

Virginia Retirement System 2014 Fiscal Impact Statement

1. Bill Number: HB 1105

House of Origin Introduced Substitute Engrossed
Second House In Committee Substitute Enrolled

2. Patron: Ingram

3. Committee: Appropriations

4. Title: Life insurance for retired state and local employees.

5. Summary: Provides (i) that the basic life insurance coverage for retired state employees with 15 or more years of creditable service shall not be reduced to less than \$8,000, indexed to the amount of any general salary increases for state employees, and (ii) that retired state employees be offered optional group life insurance coverage with premiums to be paid by the retirees.

6. Budget Amendment Necessary: No.

7. Fiscal Impact Estimates: This legislation provides for two changes to the life insurance program. One affects the Group Life Insurance Program and one affects the Optional Life Insurance Program.

Group Life Insurance

HB 1105 would provide a minimum group life insurance death benefit of \$8,000 for all retirees eligible for VRS Group Life Insurance who retire with at least 15 years of creditable service. Additionally, the \$8,000 minimum benefit is to be increased annually by the same percentage or amount of any general salary increases for state employees on the date such salary increases apply. Approximately 4,400 current retirees would have their group life insurance benefit increased as a result of this bill.

In determining the cost impact of the legislation, the proposed benefit changes were assumed to apply to the eligible active, retired, and disabled members of the State, Teachers, Political Subdivisions, State Police (SPORS), Judicial Employees (JRS), Virginia Law Officers (VaLORS), and Optional Retirement Plan (ORP) employer groups. For estimation purposes, the following assumptions were made:

- To be consistent with the retiree life insurance benefit's eligibility requirements, disabled retirees and members on long-term disability were assumed to be eligible for the minimum death benefit regardless of their amount of creditable service.

- The \$8,000 minimum benefit was indexed at an annual rate of 3.00%, which is the annual payroll growth assumption used in the valuation of the group life plan.
- For service retirees, eligibility for the minimum benefit was based upon 15 years of estimated creditable service.
- The indexing of the minimum benefit was assumed to apply to a member’s benefit annually. As such, a member with an \$8,000 minimum benefit in fiscal year 2014 is assumed to have an \$8,240 minimum benefit in fiscal year 2015, an \$8,487 minimum benefit in fiscal year 2016 and so on. Similarly, a member not immediately eligible for the minimum benefit may become eligible at a future point in time.

As of June 30, 2013, the Group Life Insurance Program had an unfunded liability of \$1.735 billion. The proposed changes in HB1105 would increase the unfunded liability for the Group Life Program by \$22.1 million. The increase in annual cost is expected to be approximately 0.01% of covered payroll. Exhibit 1 below provides estimated cost impacts.

Group Life Insurance Exhibit 1

	<u>FY15 Cost</u>	<u>FY16 Cost</u>	<u>FY17 Cost</u>	<u>FY18 Cost</u>	<u>FY19 Cost</u>	<u>FY20 Cost</u>
State - General Fund	\$ 152,000	\$ 152,000	\$ 152,000	\$ 152,000	\$ 152,000	\$ 152,000
SPORS - General Fund	9,000	9,000	9,000	9,000	9,000	9,000
VaLORS - General Fund	29,000	29,000	29,000	29,000	29,000	29,000
JRS - General Fund	6,000	6,000	6,000	6,000	6,000	6,000
Teacher - General Fund	272,000	274,000	274,000	274,000	274,000	274,000
TOTAL General Fund	\$ 468,000	\$ 470,000				
State - Non-General Funds	\$ 198,000	\$ 198,000	\$ 198,000	\$ 198,000	\$ 198,000	\$ 198,000
SPORS - Non-General Funds	2,000	2,000	2,000	2,000	2,000	2,000
VaLORS - Non-General Funds	3,000	3,000	3,000	3,000	3,000	3,000
TOTAL - Non-General Funds	\$ 203,000					
Teacher - Local Funds	\$ 414,000	\$ 416,000	\$ 416,000	\$ 416,000	\$ 416,000	\$ 416,000
Political Subdivisions - Local Funds	\$ 409,000	\$ 415,000	\$ 418,000	\$ 418,000	\$ 418,000	\$ 418,000
TOTAL Local Funds	\$ 823,000	\$ 831,000	\$ 834,000	\$ 834,000	\$ 834,000	\$ 834,000
Grand Totals	\$ 1,494,000	\$ 1,504,000	\$ 1,507,000	\$ 1,507,000	\$ 1,507,000	\$ 1,507,000

Estimated projections based on employee data and valuations results as of June 30, 2013 and assume a level population throughout projection period.

Payroll projections include only known payroll increases; including FY 2014 across the board merit increase and increases for compression for State employees and payroll increases for Teachers & Locals employees transitioning member contribution requirements effective July 1, 2012.

Optional Group Life Insurance

Optional Group Life insurance is a participant funded benefit. Therefore, the cost is to be borne by members who elect to participate. See “Other Comments” for additional information.

8. Fiscal Implications:

Group Life Insurance

See Fiscal Impact Estimate above.

Optional Life Insurance

See Fiscal Impact Estimate above.

9. Specific Agency or Political Subdivisions Affected:

Group Life Insurance

VRS, all participating employers, all active members and retirees.

Optional Life Insurance

VRS and all eligible state retirees.

10. Technical Amendment Necessary:

Group Life Insurance

No technical amendment is necessary for the Group Life Insurance portion of this legislation.

Optional Life Insurance

The Optional Life Insurance portion of this legislation does require technical amendments.

Section 51.1-512(E) currently provides that “[a]ll accidental death and dismemberment insurance shall cease at retirement.” If state retirees are to be allowed to purchase accidental death and dismemberment insurance, this language should be struck. Section 51.1-512(F) provides that the Board may discontinue the optional insurance plan at any time upon determination that employee participation is not sufficient to continue the plan on a sound actuarial basis. If this legislation passes, a reference to state retirees should be added to this provision.

Lines 150 and 151 Strike All accidental death and dismemberment insurance shall cease at retirement.

Line 154 insert *or state retiree* after employee

11. Other Comments: This legislation provides for two adjustments to the life insurance benefits provided under Title 51.1.

Group Life Insurance

In general, § 51.1-505 provides that the current amount of group life insurance for each covered employee is twice the employee's annual salary, rounded up to the next higher \$1,000. This amount begins to be reduced by 25% per year on January 1 following the first full year from the date the employee is separated from service and each January 1 thereafter. The reduction is not to decrease the amount of life insurance to less than 25% of the amount of life insurance to which the initial reduction is applied. So for example, in order to benefit from the initial \$8,000 floor provided in HB1105, an employee would need to have an annual salary of less than \$16,000 ($\$16,000 \times 2 =$ group life benefit of \$32,000). Final reduction of this retiree's group life benefit under current law would be \$8,000.

This bill does not affect the group accidental death and dismemberment insurance, which terminates upon retirement.

This legislation provides for an indexed minimum life insurance benefit for all eligible members of the Group Life Insurance Program.

Under the proposed legislation, eligible employees with at least 15 years of service will have a retirement life insurance minimum of the greater of \$8,000 or 25% of the amount of the group life insurance amount available prior to retirement.

The \$8,000 minimum will be increased by the same percentage or amount as any across the board salary increases provided for active employees. For example, if all active employees get a 2% increase, the minimum for retirees (current and future) would go up to \$8,160. The legislation states that the benefit would increase by "percentage or amount," so if everyone got a \$500 increase, the retiree minimum would go up by that amount as well.

From a cost perspective, HB1105 has the potential for increasing claim cost by approximately \$1.6 million annually, based on a minimum insurance amount of \$8,000. This is based on the last two years of actual claims experience and assumes the minimum death benefit is increased on both current and future retirees.

Depending on the rate and amount of increase in the minimum benefit, the maximum premium rate may need to be increased.

The original summary indicated that this bill is applicable only to retired state employees. The bill as currently drafted, however, applies to all VRS retirees eligible for Group Life Insurance coverage pursuant to Chapter 5 of Title 51.1.

The Group Life Insurance portion of HB1105 is identical to SB 102.

Optional Life Insurance

This legislation proposes to allow state retirees to enroll in the Optional Life Insurance plan, without requiring that the employee had to have participated in the plan prior to retirement.

Generally, the focus of employer provided group life insurance plans, such as the VRS Group Insurance Program set out in Chapter 5 of Title 51.1, is on active employees. Available benefits upon retirement are based on benefits established while a member was actively employed in a VRS covered position. Currently, active members who have Optional Life insurance have two options to continue Optional Life Insurance when they retire.

Conversion

Within 30 days of terminating service a member has the opportunity to convert existing Optional Life insurance to an individual whole life insurance policy, with guaranteed coverage (no medical underwriting). The cost of the converted coverage is at non-group rates through Minnesota Life, VRS' third-party administrator for life insurance and accidental death and dismemberment coverage. The benefit is payable upon death as long as the premiums are paid by the member. After the 30-day window, a member who has terminated service no longer has the opportunity to convert optional life insurance to an individual policy.

Continuation

If a member had Optional Life coverage for at least 60 continuous months prior to retirement or before leaving service, the member may elect to continue Optional Life coverage and pay the same group rates as the active member group. However, this continued coverage only lasts until age 80. The coverage is subject to 25% reductions at age 65, 70, 75, and by age 80 Optional Life coverage ceases.

Exhibit 1 below details the current optional life membership:

Optional Life Insurance Exhibit 1

Optional Life Insurance			
Employer	Active Members	Retired Members	Total Members
Judges	124	10	134
State Police	887	33	920
State	21,559	827	22,386
Teachers	17,935	724	18,659
Political Subdivisions	24,220	821	25,041
VaLORS	3,093	133	3,226
Total	67,818	2,548	70,366

In addition to the 2,548 members who have chosen to continue optional life coverage into retirement, each year another 15-20 members convert their optional coverage within 30 days of retiring. In total, less than 4% of active members with optional life coverage choose to continue coverage into retirement.

Allowing state retirees to enroll in a post-retirement benefit, which they did not elect while actively working, creates anti-selection against the current plan format by providing an opportunity for those with higher risk to enroll. As a whole, retirees are a higher risk group than active employees. For example, as indicated by Minnesota Life, even retirees currently covered in the Optional Life plan have experience that is five (5) times more negative than the experience of active employees. These two factors, anti-selection and the high risk profile of this population, could negatively impact premiums for this group. § 51.1-512(B) provides in part that “[t]he conditions prescribed by the Board shall provide that offering the optional insurance does not materially increase the rates for any group life insurance policy provided pursuant to § 51.1-505.”

If this legislation were to be enacted, applicants would need to be medically underwritten to protect against anti-selection. Generally speaking, the underwriting decline rate of a group with demographics similar to a retiree group is high. Minnesota Life estimates that close to 80% of applicants could be declined for coverage. (In contrast, only 20% of active members who apply are declined.) From a cost/benefit analysis, the additional resources needed to manage such a high percentage of declined participation may not be worth the benefit, especially where other options are currently available to active members that would allow them to continue Optional Life insurance into retirement. Without this legislation, however, some retirees will not have access to the Optional Group Life insurance program. As a practical matter, though, the cost for this type of retiree coverage might be prohibitive to most members. This coupled with a high decline rate for retirees, could result in a negative perception of the program overall.

The Optional Life Insurance portion of HB1105 is identical to SB 101.

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