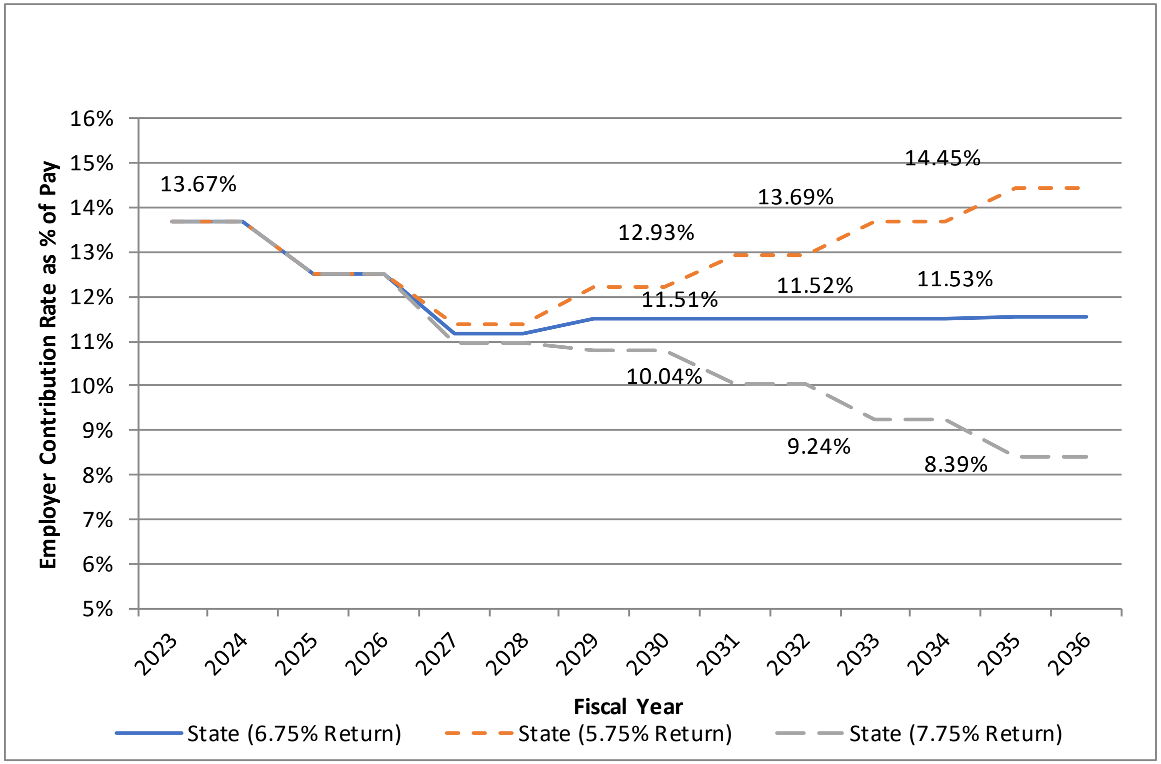
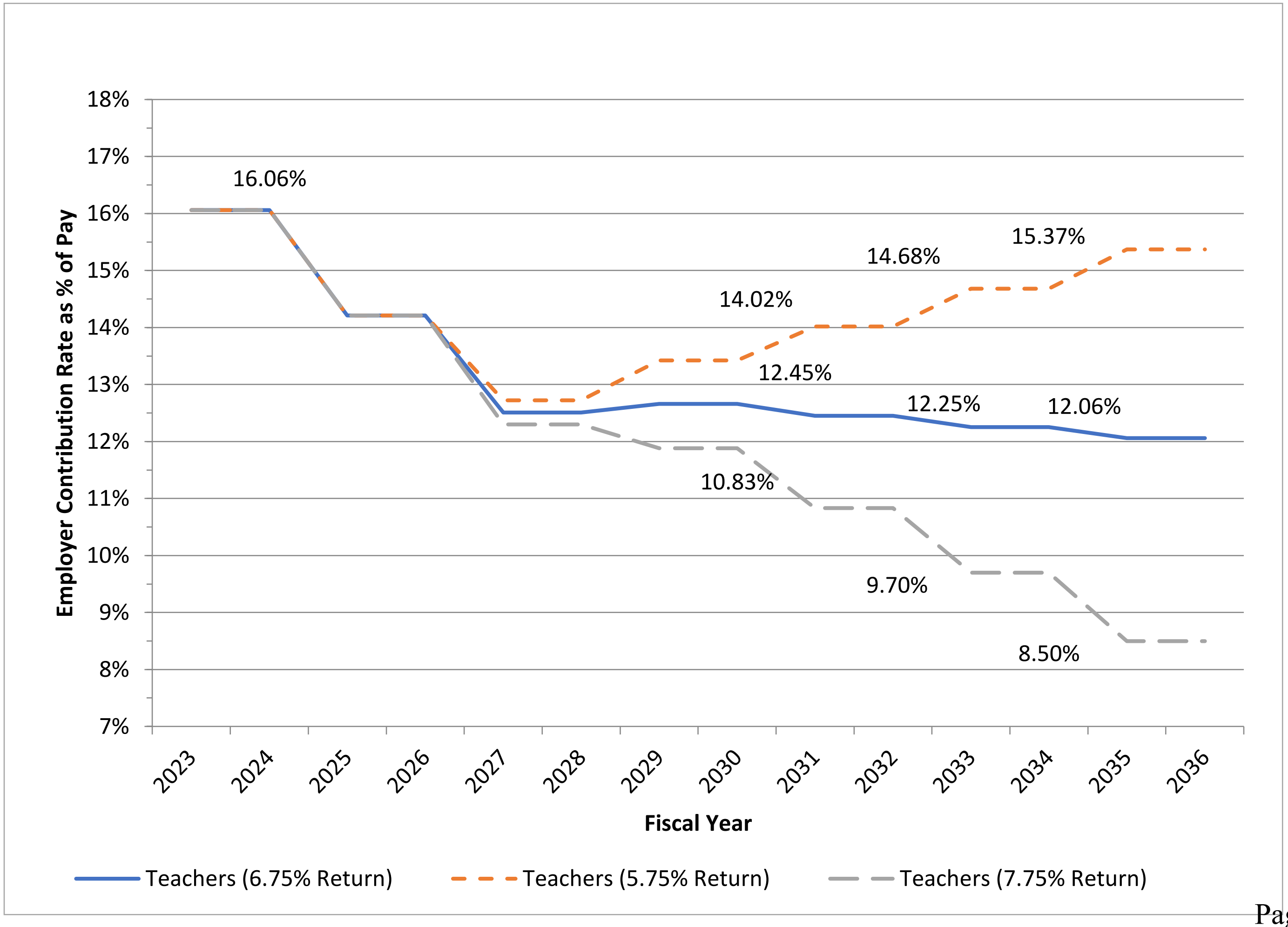
# Projected Employer Contribution Rates (Fiscal Year) – Defined Benefit Portion Only

## State Employees



# Projected Employer Contribution Rates (Fiscal Year) – Defined Benefit Portion Only

## Teachers

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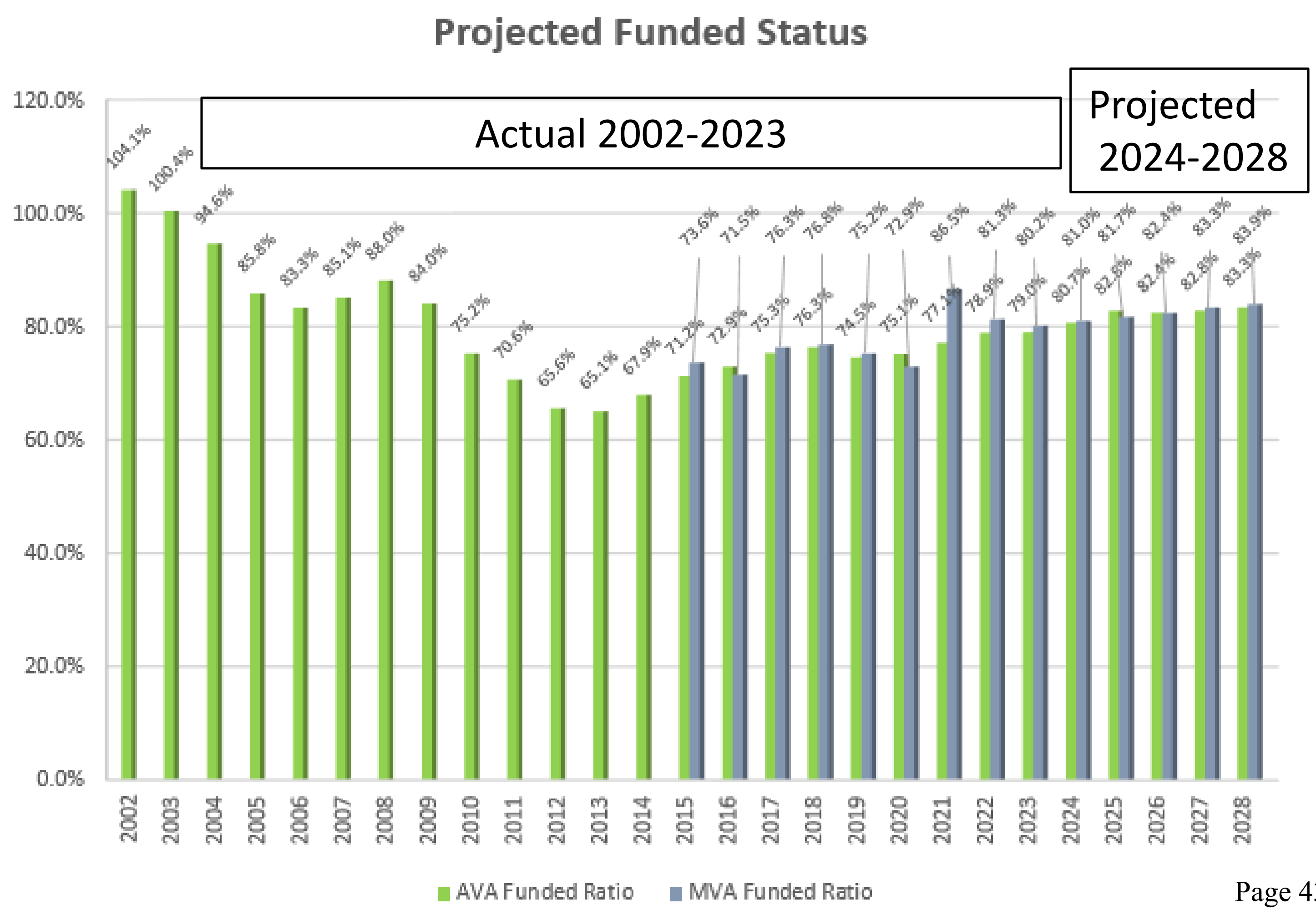
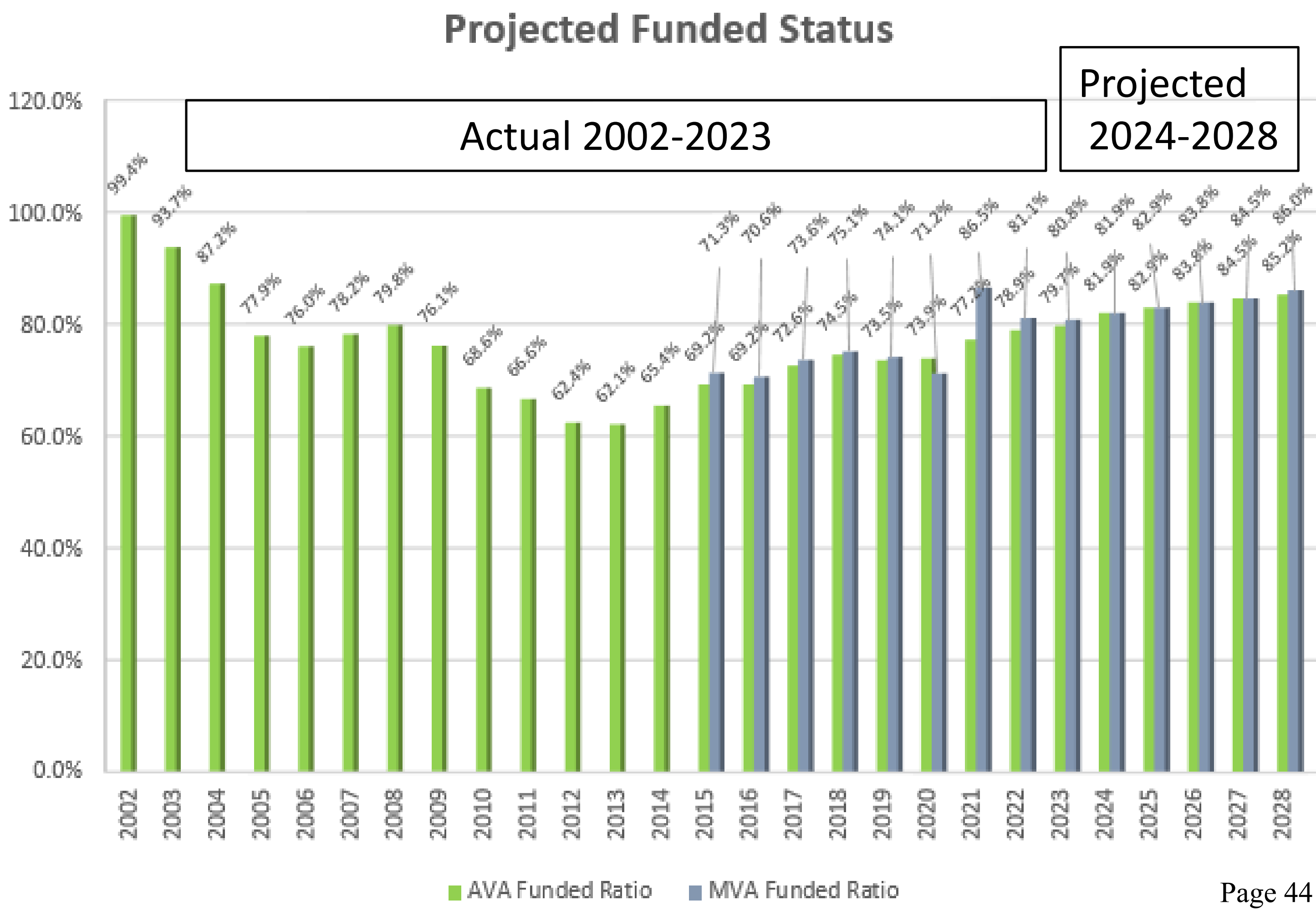
# Projected Pension Funded Status

## State Employees



# Projected Pension Funded Status

## Teachers



# Conclusion

1. **Maintained Funded Status on Actuarial Asset Basis**
   - Despite lower than expected returns for fiscal years 2021-2022, recognition of prior asset gains resulted in small gains
2. **Contributions**
   - Pension & OPEB rates are mostly consistent with last year's informational valuation
   - Generally, slightly lower rates than those currently being paid
   - DC Hybrid estimates have been decoupled from the DB rates for State, Teachers, and JRS
   - Alternative amortization schedule slightly increases rates in the short term but moderates rates in the long term and saves money over time


# HOT TOPICS

# Actuarial Standard of Practice 4 – LDROM

LDROM = Low-Default-Risk Obligation Measure

- Actuaries must disclose a liability using a discount rate tied to a low-default-risk index
- Amounts shown are based on Entry Age Normal and June 2023 Treasury Yield Curve Spot Rates (end of month)
  - 1-, 5-, 10-, 30-year rates = 5.29%, 3.99%, 3.61%, 3.84%

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# LDROM vs. AAL June 30, 2023 ($Billions)

| Measure | State | Teachers | SPORS | VaLORS | JRS |
|---|---|---|---|---|---|
| AAL | $29.1 | $58.8 | $1.5 | $2.7 | $0.8 |
| LDROM | $41.0 | $86.9 | $2.2 | $3.9 | $1.0 |

- Actuarial accrued liability (AAL) amount impacts contributions, UAAL, funded ratio
- LDROM represents a market-based measure of pension obligation
  - Does ***NOT*** impact contributions, UAAL, funded ratio
- Difference between AAL and LDROM illustrates anticipated savings by taking on risk in asset portfolio – added to Risk section of Pension Report

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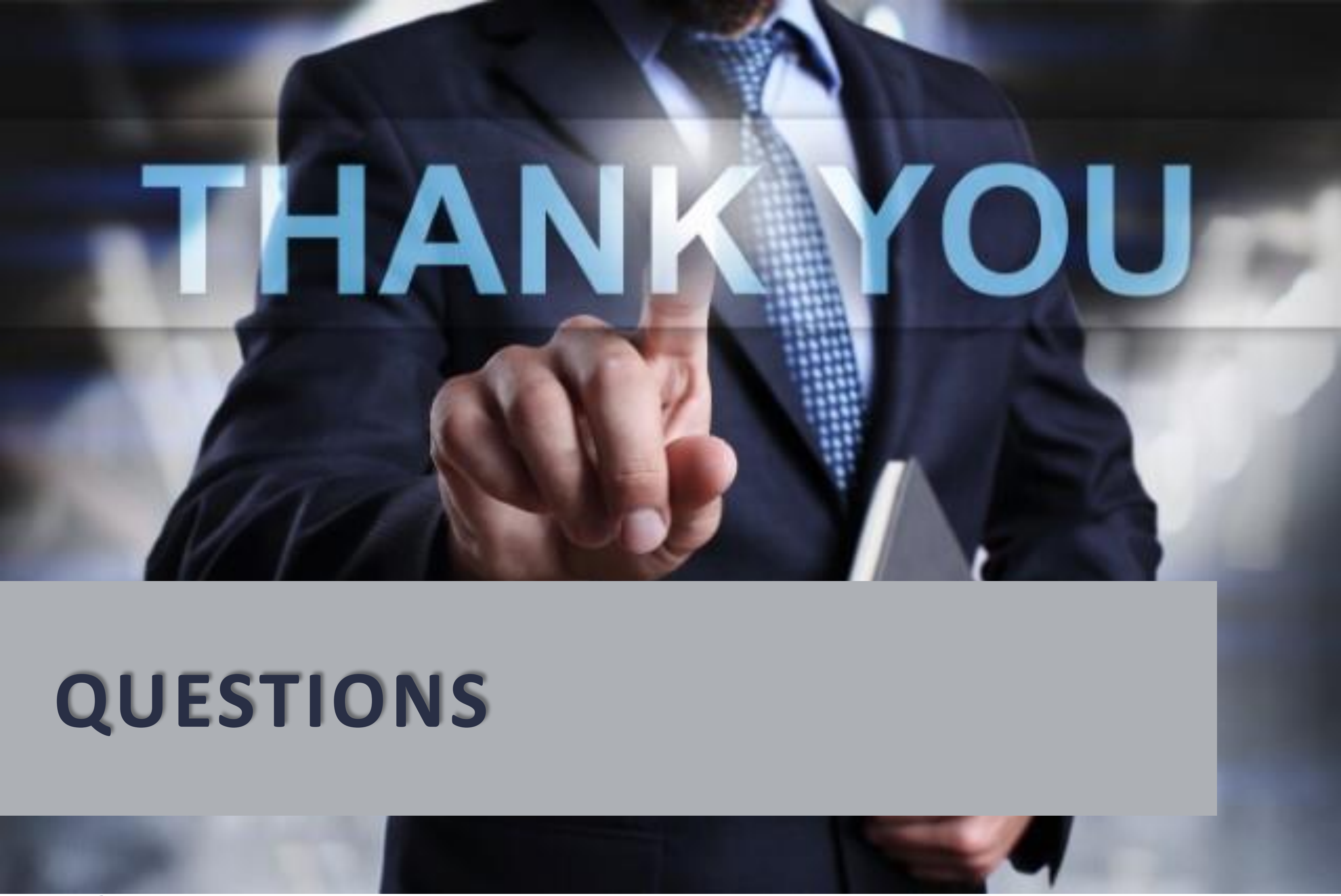
# August 2023 Study on COVID Mortality

- Excess mortality increased during the pandemic, but much less for the insured population
- Actuaries build in future improvements to current mortality rates into their calculations
- These rates of improvement have slowed over the last 5 to 10 years
- Next VRS experience study will be completed after the June 2024 valuation cycle




# QUESTIONS


# APPENDIX

# Contribution Alternative

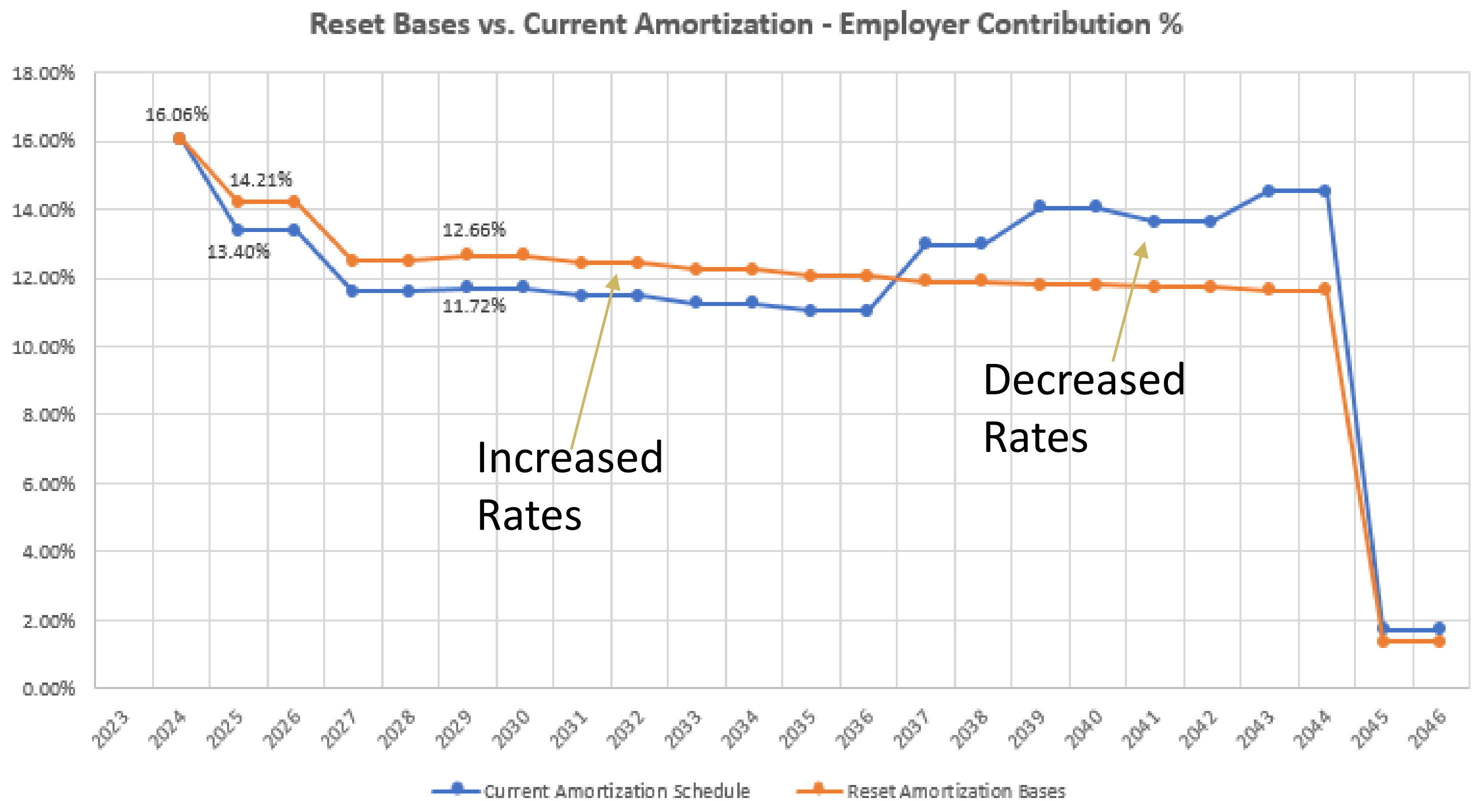
## Teacher Pension Amortization Bases (2023)

| Description | | Original Amount | Outstanding Balance as of June 30, 2023 | Years Remaining June 30, 2023 |
|---|---|---|---|---|
| 2013 | Original Unfunded | $ 14,493,629,234 | $ 15,197,265,483 | 20 years |
| 2014 | Experience (Gain)/Loss | (958,176,017) | (799,485,170) | 11 years |
| 2015 | Experience (Gain)/Loss | (1,043,509,874) | (906,079,611) | 12 years |
| 2016 | Experience (Gain)/Loss | (411,540,187) | (369,327,943) | 13 years |
| 2017 | Assumption Change | 104,287,885 | 96,169,702 | 14 years |
| 2017 | Experience (Gain)/Loss | (685,386,348) | (632,033,158) | 14 years |
| 2018 | Experience (Gain)/Loss | (554,684,143) | (522,979,773) | 15 years |
| 2019 | Experience (Gain)/Loss | (304,039,579) | (291,824,042) | 16 years |
| 2019 | Assumption Change | 1,469,767,609 | 1,410,716,084 | 16 years |
| 2020 | Experience (Gain)/Loss | 179,548,117 | 174,927,240 | 17 years |
| 2021 | Experience (Gain)/Loss | (2,139,250,000) | (2,108,452,664) | 18 years |
| 2021 | Assumption Change | 876,189,832 | 863,575,918 | 18 years |
| 2022 | Experience (Gain)/Loss | (1,024,579,997) | (282,873,759) | 19 years |
| 2023 | Experience (Gain)/Loss | 121,241,328 | 121,241,328 | 20 years |
| **Total** | | | **$ 11,950,839,635** | |

What if VRS “Resets” all bases to 20 years?

# Current and Alternate Projected Employer Contribution Rates (Fiscal Year)

## Teachers

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# Summary: Pension Plan Contribution Rates

| | FY 2023/2024 2021 Valuation | Informational 2022 Valuation | FY 2025/2026 2023 Valuation | FY 2025/2026 2023 Valuation Alternate |
|---|---|---|---|---|
| State | 14.46%* | 13.19% | 11.78% | 12.52% |
| Teachers | 16.62%* | 14.13% | 13.40% | 14.21% |
| SPORS | 29.98% | 28.88% | 29.97% | 31.32% |
| VaLORS | 24.60% | 21.92% | 22.17% | 22.81% |
| JRS | 30.67% | 29.10% | 27.46% | 30.66% |
| Pol. Sub (Weighted Avg) | 11.62% | 11.07% | TBD | TBD |

* State and Teachers contribution rates set at 2019 valuation level, increased from 14.13% and 14.76% respectively, and include DC rate for Hybrid members.

Note: Beginning with 2023 valuation the DC contribution for State, Teachers, and JRS has been decoupled

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# Summary: OPEB Contribution Rates

| | FY 2023/2024 | Informational | FY 2025/2026 | FY 2025/2026 |
|---|---|---|---|---|
| | 2021 Valuation | 2022 Valuation | 2023 Valuation | 2023 Valuation Alternative |
| Group Life Insurance | 1.34%* | 1.21% | 1.15% | 1.18% |
| Health Insurance Credit (HIC) | | | | |
| -- State | 1.12%* | 0.90% | 0.89% | 0.90% |
| -- Teachers | 1.21% | 1.08% | 1.03% | 1.03% |
| VSDP | 0.61%* | 0.45% | 0.45% | 0.50% |

* GLI, HIC-State, and VSDP contribution rates held at 2019 valuation level; computed contribution rate decreased to 1.19%, 1.04%, and 0.56% respectively

# Summary: Unfunded Pension Plan Liabilities ($000)

## Unfunded Liability

### (AVA)

| | 2022 | 2023 |
|---|---|---|
| State | $ 5,861,321 | $ 6,128,594 |
| Teachers | 11,792,090 | 11,950,840 |
| SPORS | 416,642 | 449,999 |
| VaLORS | 718,017 | 770,210 |
| JRS | 110,861 | 125,232 |
| Total | $ 18,898,931 | $ 19,424,875 |

### (MVA)

| | 2022 | 2023 |
|---|---|---|
| State | $ 5,199,844 | $ 5,774,483 |
| Teachers | 10,550,802 | 11,293,666 |
| SPORS | 387,081 | 434,126 |
| VaLORS | 666,103 | 742,651 |
| JRS | 91,593 | 114,836 |
| Total | $ 16,895,423 | $ 18,359,762 |

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# Summary: Unfunded OPEB Liabilities ($000)

## Unfunded Liability

### (AVA)

| | 2022 | 2023 |
|---|---|---|
| GLI | $ 1,349,005 | $ 1,357,720 |
| HIC - State | 802,184 | 797,401 |
| HIC - Teachers | 1,237,047 | 1,196,302 |
| VSDP | (291,190) | (316,522) |
| Total | $ 3,097,046 | $ 3,034,901 |

### (MVA)

| | 2022 | 2023 |
|---|---|---|
| GLI | $ 1,273,766 | $ 1,309,524 |
| HIC - State | 801,741 | 799,546 |
| HIC - Teachers | 1,235,793 | 1,196,910 |
| VSDP | (307,488) | (325,183) |
| Total | $ 3,003,812 | $ 2,980,797 |

# Pension Inactive Participants at June 30, 2023

| System | Plan 1 | Plan 2 | Hybrid | Total 2023 | Total 2022 | Percent Change |
|---|---|---|---|---|---|---|
| State | 15,968 | 22,829 | 24,378 | 63,175 | 60,176 | 5.0% |
| Teachers | 22,348 | 32,616 | 36,246 | 91,210 | 84,886 | 7.4% |
| SPORS | 270 | 492 | - | 762 | 750 | 1.6% |
| VaLORS | 2,609 | 10,516 | - | 13,125 | 12,273 | 6.9% |
| JRS | 12 | 1 | 1 | 14 | 14 | 0.0% |
| Pol. Sub. | TBD | TBD | TBD | TBD | 111,308 | TBD |
| Total | TBD | TBD | TBD | TBD | 269,407 | TBD |

*Includes counts for each plan from which members are entitled to deferred pension benefits. Members with benefits from more than one employer are counted more than once.*

# Pension Retired Participants at June 30, 2023

| System | Plan 1 | Plan 2 | Hybrid | Total 2023 | Total 2022 | Percent Change |
|---|---|---|---|---|---|---|
| State | 69,866 | 1,984 | 416 | 72,266 | 71,374 | 1.2% |
| Teachers | 107,853 | 2,420 | 403 | 110,676 | 108,579 | 1.9% |
| SPORS | 1,793 | 13 | - | 1,806 | 1,774 | 1.8% |
| VaLORS | 6,575 | 235 | - | 6,810 | 6,545 | 4.0% |
| JRS | 576 | 6 | 10 | 592 | 580 | 2.1% |
| Pol. Sub. | TBD | TBD | TBD | TBD | 83,667 | TBD |
| Total | TBD | TBD | TBD | TBD | 272,519 | TBD |

*Includes counts for each plan from which members receive pension benefits. Members with benefits from more than one employer are counted more than once.*

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# Disclaimers

- This presentation expresses the views of the authors and does not necessarily express the views of Gabriel, Roeder, Smith & Company.
- Future actuarial measurements may differ significantly from the current measurements presented in this report due to such factors as the following: plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the methodology used for these measurements (such as the end of an amortization period or additional cost or contribution requirements based on the plan's funded status); and changes in plan provisions or applicable law.

# Disclaimers

- This presentation is intended to be used in conjunction with the forthcoming actuarial valuation reports. This presentation should not be relied on for any purpose other than the purposes described in the valuation reports.
- This presentation shall not be construed to provide tax advice, legal advice, or investment advice.
- Jim Anderson and Becky Stouffer are independent of the plan sponsor, are Members of the American Academy of Actuaries (MAAA), and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

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## VRS Funding Policy Statement[1]

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### 1. Introduction

A plan funding policy determines how much should be contributed each year by employers and participants to provide for the secure funding of benefits in a systematic fashion.

The principal goal of a funding policy is to ensure that future contributions along with current plan assets are sufficient to provide for all benefits expected to be paid to members and their beneficiaries when due. The funding policy should seek to manage and control future contribution volatility to the extent reasonably possible, consistent with other policy goals. The actuarially determined contribution should be calculated in a manner that fully funds the long-term costs of promised benefits, while balancing the goals of 1) keeping contributions relatively stable and 2) equitably allocating the costs over the employees' period of active service.

The current funding policy used by the VRS Board sets contribution rates using the Entry Age Normal cost method, an investment return assumption of 6.75%, an inflation assumption of 2.5%, and a closed 20-year amortization period for unfunded liabilities (Legacy unfunded liabilities as of 6/30/13 are amortized over a closed 30-year amortization period.)

Article X, § 11 of the *Constitution of Virginia* provides that the Virginia Retirement System benefits shall be funded using methods which are consistent with generally accepted actuarial principles. Until 2012, the Annual Required Contribution (ARC) as described in the Governmental Accounting Standards Board's (GASB's) Statements No. 25 and No. 27 was a de facto funding policy for many public- sector retirement systems, including the Virginia Retirement System.

The Board sets contribution rates for all local employers under this policy. However, with respect to the plans for state employees and the teacher plan, while the rates developed under the Board's policy are the certified contribution rates, the Governor and the General Assembly determine the funding that they will provide through the state budget process toward the Board certified contribution rates for the State and Teachers and other statewide OPEB plans. Beginning in FY 2013, § 51.1-145.K1 of the Code of Virginia set out guidelines for the General Assembly to follow for the funding of the contribution rates certified by the VRS Board, phasing in from approximately 67% of Board-certified rate to 100% of the Board-certified rate over the next four biennia. These statutory guidelines do not apply to funding levels for Other Postemployment Benefits (OPEBs) administered by VRS.

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[1] Adopted October 17, 2013; amended November 14, 2013, June 7, 2016, November 15, 2017, November 20, 2019, ~~and~~ October 18, 2022, and October 18, 2023.

In June 2012, GASB revised public pension accounting standards and has communicated an important message in the process: accounting standards are no longer funding standards. However, GASB did not address how employers should calculate the annual required contribution (ARC). To assist state and local government employers, several national groups developed policy guidelines for funding standards. This document is the result of an extensive review of the current funding policy, industry standards and best practices, and the development and approval of funding policy assumptions effective with the June 30, 2013 valuation. A copy of Request for Board Action 2013-07-18 adopting the funding policy assumptions is attached. This Funding Policy is intended to provide guidance to future Boards on how to set employer contribution rates and support the plan's primary goals of contribution and budgetary predictability, accumulation of required assets over time to provide for all benefits earned and achievement of intergenerational equity.

In June 2015, GASB adopted two new statements regarding OPEBs. GASB statement 74, *Financial Reporting for Postemployment Benefits Other than Pension Plans*, and GASB statement 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. These statements replace GASB 43 and GASB 45. As was the case with GASB 67 and 68, these new statements represent a significant change to the methods used to account for postemployment benefits and provide for a clear separation between accounting for and funding of OPEBs. The new standards require the adoption of a new funding policy for OPEB plans. The current VRS funding policy has been modified to accommodate funding requirements for the VRS OPEB plans.

The VRS OPEB plans include the Health Insurance Credit Program, Group Life Insurance Program, the Virginia Sickness and Disability Program (VSDP), the Virginia Local Disability Program (VLDP) and the Long Term Care benefits associated with the VSDP and VLDP. The Line of Duty Act Fund is also a defined benefit OPEB plan, although it is not a benefit exclusively for VRS members.[2]

[2] As of April 2016 all VRS OPEBs already incorporate the actuarial methods outlined in the Funding Policy, with the following exceptions:

- Health Insurance Credit Program for Political Subdivisions will incorporate a five-year asset smoothing method for funding valuations effective with the June 30, 2016 actuarial valuation.
- The Long Term Care valuation will incorporate the Entry-Age Normal cost method and five-year smoothing method for funding valuations effective with the June 30, 2016 actuarial valuation.
- Line of Duty Act Program (LODA) is currently not prefunded and as set forth in the *Code* shall be funded on a current disbursement basis or in other words is considered a "pay-as-you-go" plan. As such, the plan has no unfunded liabilities and uses market value of assets for valuation purposes. In the event that the General Assembly takes action to begin prefunding this program, the Board of Trustees would move to adopt the various funding provisions contained in this document including moving the program to a five-year asset smoothing method for funding valuations effective with any decision to prefund the LODA program.

These changes were approved by the Board of Trustees at its June 7, 2016 meeting, and were incorporated into this amended Funding Policy. Where a particular actuarial method was already in use, the Funding Policy notes that the Board confirms the actuarial methods for OPEBs.

The Funding Policy addresses the following general policy objectives:

- □ Ensure funding of plans is based on actuarially determined contributions;
- □ Build funding discipline into the policy to ensure promised benefits can be paid;
- □ Maintain intergenerational equity so the cost of employee benefits is paid by the generation of individuals who receive services;
- □ Make employer costs a consistent percentage of payroll; and
- □ Require clear reporting to show how and when plans will be adequately funded.

This document serves as the Funding Policy for VRS. It has been prepared by VRS in collaboration with the Board and the VRS Plan Actuary and is effective as of the June 30, 2013 valuation, and modified to accommodate the OPEB plans effective as of the June 30, 2016 valuation.

## 2. Authority

The Virginia Retirement System is administered in accordance with Title 51.1, chapters 1, 2, 2.1, 3 and 4 of the *Code of Virginia*. The contribution to be paid by members of VRS is fixed at a level that covers only part of the cost of accruing benefits. The balance of the cost is paid by employers within the Trust Fund (the "Fund").

The OPEB plans are administered in accordance with Title 51.1, chapters 5, 11, 11.1, and 14 of the *Code of Virginia.* The cost associated with OPEBs is generally borne by the employer and benefits are paid from the various trust funds. An exception to this practice is the Group Life Insurance Program. The Board determines the amount each insured shall contribute for the cost of insurance and by statute this amount is capped at $0.70 per month for each $1,000 of annual salary. Each employer determines whether this cost will be paid by the member or funded by the employer. The balance of the cost is paid by employers within the Fund. The Group Life Insurance plan, however, is a cost-sharing plan so all employers are charged the same rate.

The Funding Policy focuses on the pace at which these liabilities are funded and, in so far as is practical, the measures to ensure that employers pay for their own liabilities.

The Funding Policy is authorized by a framework that includes:

- Article X, § 11 of the *Constitution of Virginia*
- Title 51.1 of the *Code of Virginia*

This is the framework within which the VRS Plan Actuary carries out valuations to set employer contribution rates and provide recommendations to the Board when other funding decisions are required. The Funding Policy applies to all employers participating in the Fund.

The methods and assumptions used in the VRS funding policy are periodically reviewed as part of the quadrennial experience study as required under § 51.1-124.22(A)(4). As such, the content of this document may be updated to reflect changes approved by the VRS Board of Trustees.

### 3. Contributions

The Funding Policy provides for periodic employer contributions set at actuarially determined rates in accordance with recognized actuarial principles (§51.1-145(A)). Originally based on parameters set out in GASB 25/27 and GASB 43/45, the contribution should include the employer's normal cost and provisions for amortizing any unfunded actuarial accrued liability (UAAL) in accordance with the requirements originally defined in GASB 25/27 and GASB 43/45.

Member and employer contributions for retirement are required by §§ 51.1-144 and -145 of the *Code of Virginia*. Chapters 5, 11, 11.1, and 14 of Title 51.1 of the *Code of Virginia* and the applicable provisions in each year's Appropriation Act relate to contribution requirements for OPEB plans administered by VRS.

Employer contributions are normally made up of two main elements[3]:

a) the estimated cost of future benefits being accrued, referred to as the "normal cost"; and

b) an adjustment for the funding position of accrued benefits relative to the Fund's actuarially adjusted assets, or the "amortization payment UAAL." If there is a surplus there may be a contribution reduction; if there is a deficit, there will be a contribution addition, with the amount of surplus or deficit being spread over a number of years.

Items a) and b) above are then combined and expressed as a percentage of covered payroll. Employer contribution rates are set each biennium and are in effect for the entire biennium. Valuations in the "off" years are for informational purposes only. Generally, employers with well-funded pension plans consistently pay their annual required contribution in full.

Where this process as applied to a political subdivision would, in the Plan Actuary's opinion, not be expected to maintain the plan's solvency, the VRS staff, working with the Plan Actuary, may determine alternative funding requirements that would maintain the political subdivision's solvency while also meeting the other objectives of this Funding Policy Statement.

With respect to statewide plans, if unfunded liabilities exist in a plan, the Board may recommend alternative contribution rates in excess of the actuarially determined rates if opportunities exist to accelerate paydown of unfunded liabilities. Examples of alternative rates could potentially include approaches such as maintaining rates from the prior year if rates drop in subsequent rate setting or maintaining a higher level contribution rate until a certain funded status is achieved.

[3] Contributions also include administrative expenses.

## 4. Funding Target

VRS operates the same target funding level for all ongoing employers of 100% of its accrued liabilities valued on an ongoing basis. This means that contribution rates are set with the intent of funding 100% of a member's benefits during a member's working lifetime. The Line of Duty Act Fund is an exception, as employer contributions are currently determined by the Board on a current disbursement basis per statute. As such, the target funding level for all ongoing employers for LODA is at or near 0% of its accrued liabilities.

Funded Status is defined as the ratio of the actuarial value of assets to the value placed on the benefits, or plan's liabilities, by the VRS Plan Actuary. The VRS Plan Actuary reports on the funded status of each plan in the system in each annual valuation.

## 5. Actuarial Cost Method

The actuarial cost method is the means by which the total present value of all future benefits for current active and retired participants is allocated to each year of service (i.e., the "normal cost" for each year) including past years (i.e., the "actuarial accrued liability"). There are several available actuarial cost methods, but most governmental plans use the entry age normal (EAN) cost method while a significant minority use the projected unit credit (PUC) method. In the past, VRS has used the EAN method for most of the plans it administers.

Although the EAN and PUC cost methods are both considered reasonable under actuarial standards of practice and GASB 25 and GASB 43 in most circumstances, it is important for plan stakeholders to understand the implications of either method. EAN tends to recognize actuarial liabilities sooner than PUC, and it also tends to result in a more stable normal cost pattern over time for pay-related benefits, even in the face of demographic shifts. The more stable normal cost pattern over time should help in reducing the risk of higher levels of future contributions.

Under the PUC method, the plan's normal cost is the present value of the benefits "earned" during the year, but based on projected pay levels at retirement. For an individual participant, the PUC normal costs increase each year because the present value increases as the participant gets a year closer to retirement. In contrast, under the EAN method, the normal cost is specifically determined to remain a level percentage of pay over each participant's career.

Because EAN normal cost rates are level for each participant, the normal cost pattern for the entire plan under EAN is more stable for pay-related benefits in the face of demographic shifts in the workforce. It is this normal cost stability that makes the EAN method the preferred funding method for pay-related benefits of public plans.

GASB has reaffirmed its decision to require governmental pension plans to base their financial statement reporting on the EAN method. For comparability, GASB has also decided to require governmental OPEB plans, which may not provide pay-related benefits, to base their financial statement reporting on the EAN method.

**Effective with the June 30, 2013 valuation, the Board has adopted the Entry-Age Normal cost method in deriving plan liabilities. This is a continuation of the Board's existing cost method. Effective with the June 30, 2016 valuation, the Board has adopted the Entry-Age Normal cost method for all OPEB plans.**

## 6. Asset Valuation Method

Because investment markets are volatile and because pension plans typically have long investment horizons, asset-smoothing techniques can be an effective tool to manage contribution volatility and provide a more consistent measure of plan funding over time. Asset-smoothing methods reduce the effect of short-term market volatility on contributions, while still tracking the overall movement of the market value of plan assets, by recognizing the effects of investment gains and losses over a period of years. This is also in keeping with § 51.1-145(A), which requires that contribution rates be determined in a manner so as to remain relatively level from year to year.

Determining the ideal asset-smoothing policy involves balancing the two goals of ensuring fairness across generations and controlling contribution volatility for plan sponsors. A very long smoothing period will greatly reduce contribution volatility, but this may mean the impact of recent investment experience is deferred to future generations. However, a very short smoothing period (or none at all) may result in contribution requirements that fluctuate dramatically from year to year.

Such volatility may also result from an asset-smoothing method that constrains how far the smoothed value differs from the market value by imposing a market value "corridor." A corridor is typically expressed as a ratio of the smoothed value of assets to the market value of assets. Actuarial standards of practice and related actuarial studies seek to identify asset-smoothing methods that achieve a reasonable balance between how long it takes to recognize investment experience (the smoothing period) and how much smoothing is allowed in the meantime (the corridor). The resulting smoothing periods are in the range of three to 10 years (with five the most common) and a corridor wide enough to allow the smoothing method to function except in the most extreme conditions.

While the smoothing period for governmental plans is not limited by federal laws or regulations, the Actuarial Standards Board has set out principles for asset smoothing in ASOP No. 44. Under these principles, when a smoothed asset valuation method is used, the actuary should select a method so that the smoothed asset values fall within a reasonable range of the corresponding market values and any differences between the actuarial value and market value of assets should be recognized within a reasonable period.

**Effective with the June 30, 2013 valuation, the Board has adopted a five-year asset smoothing period, which also includes a corridor that will restrict the smoothed value from falling below 80% of the true market value or exceeding 120% of the true market value. This is a continuation of the Board's existing asset valuation method. Effective with the June 30, 2016 valuation, the Board has adopted the same asset smoothing period and corridors for the OPEB plans, with the exception of the LODA program, which, by statute, does not prefund benefits. In the event a change to the statutory contribution requirements**

**of the LODA program necessitate an asset valuation method, the same asset smoothing period and corridors should be applied to the LODA program at that time.**

## 7. Amortization Method

Amortization of unfunded liabilities is a major component of the annual contribution. Amortization policies involve a balance between controlling contribution volatility and ensuring a fair allocation of costs among generations. The Plan Actuary uses the specific amortization periods adopted by the Board for all employers when developing a method over which to pay down any unfunded liabilities that may exist. The amortization period should allow adjustments to contributions to be made over periods that appropriately balance intergenerational equity against the goal of keeping contributions level as a percentage of payroll over time as required by § 51.1-145.

Amortization of the unfunded actuarial accrued liability (UAAL) determines how current and future UAAL will be paid off or "amortized," and so includes how changes in benefits or actuarial assumptions that affect the actuarial accrued liability should be funded over time. Even more than with asset smoothing methods, amortization policies involve a balance between controlling contribution volatility and ensuring a fair allocation of costs among generations. Longer amortization periods help keep contributions stable, but excessively long periods may inappropriately shift costs to future generations. In seeking to achieve an appropriate balance between these two important policy goals, a comprehensive amortization policy will involve the following distinct elements:

- □ Payment basis
- □ Payment structure
- □ Amortization period

A. Payment Basis: Level Dollar vs. Level Percent of Pay

One of the first considerations is whether amortization payments will be set at a level dollar amount (similar to a home mortgage) or as a level percent of pay. The great majority of public pension plans use level-percent-of-pay amortization where the payments toward the UAAL increase each year at the same rate as is assumed for payroll growth. Compared with the level-dollar approach, payments start at a lower dollar amount under the level percent approach, but then increase in proportion to payroll. The level-dollar method is more conservative in that it funds the UAAL faster in the early years. However, the level-percent-of-pay approach is consistent with the pay-related structure of benefits under most public plans. Moreover, because the normal cost is also determined as a level percent of pay, level percent amortization provides a total cost that remains level as a percentage of pay. In contrast, level- dollar amortization of UAAL will produce a total cost that decreases as a percentage of pay over the amortization period. A plan should balance these considerations in choosing between level-percent and level dollar amortization. Section 51.1-145(A) of the *Code of Virginia* provides in part that "[t]he total annual employer contribution for each employer, expressed as a percentage of the annual membership payroll, shall be determined in a manner so as to remain relatively level from year to year...."

**Effective with the June 30, 2013 valuation the Board has elected to use the level percent of pay payment basis. This is consistent with historical VRS practice. Effective with the June 30, 2016 valuation the Board confirms the continued use of the level percent of pay payment basis put in effect June 30, 2013 for the OPEB plans when an actuarially determined contribution is calculated.**

B. Payment Structure

Amortization policy must also consider how amortization payments should be structured. For example, a determination needs to be made as to whether the entire UAAL should be aggregated and amortized as a single amount, or whether the plan should track individual bases for each source of UAAL or surplus each year, and amortize these separately. Amortization periods can be fixed, open or "rolling" (with the amortization period restarted each year).

Although use of a single amortization base provides simplicity, use of separate amortization bases for each source of UAAL has the advantage of tracking separately each new portion of UAAL and providing another mechanism to stabilize contribution rates. Under this approach, over time there will be a series of bases, one for each year's gain or loss as well as for any other changes in UAAL. This provides useful information to stakeholders, as they can view the history of the sources of a plan's UAAL in any year. The use of separate amortization bases should help balance the annual ups and downs in the UAAL. In practice, the number of bases will be limited by the length of the amortization period as eventually bases will be fully amortized, and so will no longer be part of the UAAL.

Fixed amortization periods identify a date certain by which each portion of the UAAL will be funded. This can be contrasted with open or rolling amortization, whereby the plan "resets" its amortization period every year. This is analogous to a homeowner who refinances his mortgage each year. Although both methods are common in current practice, fixed amortization periods have the advantage of providing stakeholders with a clearer understanding of the ultimate funding target (full funding) and the path to get there. It is the structure required for private sector pensions, and is increasingly common for public pension plans.

**Effective with the June 30, 2013 valuation the Board has elected to use individual bases for each source of UAAL or surplus each year and to use fixed amortization periods rather than open or rolling periods. This is a change from past VRS practice but is consistent with industry best practices. Effective with the June 30, 2016 valuation the Board confirms the continued use of individual bases for each source of UAAL or surplus each year and the use of fixed amortization periods rather than open or rolling periods put in effect June 30, 2013 for all OPEB plans, with the exception of the LODA program, which, by statute, is currently not prefunded. For the purposes of accounting disclosures under GASB 43 and 45, the LODA program will continue to use an open period. In the event a change to the statutory contribution requirements of the LODA program necessitate a payment structure, individual bases for each source of UAAL or surplus each year and fixed amortization periods, rather than open or rolling periods, will be used by the LODA program at that time.**

C. Amortization period

Amortization period is a determination of the appropriate period of time over which amortization should occur. The answer can depend on the source of the UAAL being amortized, as discussed below:

UAAL Due to Actuarial Gains/ Losses

> Actuarial gains and losses arise when there is a difference between the actuary's estimates (assumptions) and the actual experience of the plan. They can result from demographic experience (e.g., the number of new retirees is higher or lower than expected), investment experience (e.g., returns that are higher or lower than expected), or other economic experience (e.g., payroll growth that is higher or lower than expected). In determining the appropriate period for amortizing gains and losses, plan sponsors should strike a balance between reducing contribution volatility (which would lead to longer amortization periods) and maintaining a closer relationship between contributions and routine changes in the UAAL (which would lead to shorter amortization periods). For many plans, amortization periods in the range of 15 to 20 years for gains and losses would assist plans in achieving a balance between these objectives.

UAAL Due to Changes in Actuarial Assumptions

> Assumption changes will result in an increase or decrease in the UAAL. Unlike gains and losses, which reflect actual past experience, assumptions are modified when future expectations about plan experience change. This amounts to taking the effect of future expected gains or losses and building it into the cost today. For that reason, and because of the long-term nature of assumption changes, a plan could be justified in using a longer amortization period than that used for actuarial gains or losses, perhaps in the range of 15 to 25 years.

Amortization of UAAL Due to Plan Amendments

> Because plan amendments are under the control of the plan sponsor, managing contribution volatility is generally not a consideration for plan amendments. This means that the primary rationale in selecting the period is to support intergenerational equity by matching the amortization period to the demographics of the participants receiving the benefit. This leads to shorter, demographically based amortization periods. For active participants, this could be the average future working lifetime of the active participants receiving the benefit improvement, while for retirees, this could be the average life expectancy of the retired participants receiving the benefit improvement. This approach would usually result in no longer than a 15-year amortization period for benefit improvements.

An equitable amortization policy should ensure that the UAAL will be paid off in a reasonable period of time. Long amortization periods can make paying down the UAAL appear more affordable, but, because interest charges accrue and compound on the unpaid UAAL, it is prudent to set amortization periods that are not excessively long. This is especially important where level percent of pay amortization is used.

In an effort to balance the need to pay down the current unfunded liability while managing already increasing contribution rates, the Board elected to manage the paydown of any unfunded liabilities created prior to June 30, 2013 over a 30-year closed period. In an effort to better manage intergenerational equity and to build funding discipline into the VRS policy, the Board also decided that future unfunded liabilities would be best amortized over 20-year closed periods.

With long amortization periods, the UAAL may increase during the early years of amortization period, even though contributions are being made to amortize the UAAL. This phenomenon, known as "negative amortization", occurs only with level percent of pay amortization. This happens because, under level percent of pay amortization, the lower early payments can actually be less than interest on the outstanding balance, so that the outstanding balance increases instead of decreases. For typical public plans, this happens whenever the average amortization period is longer than approximately 20 years.

While there is nothing inherently wrong with negative amortization in the context of a public plan, stakeholders should be aware of its consequences, especially for amortization periods substantially longer than 20 years. Negative amortization is a particular concern for plans using open, or rolling, amortization periods. As described above, plans that use open/rolling amortization methods "reset" to a new amortization period every year. By contrast, a plan using a closed amortization commits to paying down the UAAL over a fixed period.

**Effective with the June 30, 2013 valuation the Board has elected to amortize the legacy unfunded liability as of June 30, 2013, over a closed 30-year period. New sources of unfunded liability will be explicitly amortized over closed 20-year periods. The amortization period for the deferred contributions from the 2010-2012 biennium will remain a 10-year closed period. These amortization periods reflect a shift to closed amortization periods and tiered successive 20-year closed periods for new sources of unfunded liability. This is a change from past VRS practice of using a 20-year rolling method. Effective with the June 30, 2016 valuation the Board confirms the continuation of the amortizations put in effect June 30, 2013 for all OPEB plans, with the exception of the LODA program, which, by statute, is currently not prefunded. For the purposes of accounting disclosures under GASB 43 and 45, the LODA program will continue to use an open 30- year period. In the event a change to the statutory contribution requirements of the LODA program necessitate an amortization period, the LODA program will, at that time, explicitly amortize new sources of unfunded liability over closed 20-year periods.**

**Effective November 20, 2019, the Board amends this policy to clarify that amortization periods of explicit bases may be shortened in an effort to pay off unfunded liabilities of either pensions or OPEBs earlier than originally scheduled.**

**Effective October 18, 2022, the Board amends this policy to set the amortization period for unfunded liabilities generated by plan amendments to be 10 years rather than 20 years.**

**Effective October 18, 2023, the Board amends this policy for pension and OPEB plans to allow for the legacy unfunded liability, which was originally amortized over a 30-year period in 2013,**

**<u>and all subsequent amortization bases established between 2014 and 2023, which were initially amortized over 20 years, to be amortized over a new 20-year period. New layers will be established in future years according to the parameters of the funding policy. The reset would exclude unfunded liabilities being amortized over a shorter 10-year period associated with new employers or benefit enhancements elected by certain political subdivision employers.</u>**

## 8. Actuarial Assumptions

Setting actuarial assumptions is critical to the funding of a plan. Forward-looking assumptions about plan demographics, wages, inflation, investment returns and more drive the measurement of liabilities and costs, and therefore affect funding. Unlike the selection of funding methods, which involves a fair degree of policy discretion, the selection of assumptions should be based solely on best estimates of actual future experience. While it may be tempting to set assumptions based on how they might affect current contribution requirements, such "results-based assumption setting" should be avoided. ***It is the plan's actual experience that ultimately determines the cost of the benefits, so the assumptions should try to anticipate actual experience.*** Periodic reexamination of plan assumptions is an essential part of any plan's actuarial processes. As a general rule, many plans conduct an experience study every three to five years, an interval that should help ensure that assumptions remain appropriate in the face of evolving conditions and experience. VRS reviews assumptions every four years as required under § 51.1-124.22(A)(4).

All assumptions should be consistent with Actuarial Standards of Practice and reflect professional judgment regarding future outcomes.

VRS plans to continue experience studies once every four years as required by § 51.1-124.22(A)(4) to determine whether changes in the actuarial assumptions are appropriate.

Appendix A contains a chart summarizing some of the current assumptions used for the various benefit plans managed by the VRS.

Appendix B is RBA 2013-07-18, which documents the approval of VRS funding policy assumptions.

Appendix C is RBA 2013-11-26, which documents the approval of revisions to the VRS funding policy assumptions for political subdivisions.

Appendix D is RBA 2016-06-15, which documents the approval of VRS funding policy methods and assumptions with regard to the OPEB plans.

Appendix E is RBA 2016-06-16, which documents the Board's approval of changes to actuarial methods for certain OPEB plans.

Appendix F is RBA 2017-04-9, which documents the approval of VRS funding policy assumptions.

Appendix G is RBA 2019-10-13, which documents approval of a discount rate of 6.75% for actuarial valuations effective with the June 30, 2019 valuations.

Appendix H is RBA 2019 -11 -, which documents the approval of the use of shortened amortization periods for unfunded liabilities and maintaining prior contribution rates to assist in paying unfunded liabilities.

## 9. Additional Considerations

Where the Funding Policy Statement as applied to a political subdivision would, in the Plan Actuary's opinion, not be expected to maintain the plan's solvency, the Board authorizes the VRS staff, working with the Plan Actuary, to determine alternative funding requirements that would maintain the plan's solvency while also meeting the other objectives as stated in the Board's funding policy.

1. **Additional Funding Contribution** - The Additional Funding Charge is the contribution rate needed, if necessary, to allow the local system to use the plan's assumed Investment Return Rate as its Single Equivalent Interest Rate (SEIR) under GASB Statement No. 67. The additional funding contribution rate, if needed, allows for the use of the 6.75% investment return as the single equivalent investment return assumption for purposes of the GASB 67/68 statements. To determine the SEIR, the Fiduciary Net Position (FNP) must be projected into the future for as long as there are anticipated benefits payable under the plan's provisions applicable to the members and beneficiaries of the system on the Measurement Date. If the FNP is not projected to be depleted at any point in the future, the long term expected rate of return on plan investments expected to be used to finance the benefit payments may be used as the SEIR. If the FNP is projected to be depleted, an Additional Funding Charge is developed to avoid depletion.

2. **Surcharge for "At Risk" Plans** – Political subdivision plans identified as potentially "at-risk" due to low funded levels may require an additional surcharge or shortened amortization periods to bring the funding level of the plan to a sustainable level as determined by the Plan Actuary.

3. **Limitation on Benefit Enhancements Increasing Liability** - Benefit enhancements to a political subdivision pension plan that would have the effect of increasing the plan's liabilities by reason of increases in benefits, establishment of new benefits, changing the rate of benefit accrual, or changing the rate at which benefits become non-forfeitable may take effect during any plan year if the political subdivision's current funded ratio for such plan year would be at least 75 percent after taking into account such amendment.

   In order to increase benefits in circumstances where the funded ratio would be less than 75 percent after taking into account the amendment, the political subdivision would be required to make a lump sum contribution in the amount necessary to bring the funding level to 75 percent as of the effective date of the change, in addition to any increase in annual funding due to plan enhancements.

   Any accrued liability generated by the plan amendment that is not covered by the lump sum contribution will be amortized over no more than 10 years.

4. **Pension Plans for New Employers –**
   **Any new employer must have a funded status of at least 75 percent for pension benefits.** Any past service that is granted by the employer or purchased at the time the employer joins VRS must be at least 75 percent funded at the join date with the remaining amount amortized over no more than 10 years.

5. **Health Insurance Credit (HIC) Elections** –
   Any employer (new and existing VRS employers) that elects the HIC benefit is required to pay an initial contribution equal to the greater of two years of expected benefit payments or the amount required to reach at least 25 percent funded for its HIC plan, with the remainder of the unfunded liability amortized over no more than 10 years.

   In addition, Any employer (new and existing employers) that wishes to enhance the health insurance credit by electing the extra $1.00 of coverage per year of creditable service or expand coverage to additional non-covered members is required to meet the following requirements:
   - If the funded status of the plan is below 50% prior to the change, the employer must make an initial contribution equal to the full increase in the plan's liability associated with enhancing the HIC benefit.
   - If the funded status of the plan is greater than 50% but below 75% prior to the change, the employer must make an initial contribution equal to 50% of the increase in the plan's liability associated with enhancing the HIC benefit, with the remaining additional liability to be amortized over 10 years.
   - If the funded status of the plan is greater than 75% prior to the change, the employer must make an initial contribution in the amount necessary to keep the funded status at the 75% threshold after the change, with any remaining additional liability to be amortized over 10 years.

## 10. Conclusion

In funding defined benefit pension plans and OPEBs, governments must satisfy a range of objectives. In addition to the fundamental objective of funding the long-term costs of promised benefits to plan participants, governments also work to:

1. Keep employer's contributions relatively stable from year to year
2. Allocate pension costs on an equitable basis
3. Manage pension risks
4. Pay off unfunded liabilities over reasonable time periods

This Funding Policy was developed to help decision-makers understand the tradeoffs involved in reaching these goals and to document the reasoning that underlies the Board's decisions.

Adopted October 17, 2013

Amended November 14, 2013, June 7, 2016, November 15, 2017, ~~and~~ November 20, 2019, and October 18, 2022

| Policy | State | Teachers | SPORS | VALORS | JRS | Locals | | HIC | Group Life | VSDP | LODA |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | Non-LEOS | LEOS | | | | |
| Actuarial Cost Method | Entry-age Normal | | | | | | | | | | |
| Asset Valuation Method | 5 Year Smoothing 80/120 Corridor | | | | | | | | | | Market Value * |
| Amortization Method | 30 year decreasing each year down to 20 then remains open - Level % of Pay | | | | | | | | | | 30 Year Open Level % of Pay |

* LODA is statutorily required to be funded on a current disbursement or "pay-as-you-go" basis. Accordingly, the market value of assets is used.

| Actuarial Assumptions | State | Teachers | SPORS | VALORS | JRS | Locals | | HIC | Group Life | VSDP | LODA |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | Non-LEOS | LEOS | | | | |
| - Discount Rate | 6.75% | | | | | | | | | | 4.75% |
| - Payroll Growth Rate | 3.00% | | | | | | | | | | |
| - Inflation Assumption | 2.50% | | | | | | | | | | |
| - Salary Increases | Inflation rate of 2.5% plus real wage component of 1.0% & step-rate component that varies by Plan and Service | | | | | | | Same as Retirement Plans | | | N/A |
| Year 1 | 5.35% | 5.95% | 4.75% | 4.75% | 4.50% | 5.35% | 4.75% | | | | |
| Year 5 | 4.45% | 5.45% | 4.65% | 4.65% | 4.50% | 4.45% | 4.65% | | | | |
| Year 10 | 4.00% | 4.85% | 4.00% | 4.00% | 4.50% | 4.00% | 4.00% | | | | |
| Year 20 | 3.50% | 3.50% | 3.50% | 3.50% | 4.50% | 3.50% | 3.50% | | | | |
| - Cost-of-Living Adjustments | Plan 1 vested - 2.50% per year / Plan 1 non-vested & Plan 2 - 2.25% per year | | | | | | | N/A | N/A | Same as Retirement Plans | N/A |
| - Mortality Rates | RP 2014 Mortality Table projected to 2020 for males and females | | | | | | | | | | |
| * Pre Retirement | Adjustments vary based on employer group and gender | | | | | | | | | | |
| * Post Retirement | Adjustments vary based on employer group and gender | | | | | | | Adjustments similar to retirement plans, by group covered | | | |
| * Post Disability | RP 2014 Disability Table with varying setbacks based on employer group and genders | | | | | | | | | | |
| - Withdrawal Rates | **"Experience Related"** Varies by Plan, Gender and Service at Retirement | | | | | | | | | | |
| - Disability Rates | **"Experience Related"** Varies by Plan, Gender and Age at Disability | | | | | | | | | | |
| - Retirement Rates | **"Experience Related"** Varies by Plan, Gender, Age and Service at Retirement | | | | | | | | | | |

## Appendix B

Appendix B is RBA 2013-07-18, which documents the approval of VRS funding policy assumptions.



## REQUEST FOR BOARD ACTION

## Requested Action

**The VRS Board of Trustees approves its plan actuary's and VRS staff recommendations, which are consistent with industry best practices, to use the Entry Age Normal Actuarial Cost Method and the five-year asset smoothing method; and to amortize the legacy unfunded liability over a closed 30-year period, with new sources of unfunded liability explicitly amortized over closed 20-year periods, effective with the June 30, 2013 valuation. Lastly, the 10-year payback of the retirement contribution payments deferred for the 2010-12 biennium will remain as a separate 10-year closed amortization period ending in FY 2020.**

Description/Background

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 67, *Financial Reporting/or Pension Plans,* which addresses financial reporting for state and local government pension plans, and Statement No. 68, *Accounting and Financial Reporting/or Pensions,* which establishes new accounting and financial reporting requirements for governments that provide their employees with pensions. The guidance contained in these Statements will change how governments calculate and report the costs and obligations associated with pensions in important ways. Statement No. 67 replaces the requirements of Statement No. 25, *Financial Reporting/or Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans,* for most public employee pension plans. Statement No. 68 replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers,* for most government employers. The new Statement Nos. 67 and 68 made a definitive separation between funding for and accounting of pensions and moved away from defining an "annual required contribution" (ARC) that was used by many public sector employers, including the Virginia Retirement System, as a de facto "funding policy." Accordingly, the VRS Board has undertaken a review of its current funding policy and seeks to develop a written policy. The funding policy has significant implications related to contribution rates and funded status.

Beginning in February 2013, the VRS Benefits and Actuarial Committee began a review of the VRS Funding Policy. The process included a summarization of the current VRS funding policy; an overview of the various components that go into the development of a funding policy; as well as a review of recommendations provided by a Pension Funding Task Force which was created by national associations representing local and state governments. The Task Force was created to provide funding policy guidelines to fill the void created by GASB when it updated its pension accounting standards in 2012.

The Benefits and Actuarial Committee discussed the three core elements of pension funding: the actuarial cost method, the asset smoothing method and the amortization policy. Special consideration was given to the amortization policy as it is the only area where the Task Force's recommendation differs from current VRS funding policy and methodology.

As a result of its review, the Benefits and Actuarial Committee recommends that the Board adopt the following principles: use of the Entry Age Normal actuarial cost method; use of the five-year asset smoothing method; and amortization of legacy unfunded liability over a thirty-year closed period, with new sources of unfunded liability explicitly amortized over twenty-year closed periods. The IO-year payback of the retirement contribution payments deferred for the 2010-12 biennium will remain as a separate 10-year closed amortization period, ending in fiscal year 2020_.This change in the amortization methodology is designed to maintain contribution rates in the near term, improve the plan's funded status, and create intergenerational equity.

Rationale for Requested Action

Article X, § 11 of the *Constitution of Virginia* establishes that the Virginia Retirement System benefits shall be funded using methods which are consistent with generally accepted actuarial principles. VRS has relied on GASB Standard Nos. 25 and 27 as a de facto funding policy. In June 2012, GASB updated its pension accounting standards. The new Standard Nos. 67 and 68 made a definitive separation between funding for and accounting of pensions and moved away from defining an "annual required contribution" (ARC) that was used by many public sector employers, including the Virginia Retirement System, as a de facto funding policy. The change in GASB standards necessitates the review of current funding practices and development of a written VRS funding policy.

Authority for Requested Action

The Board's authority for this action is contained in:

- Article X, § 11 of the *Constitution of Virginia,* establishing that the Virginia Retirement System benefits shall be funded using methods which are consistent with generally accepted actuarial principles;
- § 51.1-145 of the *Code of Virginia,* providing additional details on the basis for employer contributions; and
- § 51.1-124.22 of the *Code of Virginia* empowers the Board to promulgate regulations and procedures and make determinations necessary to carry out the provisions of Title 51.1 and adopt rules and policies that bring the Retirement System into compliance with any applicable law or regulation of the Commonwealth or the United States.

The above action is approved effective July 11, 2013.

Diana F. Cantor, Chair
VRS Board of Trustees

## Appendix C

Appendix C is RBA 2013-11-26, which documents the approval of revisions to the VRS funding policy assumptions for political subdivisions.

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(14 pages)

## Appendix D

Appendix D is RBA 2016-06-15, which documents the approval of VRS funding policy methods and assumptions with regard to the OPEB plans.

2

(3 pages)

## Appendix E

Appendix E is RBA 2016-06-16, which documents the Board's approval of changes to actuarial methods for certain OPEB plans.

2

(3 pages)

## Appendix F

Appendix F is RBA 2017-04-9, which documents the approval of VRS funding policy assumptions.

(2 pages)

## Appendix G

Appendix G is RBA 2019-10-13, which documents approval of a discount rate of 6.75% for actuarial valuations effective with the June 30, 2019 valuations.

**Request for Board Action**
**RBA 2019-10-13**

Virginia Retirement System

**Approve a reduction in the actuarial assumed rate of return from 7.00% to 6.75%, effective as of July 1, 2019, to be applied beginning with the 2019 actuarial valuations.**

### Requested Action

The Board approves a reduction in the actuarial assumed rate of return from the current 7.00% to 6.75%, effective as of July 1, 2019, to be applied beginning with the 2019 actuarial valuations.

### Description/Background

The Investment Policy Committee (IPC) conducted a series of luncheon meetings in February, May and June 2019. Overall asset/liability modeling, which included the actuarial assumed rate of return, was the subject of significant discussion during each of those meetings. In addition, the Investment Advisory Committee (IAC) discussed forward looking returns in its April 2019 meeting.

An asset/liability study presented by Verus to a joint meeting of the IAC and the IPC on August 13, 2019 served as a catalyst for continued robust discussion among IAC and IPC members regarding the actuarial assumed rate of return. Factors considered by the members included the effect of a change in the assumed rate of return on current and projected contribution rates and funded status, as well as historical trends and projections with respect to portfolio returns under several asset mix alternatives, especially in light of the related changes to the policy portfolio effective January 1, 2020.

### Authority for Requested Action

Article X, § 11 of the *Constitution of Virginia,* which establishes that VRS benefits shall be funded using methods which are consistent with generally accepted actuarial principles, and *Code of Virginia* § 51.1-124.22(A)(8), which authorizes the Board to promulgate regulations and procedures and make determinations necessary to carry out the provisions of Title 51.1.

The above action is approved.

Mitchell L. Nason, Chairman
VRS Board of Trustees

10/10/19
Date

Page 1 of 1
October 10, 2019

## Appendix H

Appendix H is RBA 2019-11- , which documents the approval of VRS funding policy amendments related to alternative funding requirements, reducing amortization periods to accelerate payback of unfunded liabilities, and clarifying funding parameters for political subdivision plans entering VRS or enhancing benefits for members.

# Amend VRS Funding Policy Statement to Allow for Resetting of Total Unfunded Accrued Liability as of June 30, 2023, Over 20 Years; Establish Employer Funded Status When Modifying the HIC Program, and Confirm that Stress Testing Report is to be issued Regularly Instead of Annually.

## Requested Action

The Board approves the changes to the VRS Funding Policy Statement to allow for resetting of the total unfunded accrued liability as of June 30, 2023, over 20 years and to establish employer funding rules associated with modifications to the health insurance credit program when either enhancing the HIC benefit or adding groups of previously non-covered members to the HIC program, as presented at this meeting and attached to this RBA.

Effective with the June 30, 2023, pension and OPEB valuations - the legacy unfunded liability, which was originally amortized over a 30-year period in 2013, and all subsequent amortization bases established between 2014 and 2023, which were initially amortized over 20 years, will be amortized over a new 20-year period. New layers will be established in future years according to the parameters of the funding policy. Note that any unfunded liabilities for political subdivisions that were originally amortized over 10 years associated with new coverage or enhancement of coverage will not be reset as part of this change.

The explicit funding requirements associated with modifying the health insurance credit programs will require employers to provide a lump sum payment prior to the enhancement of benefits or coverage based on the funded status of their plan prior to the election.

The Board also confirms that the Sensitivity and Stress Test Analyses required by § 51.1-124.30:1 shall be performed regularly, consistent with the statutory requirement. RBA 2017-06-17 provided that the report be issued annually, but issuing the report less frequently is more consistent with the rate-setting valuation schedule and is compliant with the statutory requirement.

## Description/Background

VRS staff recommends this change to the VRS Funding Policy Statement in order to reset the total unfunded accrued liability to be amortized over 20 years effective June 30, 2023. This change will spread experience since June 30, 2013, which has been mostly gains, out over a longer period of time. The legacy unfunded liability was already scheduled to be amortized over 20 years as of June 30, 2023. This change will slightly increase contribution requirements, get money into the plan quicker, level out the amortization payments in later years, and is expected to provide a savings in contributions over the 20-year period.

The additional change to the funded requirement for employers electing to either enhance HIC benefits or expand coverage will ensure that the funded status of the HIC plans for such employers does not fall below certain thresholds. This expands the current funded status requirement for employers making the initial election to offer the HIC benefit. The Funding Policy Statement will now require employers wishing to enhance the HIC benefit or expand coverage to non-covered members to potentially pay an initial contribution in order to elect the new coverage. The rules related to the new requirements are as follows:

Any employer (new and existing employers) that wishes to enhance the health insurance credit by electing the extra $1.00 of coverage per year of creditable service or expand coverage to additional non-covered members is required to meet the following requirements:

- If the funded status of the plan is below 50% prior to the change, the employer must make an initial contribution equal to the full increase in the plan's liability associated with enhancing the HIC benefit.
- If the funded status of the plan is greater than 50% but below 75% prior to the change, the employer must make an initial contribution equal to 50% of the increase in the plan's liability associated with enhancing the HIC benefit, with the remaining additional liability to be amortized over 10 years.
- If the funded status of the plan is greater than 75% prior to the change, the employer must make an initial contribution in the amount necessary to keep the funded status at the 75% threshold after the change, with any remaining additional liability to be amortized over 10 years.

Lastly, the Board confirms that the Sensitivity and Stress Test Analyses required by § 51.1-124.30:1 shall be performed regularly, as opposed to annually, consistent with the statutory requirement. This RBA updates the timing for the Sensitivity and Stress Test Analyses previously set out in RBA 2017-06-17.

### Rationale for Requested Action

The VRS Funding Policy Statement memorializes the methods by which the Board has elected to fund each plan, and the proposed amendments to the policy statement allow for the change to the HIC and plan amendment election requirements. The Sensitivity and Stress Test Analyses will be issued regularly, as opposed to annually, to mirror the statutory requirement.

### Authority for Requested Action

Article X, § 11 of the *Constitution of Virginia* requires that VRS benefits be funded using methods that are consistent with generally accepted actuarial principles, and *Code of Virginia* § 51.1-124.22(A)(8) authorizes the Board to promulgate regulations and procedures and make determinations necessary to carry out the provisions of Title 51.1. Section 51.1-124.30:1 requires that Sensitivity and Stress Test Analyses be performed regularly.

The above action is approved.

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A. Scott Andrews, Chair — Date
VRS Board of Trustees

Virginia Retirement System

# Certify the contribution rates for the Five Statewide Retirement Plans and associated OPEBs effective for FY 2025 and FY 2026.

## Requested Action

After considering the recommendations of its actuary, the Board certifies the rates as presented for: the five statewide Retirement Plans (State Employees, Teachers, JRS, SPORS, and VaLORS) and the associated OPEBs; Group Life Insurance (GLI); Health Insurance Credit (HIC); and the Virginia Sickness and Disability Program (VSDP), including self-funded Long-Term Care, all effective July 1, 2024.

## Rationale for Requested Action

In accordance with *Code of Virginia* § 51.1-145, the VRS Board of Trustees determines the required contribution rate for the various employer groups in the Retirement Program. Based on the June 30, 2023, actuarial valuations conducted by the VRS plan actuary, Gabriel, Roeder, Smith & Company, the Board certifies the full employer contribution rates as follows:

### Retirement Systems

**Fiscal Year 2025/2026**

| Plan | Board Certified Employer Defined Benefit Contribution Rate |
|---|---|
| **State** | 12.52% |
| **Teachers** | 14.21% |
| **SPORS** | 31.32% |
| **VaLORS** | 22.81% |
| **JRS** | 30.66% |

Contribution rates for retirement systems are net of member contributions and defined contribution hybrid matching contributions.

### Other Post Employment Benefit Plans (OPEBs)

**Fiscal Year 2025/2026**

| Plan | Board Certified Employer Contribution Rate |
|---|---|
| Group Life | 1.18% |
| HIC State | 0.90% |
| HIC Teachers | 1.03% |
| VSDP | 0.50% |

The certified employer contribution rates for the retirement systems and OPEBs listed above reflect the assumptions and provisions in effect as of June 30, 2023, including: 1) the assumption and method changes from the most recent experience study for the period from July 1, 2016 to June 30, 2020 and 2) the funding principles approved by the Board effective on or after June 30, 2013, as amended, which includes a reset of the unfunded liability as of June 30, 2023, over a closed 20-year period decreasing by one each year until reaching 0 years, and future annual increases or decreases in unfunded liability to be funded over closed 20-year periods beginning on each valuation date.

The certified employer contribution rates for the retirement plans and associated OPEBs will go into effect on July 1, 2024.

## Authority for Requested Action

*Code of Virginia* § 51.1-145 authorizes the Board to determine the required contribution rate for the various employer groups in the Retirement Program.

The above action is approved.

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A. Scott Andrews , Chair Date
VRS Board of Trustees