Response to Questions on the FY 2018 Budget

Request By: Supervisor McKay

Question: The School Board has had considerable discussion on making changes to the Educational Employees' Supplementary Retirement System of Fairfax County (ERFC) over the last months, including review of several options before reaching consensus on including the ERFC Board action item at its meeting on February 9, 2017. Please provide responses on the following questions:

1) What is the chronology of School Board discussion about the changes to ERFC that are currently being considered?
2) In the context of the decision by the School Board to defer action on changes to ERFC until additional questions can be answered, why was the transfer request increased on February 9, 2017?
3) In addition to the changes currently being considered, what is the history of changes to ERFC?

Response: The following response was provided by Fairfax County Public Schools (FCPS):

1) In FY 2016, FCPS hired a consultant, AON Hewitt, to complete an unbiased study on FCPS' retirement benefit levels from the VRS and ERFC programs as compared to the surrounding school divisions, Fairfax County, and the federal government. The following chart details the chronology of School Board discussions regarding the study and proposed changes to the ERFC retirement plan.

May 12, 2016 Work Session	The results of the study mentioned above were presented to the School Board. The presentation included the comparison to the surrounding jurisdictions, Fairfax County and the federal government along with a comprehensive analysis of income replacement at retirement provided by the retirement programs that FCPS offers. A history of FCPS retirement programs was also included in the presentation. Options for future consideration were presented: • Continue to support the benefit level provided by the current ERFC plan • Modify ERFC to establish a minimum retirement age of 55 years for new hires • Lower the interest crediting rate on ERFC member accounts from 5.0% to 4.0% • Increase the ERFC averaging period for the final average salary from 3-years to 5-years for new hires • Change the Cost-of-living-adjustment for new hires to equal the annual change in the CPI-U index, with a maximum increase of 4.0% • Eliminate ERFC plan for new hires and replace with an employer match on a Defined Contribution plan, material savings to FCPS will not occur in the immediate future • Eliminate ERFC plan for new hires; material savings to FCPS will not occur in the immediate future The Board requested additional information on the benefit and cost impact of the proposed options for new hires.

July 21, 2016 Work Session	The Board discussed the benefit impact on new hires and the employer cost savings associated with the ERFC options, identified by Aon Hewitt, as initially presented at the work session on May 12, 2016.

September 19, 2016
Work Session
	The Board continued the discussion of the employer cost savings associated with the proposed options for new hires. The Board requested information on the short-term and long-term cost implications of:
	• Eliminating ERFC for new hires
	• Savings for both new hires and non-vested employees and vested but not yet eligible for full service retirement, including deferred vested members for the proposed modifications from the May 12, 2016 work session and the below additional modifications:
	  ◦ Lower interest crediting rate on member accounts to 3.0%, 3.5%
	  ◦ Increasing minimum retirement age to 60, 62, maybe higher or lower
	  ◦ Using same COLA as VRS

November 7, 2016 Work Session	The employer cost savings associated with expanding the modifications proposed on May 12, 2016, to include new hires and non-vested employees was presented. In addition, the Board discussed the cost implications of closing ERFC to new hires. Other data requested at the September 19, 2016, work session was shared: • Savings impact of various interest crediting rates • Information update on Fairfax County retirement system review • Comparative data on teacher retirement programs nationally
December 5, 2016 Work Session	The employer cost savings associated with expanding the November 7, 2016, options to include all (new hires, non-vested and vested) members was presented. Current retirees were excluded from all of the analysis. The Board discussion focused on expanding these options to include all members except those currently eligible for full service retirement. Board discussion included consensus on modifications to the ERFC plan provisions including employee groups impacted. The Board requested disaggregated data regarding increasing the retirement age to 60 years for new hires and non-vested employees.
January 19, 2017 Work Session	The employer cost savings associated with the December 5, 2016, options and increasing the minimum retirement age from age 55 to age 60 for new hires and non-vested employees was discussed.
February 9, 2017 Regular Meeting	The School Board considered the main motion to direct the ERFC Board of Trustees to initiate the process to implement the following ERFC Plan modifications, effective July 1, 2017: All ERFC members: 1) Lowering the interest crediting rate on ERFC member accounts from 5.0 percent to 4.0 percent ERFC 2001 members hired on or after July 1, 2017, and non-vested members as of June 30, 2017: 2) Instituting a minimum retirement age of 55 3) Increasing the period for calculating the final average salary from 3 years to 5 years 4) Changing the cost-of-living adjustment to equal 100 percent of the Consumer Price Index (CPI-U) with a cap of 4.0 percent; and present the ERFC 2001 amended plan documents to the School Board for approval, by June 2017.

	The School Board voted to postpone the motion until the April 27 regular meeting. The School Board directed the ERFC Board of Trustees to provide an analysis of fund management alternatives (e.g. the mix of passive and active management) that may produce savings for the fund without harm to the interests of employees and retirees and to bring that analysis to the School Board on or before March 31, 2017. The FCPS School Board directed the ERFC Board of Trustees to bring to the School Board: (a) analysis and justification for investment choices; (b) report results net of fees; (c) compare any active management selections against the related index used for comparison; and (d) include no less than "Year to Date," "Trailing 12 Months," "Previous 3 Year," "Previous 5 Year," and "Previous 10 Year" periods. The report on potential future reporting is expected no later than March 31, 2017.

2) The FY 2018 Proposed Budget was developed using a 6.40 percent employer contribution rate for ERFC as recommended by the ERFC Board of Trustees. This rate is an increase from the FY 2017 employer contribution rate of 5.60 percent and resulted in additional expenditure requirements of $11.4 million. In December 2016, the School Board provided guidance to staff to include savings of $4.7 million in the Superintendent's Proposed Budget for the modifications to the ERFC Retirement Plan which would impact new hires and non-vested employees and included increasing the averaging period for the final average salary from three years to five years, changing the cost-of-living adjustment (COLA) to equal 100 percent of CPI, but not more than 4.0 percent and instituting a minimum retirement age of 55. In addition, the modifications included reduction of the interest crediting rate from 5.0 percent to 4.0 percent for all members. The School Board was to vote on the motion to implement these changes on February 9, 2017. When the School Board deferred action on the benefit modifications until April 27, 2017, the savings were removed from FY 2018 Advertised Budget and the School Board voted to increase the County transfer request to balance the advertised budget.

3) ERFC was created in 1973 as a supplement to the primary teacher retirement plan, the Virginia Retirement System (VRS). The combination of VRS and ERFC was implemented to be comparable to the Fairfax County Employees' Retirement System (FCERS). At that time, teachers could not retire from VRS until age 60 with 30 years of service. Collective bargaining was present in Fairfax County and teachers made wage concessions to fund ERFC in order to be able to retire at age 55 with 25 years of service, and afford to continue living in Fairfax County.

   By 2001, the average retirement age in FCPS had increased beyond age 55; a retirement system designed to facilitate early retirement no longer served the teachers as well. Therefore, the legacy ERFC plan was closed and replaced by ERFC 2001, which applies to all full-time educational and administrative personnel hired on or after July 1, 2001. The following link has a comparison of the FCPS Retirement Plans eligibility and provisions on pages 6-7:

http://www.boarddocs.com/vsba/fairfax/Board.nsf/files/A9PU94686FD8/$file/Retirement%20Security%20Presentation.pdf

In addition to the eligibility and provision changes effective July 1, 2001, the ERFC employer and employee contribution rates have changed through the years. In FY 2004, there was a 2.0 percent shift from FCPS to the employee which was offset by a 2.0 percent decrease in the employee VRS contribution rate. In FY 2013, there was a 1.0 percent shift from the employee to FCPS to mitigate the impact of the 2.0 percent VRS shift back to the employee. The following chart shows the employee contribution rates from FY 2000 to FY 2018.

Employee Contribution Rates			
Year	**ERFC**	**VRS**	**Total**
FY 2018 Advertised	3.00%	5.00%	8.00%
FY 2017	3.00%	5.00%	8.00%
FY 2016	3.00%	5.00%	8.00%
FY 2015	3.00%	5.00%	8.00%
FY 2014	3.00%	5.00%	8.00%
FY 2013	3.00%	2.00%	5.00%
FY 2012	4.00%	0.00%	4.00%
FY 2011	4.00%	0.00%	4.00%
FY 2010	4.00%	0.00%	4.00%
FY 2009	4.00%	0.00%	4.00%
FY 2008	4.00%	0.50%	4.50%
FY 2007	4.00%	1.00%	5.00%
FY 2006	4.00%	1.50%	5.50%
FY 2005	4.00%	2.00%	6.00%
FY 2004 (June)	4.00%	2.50%	6.50%
FY 2004 (July-May)	2.00%	4.50%	6.50%
FY 2003	2.00%	5.00%	7.00%
FY 2002	2.00%	5.00%	7.00%
FY 2001	2.00%	5.00%	7.00%
FY 2000	2.00%	5.00%	7.00%

AON Hewitt found that the FCPS 8.0 percent employee contribution rate was higher than the surrounding school divisions, Fairfax County, and the federal government with the exception of the District of Columbia Public Schools which also has an 8.0 percent employee contribution rate. FCPS employees can choose to take full advantage of the VRS defined contribution plan by contributing an additional 4.0 percent of pay. Combine this 4.0 percent of voluntary contributions with 8 percent of mandatory contributions and FCPS has the highest total contributions of all surrounding comparators. The total required contribution of 12.0 percent required for FCPS participants to take full advantage of the retirement savings opportunity available to them under the plans, including maximizing the matching contribution under the defined contribution feature of the VRS Hybrid Plan, exceeds the comparable contribution requirements under any of the peer group employers' plans.

Due to a significant change in the Virginia Retirement System which moved from a defined benefit plan to a hybrid plan, the benefit level of VRS combined with ERFC is no longer comparable to the County's FCERS plan. AON Hewitt found that at all age and service combinations examined, the County's Plan C defined benefit plan provides greater income and lower participant contribution levels than required under the ERFC 2001 / VRS Hybrid defined benefit plans.