



Response to Questions on the FY 2010 Advertised Budget Plan

Request By: Supervisor Hudgins

Question: Please analyze the option of buying years of service towards retirement. (FCPS allows its employees to buy up to four years). What would be the potential costs to the County as well as any projected cost savings were this implemented.

Response: Before responding, it may be useful to note that all three of Fairfax County's retirement systems (Employees', Police Officers and Uniformed) permit members to purchase service credit, although they are limited to purchases of prior service within the same system and/or military service.

Many employees of Fairfax County Public Schools (FCPS) participate in the Virginia Retirement System (VRS) as well as FCPS's supplemental plan, the Educational Employees' Supplemental Retirement System of Fairfax County (ERFC). The purchase of service credit provisions for those ERFC members who were employed prior to July 1, 2001 are extensive; however, new FCPS employees and those employed on or since July 1, 2001 are limited to only the purchase of service provisions within VRS. Therefore, the following description addresses only the VRS provisions.

Under circumstances specified by the Code of Virginia, VRS permits members to purchase service credit for a variety of reasons, including periods of educational leave; public service with another state, political subdivision or public school system; federal civilian service; military service; birth/adoption leave of absence; and VRS refunded service. By purchasing such service, members can achieve vesting, increase their monthly retirement benefits, increase their health insurance credit and retire at an earlier age. Purchases are limited to four years, or fewer, of each type of service. However, it is possible to purchase more than four years in total (e.g. four years of military service plus four years of federal civilian service plus four years of other public service). While specifics can vary, in general, members who purchase service credit within the first three years of employment pay 5 percent of current salary for each year of purchased service. Members may continue to purchase at 5 percent beyond the three-year time limit if they have entered into a payroll deduction contract. After three years, with the exception of VRS refunded service, purchases are at "actuarial cost." The actuarial cost consists of the amount required, in current dollars, to fund the expected value of the increased future benefits, given the member's age, life expectancy, projected retirement date, investment earnings, inflation, etc. The VRS Handbook provides an example of a member who is 44 years old earning a salary of \$42,000 per year. Within the first three years, at 5 percent, the cost per month of service credit is \$175.00; after three years, the actuarial cost per month of service credit is \$1,027.41.

Many jurisdictions allow for the purchase of service outside of that worked under the pension plan. In some cases, this service is restricted to service worked for other public sector jurisdictions and in other cases the service doesn't even have to exist. Such "air time" purchases are rare and tend to exist in plans that are in financial difficulty due to these and other practices. The cost impact of allowing service purchases is directly

related to the amount the employee is charged. If employees are charged the full actuarial cost of their time it is less likely that they will exercise the purchase option. If they do, it does not result in an increase to the plan sponsor since the entire impact of the additional service is prepaid by the employee. Plans that require full actuarial cost purchases generally wait until the member is retirement eligible before accepting the purchase. This is because one cannot know the full actuarial cost until retirement actually occurs. Payment earlier than that would require some assumptions about retirement date and pay increases in the interim.

At the other end of the spectrum are plans that grant service with little or no cost to the employee. In these plans there is a large utilization of the service purchase option and a large increase in the liability to the plan sponsor. This is especially true in plans that allow for service purchase late in an employee's career. These purchases will have a large impact on liability because there is more certainty that the employee will remain until retirement and get the benefit of the extra service. This is why many plans that allow for service purchase require employees to make the purchase when they are first hired.

A well designed service purchase program would specify exactly what type of service is available for purchase, would assign a realistic purchase price to be borne by the employee and would require that the service purchase occur when members are first hired. The definition of a "realistic" purchase price depends on how the plan sponsor feels about sharing the cost of that prior service. In some plans the cost varies by the type of service being purchased, e.g. there may be one price for service worked in the same capacity at a neighboring jurisdiction and another price if the service is worked out-of-state. The cost structure depends on the plan sponsor's desire to encourage such purchases and to share in their cost.

If it would be helpful, specific proposals could be developed to expand purchase of service opportunities within the three County retirement systems. Obviously, such proposals would need to consider why the service purchase options are being offered and how much the County (employer) wants to share in the cost. The Systems' actuary could then be paid to develop estimates of the cost to the County for each proposal.