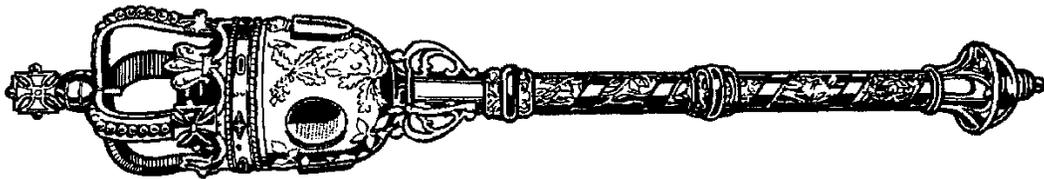


*Report of the
House Appropriations
Subcommittee*

on

Compensation & Retirement



House Bill 1600

February 4, 2001

**Respectfully Submitted by the House Appropriations Subcommittee
on Compensation & Retirement:**

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REPORT OF THE SUBCOMMITTEE

on

COMPENSATION & RETIREMENT

Mr. Chairmen and Members of the Committee:

As with all of the Subcommittees, the work of the Compensation & Retirement was retrospective and deliberative. The primary goal of this Subcommittee was to address salary increases for our teachers and the local employees in our constitutional offices and other state-supported local programs.

As you well know, state employees will receive an average salary increase of 3.5 percent next December under the Governor's proposed budget. The Compensation Subcommittee does not believe that we can do any less for our school teachers and state-supported local employees. This concept has consistently been supported by this Committee and the General Assembly.

Mr. Chairman, the introduced budget includes local savings obtained through lower teacher contribution rates in the second year. These savings have been offered as a source for localities to use to provide salary increases for teachers. However, the savings available to each locality can vary substantially and, as a result, may not be sufficient to enable all localities to provide an appropriate salary increase.

While the ultimate decision on teacher pay raises rests with the local school board, the state must be willing to offer financial incentives to encourage the desired action and ensure a minimum increase is provided statewide. There is no job more challenging than educating our children. Thus, we must continue to assess teacher salaries and provide assistance for salary increases if we want to hire and retain the best teachers.

Therefore, we recommend that the state provide its share of a 3.5 percent salary increase for teachers, effective December 1, 2001, at a cost of \$48 million.

Mr. Chairman, a salary increase for state-supported local employees in constitutional offices and in other programs was the

next issue this Subcommittee spent hours discussing. However, given the important functions these individuals provide in our localities -- law enforcement, jail security, and local mental health services among others -- providing a salary increase is paramount. As a result, we recommend a 3.5 percent salary increase, at a cost of \$13.7 million, for these employees, effective December 1, 2001.

Clearly, Mr. Chairman, with the fiscal constraints facing this body, providing the revenue to finance these two big objectives was critical. From the first day of the Session, we knew that finding additional revenue would be a substantial challenge.

But I'm happy to say that we have found a solution that makes good, sound financial sense, and it is one that helps our localities in more ways than one.

We began our budget review by examining all of the compensation adjustments contained in the budget, including the contribution rates adopted by the Virginia Retirement System. In November 2000.

As you may know, the VRS adopted rates last November for the second year of the 2000-2002 biennium based on a June 2000 actuarial valuation. The state employee and teacher rates, which were lower than the rates calculated as of the 1999 actuarial valuation, resulted in substantial savings for both the state and local governments. For example, localities saved more than \$94 million through the reduction in teacher rates.

The rate reductions recently experienced by the state and local governments reflect the exceptional investment performance of the retirement system's investment assets. This investment performance has also positively impacted other indicators that reflect the exceptional financial position of the investment fund.

For example, Mr. Chairman, the state employee fund on an actuarial basis is funded at 105 percent and almost 120 percent on a market basis. The teacher fund is funded at 103 percent on an actuarial basis and 116 percent on a market basis. More impressive is the fact that there are slightly more than \$3 billion of investment gains that have not been accounted for by the VRS actuary in developing rates. These gains provide an important cushion to the

stability of future contribution rates should actuarial experience not meet expectations.

These statistics are even more impressive when you consider that this reflects full prefunding of the cost of living allowance which was achieved in 2000. The financial commitment by this Committee and the General Assembly helped make this possible.

Mr. Chairman, when reviewing VRS' June 2000 actuarial valuation, questions were raised as to why the new rates were applied effective July 1, 2001, and not July 1, 2000? This seemed to make sense as the biennial budget takes effect on July 1, 2000. To determine if this was appropriate, we asked the JLARC actuary, the William M. Mercer Company, to evaluate whether this was actuarially sound and, if so, could this action cause rates to rise in the second year of the 2000-2002 biennium.

JLARC's actuary determined that the methodology used by the VRS assumes that the rates developed apply from that date forward. In other words, the rates were intended to be effective as of July 2000 and not July 2001.

Applying the second year's rates in the first year results in savings exceeding \$70 million for the state and localities. These savings are sufficient to fund the December 1, 2001, teacher and state-supported local employees' salary increases, accomplishing the major goal of this subcommittee.

Other Compensation Actions

In addition to our salary package, the Subcommittee would like to note one other action that bears mention. Included in the Subcommittee's proposal is a request for the VRS to conduct a study of the feasibility of combining the health insurance credit fund with the VRS retirement fund. As you know, the relatively modest size of the retiree health insurance credit fund has made providing even minor benefit enhancements prohibitively costly.

Mr. Chairman, over the course of the next year, VRS will determine whether combining these funds will enable the cost of the retiree health credit to be included in the VRS rates, enabling benefit increases to be more cost-effectively considered. If this is feasible, it

may provide a mechanism for this Committee to properly address the increasing cost of health insurance for our state and teacher retirees.

Mr. Chairmen, that covers the major recommendations of our Subcommittee.

In closing, I would like to thank the two of you, along with the members of the Subcommittee, for their hard work and the long hours spent reviewing legislation and developing a compensation package for our employees.

I now ask for the Committee's adoption of the Subcommittee report.

Budget Amendment Recommendations Compensation and Retirement Subcommittee

| <u>Amendment</u> | 2000 - 2002 BIENNIAL TOTAL | |
|------------------|----------------------------|-------------|
| | General | Non-General |
| | <u>Fund</u> | <u>Fund</u> |

Compensation Supplements

| | | |
|--|---------------------|----------------|
| Teacher Pay Raise - 3.5% on December 1, 2001 | 48,466,836 | |
| State Supported Local Employees Pay Raise -- 3.5% on December 1, | 13,700,000 | |
| VRS Rate Reduction for Teachers (includes health care credit rate de | (68,510,377) | |
| VRS Rate Reduction for State Employees | (15,023,743) | |
| Apply New VRS Group Life Rates -- First and Second Years | (6,778,246) | |
| Apply VRS Actuary's Recommended Rates to JRS/SPORS | (20,757,280) | |
| Apply VRS Actuary's Recommended Rate to VaLORS | (5,189,088) | |
| Eliminate Phase-In of State Health Credit Rate -- Second Year | (1,658,508) | |
| VRS -- Implementation of Benefit Restoration Plan | | 50,000 |
| VRS -- Partial Lump Sum Benefit Options (HB 2629) | | 250,000 |
| VaLORS -- JLARC Study of Employee Groups Eligibility | Language | |
| VRS--Remove Special Benefit Provisions | Language | |
| VRS-- Authority to Collect Premiums | Language | |
| VRS--Study of Health Insurance Credit | Language | |
| VRS--Modification of Benefit Language | Language | |
| VRS--Modification of Benefit Language | Language | |
| VRS-- Employee Benefit Provision | Language | |
| VRS--Deletes Obsolete Language | Language | |
| Career Development Program for Deputy Treasurers | Language | |
| Career Development Program for Commissioners of the Revenue | Language | |
| Study -- Cost of Employee Health and Prescription Drug Benefits | Language | |
| Remove Defined Contribution Plan Study | Language | |
| Total Cost of Compensation Package | (55,750,406) | 300,000 |