CITY OF RICHMOND
CITY AUDITOR

DATE: October 7, 2020

TO: Ms. Lenora Reid
Acting Chief Administrative Officer

FROM: Louis Lassiter LL
City Auditor

SUBJECT: Citywide
Pension & Other Post-Employment Benefits audit

The City Auditor's Office has completed the Citywide Pension & Other Post-Employment Benefits audit and the final report is attached.

We would like to thank the Administration staff for their cooperation and assistance during this audit.

Attachment

cc: The Richmond Audit Committee
The Richmond City Council
Leo Griffin, Executive Director of Richmond Retirement System
Mona Adkins-Easley, Interim Director of Human Resources
John Wack, Director of Finance
Jay Brown, Director of Budget & Strategic Planning

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City of

RICHMOND

Office of the City Auditor

Audit Report# **2021-04**

Pension & Other Post-Employment Benefits

October 7, 2020

Audit Report Staff

Louis Lassiter, City Auditor

Lily Hernandez, Deputy City Auditor

Leigh Ann Castro, Auditor

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October 2020

Highlights

Audit Report to the Audit Committee, City Council, and the Administration

Why We Did This Audit

The Office of the City Auditor conducted this audit as part of the FY2021 audit plan approved by the Audit Committee. The objective for this audit was to evaluate the City's Pension and OPEB funding and plans as compared to other large Non-VRS local governments in Virginia.

What We Recommend:

The Chief Administrative Officer:

- Set aside additional funding for the pension liability in future Budgets presented to City Council.
- Work with Human Resources to determine if an insured approach for disability benefits for Defined Contribution plan participants is a more efficient and cost-effective alternative.
- Create a cross functional team comprised of Human Resources, Finance, Budget, Public Safety and RRS staff to review the Pensions system as it pertains to member contributions, DROP, AFC and other factors, as appropriate to improve comparability in the marketplace with peer localities and improve long term funding of the Defined Benefit Plan. This review could also evaluate using VRS for new hires.
- Fully fund the OPEB Annual Required Contributions in future Budgets presented to City Council and set aside additional funding for the OPEB Trust.
- Create a cross functional team comprised of Human Resources, Finance, Budget and Public Safety staff to reduce the OPEB liability in future years to address OPEB health care benefits for existing personnel and/or for new hires that can be proposed to City Council.

Pension & Other Post-Employment Benefits

Background – The Richmond Retirement System (RRS) was established in 1945 by Richmond City Council and reestablished by the acts of the Virginia General Assembly in 1998, 2005, 2008, and 2010. The RRS is one of the few larger localities in Virginia that maintains its own retirement system outside of the Virginia Retirement System (VRS). The RRS Defined Benefit (DB) and Enhanced Defined Benefit (EDB) Plans cover all full-time permanent sworn public safety employees, general employees hired before July 1, 2006 and a select group of Senior Executives. Both plans are closed to general employees hired on or after July 1, 2006 as those employees are enrolled in a Defined Contribution (DC) 401(a) Plan. Members are vested after five years of service or at their normal retirement age.

Other Post-Employment Benefits (OPEB) are benefits, such as health insurance, that have been promised to employees upon retirement. In years past, the cost of these benefits were primarily funded by local governments on a "pay as you go" basis. However, recent financial reporting standards now require disclosure of not only the OPEB liability but also reporting the liability in the financial statements along with required supplementary information. The City provides medical insurance for some employees that retire from the City. The retiree must have been enrolled in the City health plans for five years immediately prior to retirement and have at least ten years of creditable service prior to retirement. This Plan applies to currently retired members, active members hired prior to 1/1/1997, and Sworn Police & Fire and Sworn VRS, and Executives not in the DC Plan. The City pays a portion of premiums based on the length of active service.

Commendations

Pension Plans Annual Required Contributions – The City has consistently funded the Annual Required Contributions (ARC) over the last 10 years and contributed an additional $2 million over the required contributions in FY2019.

Member of the Virginia Pooled OPEB Trust – In July 2018, the City of Richmond joined the Virginia Pooled OPEB Trust Fund to fund post-employment benefits other than pensions. To date, the City has contributed $750,000 to the Trust.

Needs Improvement

Finding #1 – *Pension Funding* - RRS was the second lowest Pension Plan, funded at 61% when compared to some other localities in Virginia. The City's position has improved somewhat over the last decade but still lags the National Conference of Public Employee Retirement Systems' (NCPERS) 2018 average funded status of 72.6%. Funded status has been impacted by Voluntary Retirement Incentive Plans (VRIP) and also by recent changes in the actuarial assumptions.

Finding #2 – Pension Benefits - The auditors compared pension benefits and provisions to other local retirement systems in Virginia as well as VRS. The City of Richmond's basic DB Plans have the lowest employee contribution rates at 1% and 1.5%. The average final compensation used to calculate benefits is three years, rather than five years as in some localities. The maximum years allowed in the Deferred Retirement Option Plan (DROP) is longer than other localities.

Finding #3 – OPEB Funding - The City has not historically allocated sufficient funding to cover the OPEB liability, which was $84 million as of June 30, 2019.

Finding #4 – OPEB Benefits - The City has not modified OPEB benefits since July 2006. Other localities have controlled the OPEB liability for new hires by eliminating benefits, through access only benefits or fixed subsidies for retiree healthcare. The OPEB liability has grown in recent years and will continue to increase unless adequately funded or benefit changes are implemented.

Management concurred with 5 of 5 recommendations. We appreciate the cooperation received from management and staff while conducting this audit.

BACKGROUND, OBJECTIVES, SCOPE, METHODOLOGY, MANAGEMENT RESPONSIBILITY and INTERNAL CONTROLS

This audit was conducted in accordance with the Generally Accepted Government Auditing Standards promulgated by the Comptroller General of the United States. Those Standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on the audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on the audit objectives.

BACKGROUND

Pension System – Overview

The Richmond Retirement System (RRS) was established in 1945 by Richmond City Council and reestablished by the acts of the Virginia General Assembly in 1998, 2005, 2008, and 2010. RRS administers its Defined Benefit Plans in accordance with provisions outlined in both the Richmond City Charter and Chapter 22 of the Richmond Municipal Code.

The Defined Benefit (DB) and Enhanced Defined Benefit (EDB) Plans cover all full-time permanent sworn public safety employees (unless they select the Defined Contribution Plan), general employees hired prior to July 1, 2006, and a select group of Senior Executives. Both plans are closed to general employees hired on or after July 1, 2006. Members are vested after five years of service or at their normal retirement age (age 65 for general employees and age 60 for public safety employees).

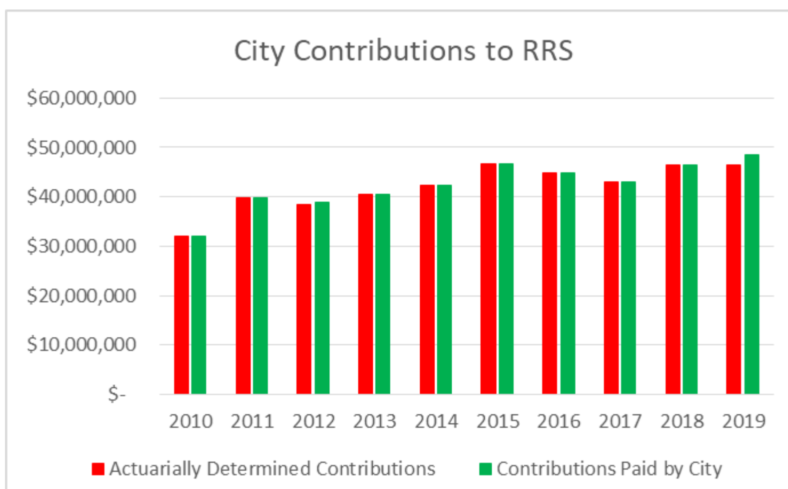
General employees are eligible for regular retirement at age 65 or at any age with 30 years of service. Public safety employees are eligible at age 60 or 25 years of service. Public safety employees participating in the EDB Plan are eligible at 20 years of service. Early retirement is permitted at any time in the 10-year period prior to the normal retirement date, provided the member has completed five or more years of creditable service.

Pension System – Funding

According to the RRS' Comprehensive Annual Financial Report (CAFR), "At June 30, 2019, the Plan Fiduciary Net Position as a percentage of the Total Pension Liability (Funded Status) was 61%, compared to 65.1% at June 30, 2018." In FY2019 the RRS reduced that rate of return from 7.5% to 7% which reduced the funded ratio by approximately 2.75%. It is generally accepted that an 80% funded level is healthy for public pension plans and the National Conference of Public Employee Retirement Systems' (NCPERS) average funded status was 72.6% for 2018. During 2019, the city of Richmond contributed $2 million in addition to fully funding the Actuarially Determined Contribution.

Pension System – Contributions & Funding

Chapter 22 of the City Code requires that City contributions to the RRS consist of a normal contribution (actuarially calculated ratio of the normal cost of all benefits and the gross annual payroll of all active members included in the valuation) plus an accrued liability contribution, which combined, equal the actuarially determined contribution. The accrued liability contribution is the amount necessary to amortize the unfunded actuarial liability and any increase or decrease in the unfunded actuarial liability in future years due to changes in actuarial assumptions, changes in RRS provisions, including the granting of ad hoc Cost of Living Adjustments (COLAs), or actuarial gains or losses amortized over a closed period not exceeding 30 years. Funding for actuarially determined contributions has been met over the last ten years.



Auditor Created Based on Information from Pension System CAFRs

General and public safety employees are required to pay 1% and 1.5% respectively, of their creditable salary in the DB Plan. Employees in the EDB Plan pay 4.57% for general employees and 5.45% for public safety officers.

Government Accounting Standards Board (GASB) Statement Nos. 67 & 68

GASB Statement No. 67, *Financial Reporting for Pension Plans*

According to the GASB 67 Summary, the objective of GASB Statement No. 67 is "to improve financial reporting by state and local governmental pension plans… This Statement replaced the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures,* as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria."

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*

According to the GASB 68 Summary, "The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

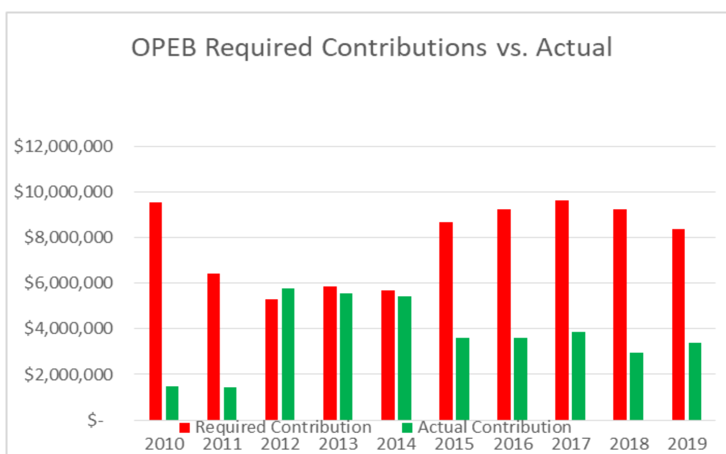
"This Statement replaced the requirements of Statement No. 27, Accounting for Pensions by State and Local Governmental Employers, as well as the requirements of Statement No. 50, Pension Disclosures, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements No. 27 and No. 50 remain applicable for pensions that are not covered by the scope of this Statement."

Other Post-Employment Benefits (OPEB) – Overview

OPEB refers to non-pension benefits that U.S. state and local governments provide to their retired employees. These benefits principally involve health care benefits, but may also include other benefits such as life insurance and disability. The City provides continuous medical insurance for some employees that retire from the City. The retiree must have been enrolled in the City's health plans for five years immediately prior to retirement and have at least ten years of creditable service at the time of retirement. This Plan only applies to currently retired members and active members that were hired prior to January 1, 1997. Additionally, Sworn Police and Fire, Sworn VRS (Richmond Sheriff Employees and constitutional officers in VRS instead of the City Pension Plan), and Executives currently not in the Defined Contribution (DC) group are also able to receive post-retirement medical benefits even if they were hired after January 1, 1997. Once the retiree becomes eligible for Medicare, they are no longer eligible to participate in the City's Plan, with the exception of Line-of-Service retirees.

The City pays a portion of premiums based on length of active service. For those with 10 to 15 years of service, the City contributes 50%; 75% for retirees with 15 to 25 years of service; and 100% of coverage for those retirees with 25+ years of creditable service at the time of retirement. The City also pays full coverage for Line-of-Service retirees for life.

OPEB – Funding



Auditor Created Based on Information from City of Richmond CAFRs

The City currently pays for post-employment benefits on a "pay-as-you-go basis". In July 2018, the City passed Ordinance No. 2018-196 establishing a Trust, through participation in the Virginia Pooled OPEB Trust Fund, to fund post-employment benefits other than pensions. Funding is allocated as available. During FYs 2019 and 2020 a total of $750,000 (3 deposits of $250,000 each) was contributed to the Pooled Trust.

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits other Than Pensions*

According to the GASB 75 Summary, "The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions… It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities.

"This Statement replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, for OPEB. Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, establishes new accounting and financial reporting requirements for OPEB plans.

"The scope of this Statement addresses accounting and financial reporting for OPEB that is provided to the employees of state and local governmental employers. This Statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this Statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed.

"In addition, this Statement details the recognition and disclosure requirements for employers with payables to defined benefit OPEB plans that are administered through trusts that meet the specified criteria and for employers whose employees are provided with defined contribution OPEB. This Statement also addresses certain circumstances in which a non-employer entity provides financial support for OPEB of employees of another entity."

OBJECTIVES

To evaluate the City's Pension and OPEB funding and benefit plans as compared to other large Non-VRS local governments in Virginia.

SCOPE

Pension and OPEB funding as of 6/30/2019 and current Pension and OPEB benefit provisions as of 7/1/2020.

METHODOLOGY

The auditors performed the following procedures to complete this audit:

- Interviewed staff;
- Reviewed and evaluated relevant City of Richmond Code, GASB Statements, and pension benefit and retiree health documentation;
- Analyzed and reviewed Comprehensive Annual Financial Reports (CAFRs) from peer localities and their respective pension plan CAFRs, and the Virginia Retirement System;
- Analyzed and reviewed retiree benefits information from peer localities and VRS Local Plan; and
- Performed other tests, as deemed necessary.

MANAGEMENT RESPONSIBILITY

City of Richmond management and the Richmond Retirement System management are responsible for ensuring resources are managed properly and used in compliance with laws and regulations; programs are achieving their objectives; and services are being provided efficiently, effectively, and economically.

INTERNAL CONTROLS

According to the Government Auditing Standards, internal control, in the broadest sense, encompasses the agency's plan, policies, procedures, methods, and processes adopted by management to meet its mission, goals, and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It also includes systems for measuring, reporting, and monitoring program performance. An effective control structure is one that provides reasonable assurance regarding:

- Efficiency and effectiveness of operations;
- Accurate financial reporting; and
- Compliance with laws and regulations.

Based on the audit test work, the auditors concluded the internal controls over determining the pension liability are good; however, the internal controls over the Pension & OPEB funding and benefit plans need improvement.

FINDINGS and RECOMMENDATIONS

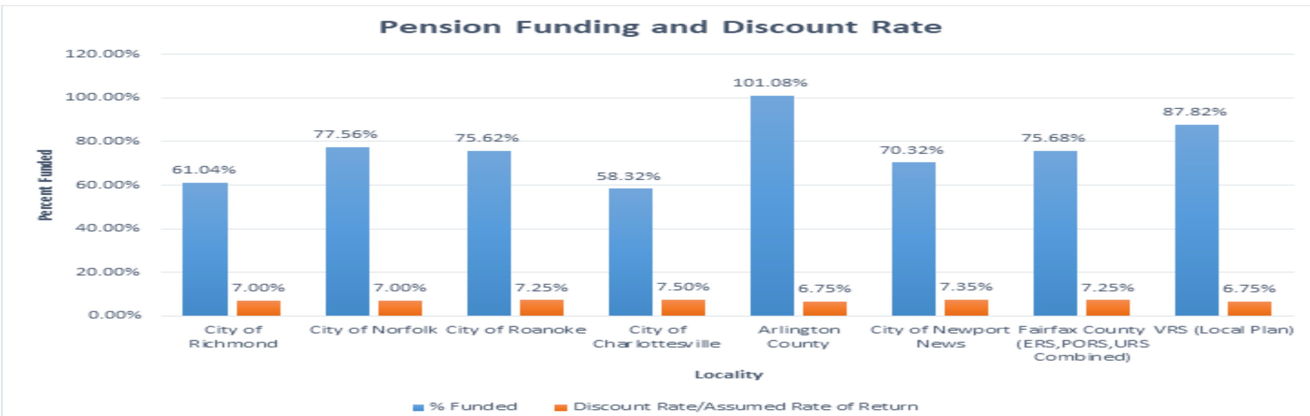
What Works Well

- Funding the Annual Required Contributions for Pension Plans – The City has consistently funded the Annual Required Contributions (ARC) over the last 10 years and contributed an additional $2 million over the required contributions in FY2019.
- Member of the Virginia Pooled OPEB Trust – In July 2018, the City of Richmond joined the Virginia Pooled OPEB Trust Fund to fund post-employment benefits other than pensions. To date, the City has contributed $750,000 to the Trust.

What Needs Improvement

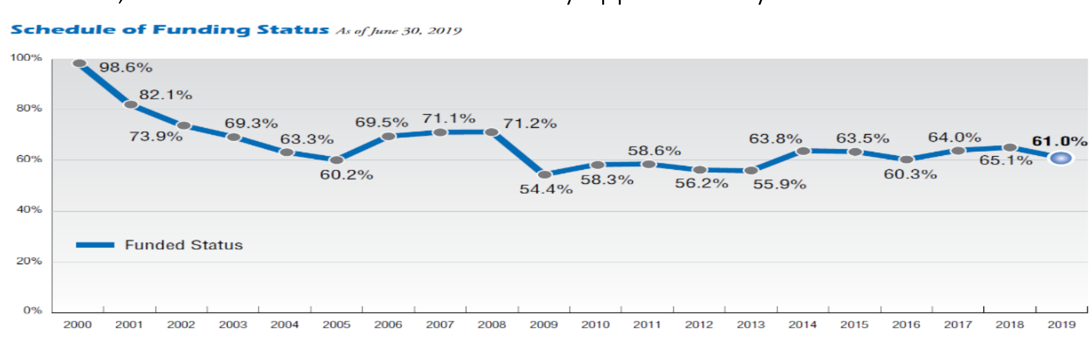
Finding #1 – Pension Funding and Annual Contributions

The auditors analyzed the City's funding status of the pension plan and compared it against several other large municipal plans in Virginia as of June 30, 2019. RRS maintained the second lowest funding percentage at 61.04%. The National Conference of Public Employee Retirement Systems' (NCPERS) average funded status was 72.6% for 2018.



Auditor Created Based on Information from Pension System CAFRs

Over the last 20 years, the funding status reached a low of 54.4% in FY2009 and has improved over the last decade. According to the RRS Executive Director, approximately $9.4 million is needed to improve the funding by one percent. Funded percentages are highly impacted by the Assumed Rate of Return as well as other factors. In FY2019 the RRS reduced that rate of return from 7.5% to 7%, which reduced the funded ratio by approximately 2.75%.



2019 RRS CAFR

Over the last ten years the City has funded the required contributions and deposited an additional $493,529 and $2 million in the RRS in FY2012 and FY2019, respectively. In FY2019 the City implemented a Voluntary Retirement Incentive Plan (VRIP) which 112 employees participated in. According to a RRS presentation to City Council in November 2019, the unfunded liability will increase by approximately $10.9 million and the funded status of the Retirement System will decrease by approximately 0.7%. No transfer of funds were sent to RRS to fund the VRIP. A VRIP was also done in FY2014, and according to the RRS Executive Director this increased the unfunded liability by $8.7 million and decreased the funded status by 0.6%. The following table shows a ten year history of the Plan:

FY Ending June 30,	Plan Fiduciary Net Position-Ending*	Total Pension Liability*	Funded Percentage	Actuarially Determined Contributions	Contributions Paid by City	Covered Payroll	Difference	Contributions as a % of Covered Payroll
2010	$ 459,436,000	$ 787,931,000	58%	$ 32,130,000	$ 32,130,000	$ 137,473,000		23%
2011	$ 493,375,000	$ 841,362,000	59%	$ 39,770,000	$ 39,770,000	$ 130,971,000		30%
2012	$ 476,123,000	$ 846,442,000	56%	$ 38,421,000	$ 38,914,529	$ 125,060,000	$ 493,529	31%
2013	$ 475,451,000	$ 850,867,000	56%	$ 40,446,000	$ 40,446,000	$ 116,666,000		35%
2014	$ 544,904,299	$ 854,284,141	64%	$ 42,342,620	$ 42,342,620	$ 110,748,076		38%
2015	$ 540,060,865	$ 850,911,445	63%	$ 46,684,500	$ 46,684,500	$ 111,738,352		42%
2016	$ 515,253,793	$ 854,875,197	60%	$ 44,926,043	$ 44,926,043	$ 108,015,367		42%
2017	$ 552,712,561	$ 863,992,966	64%	$ 42,911,076	$ 42,911,076	$ 107,363,266		40%
2018	$ 569,085,310	$ 874,789,363	65%	$ 46,548,902	$ 46,548,902	$ 107,814,490		43%
2019	$ 572,635,105	$ 938,077,477	61%	$ 46,539,647	$ 48,539,647	$ 108,326,347	$ 2,000,000	45%

Auditor Created Based on Information from Pension System CAFRs

* Prior to FY2014 GASB Changes - the funded percentage was calculated as the Actuarial Value of Assets divided by the Actuarial Liability

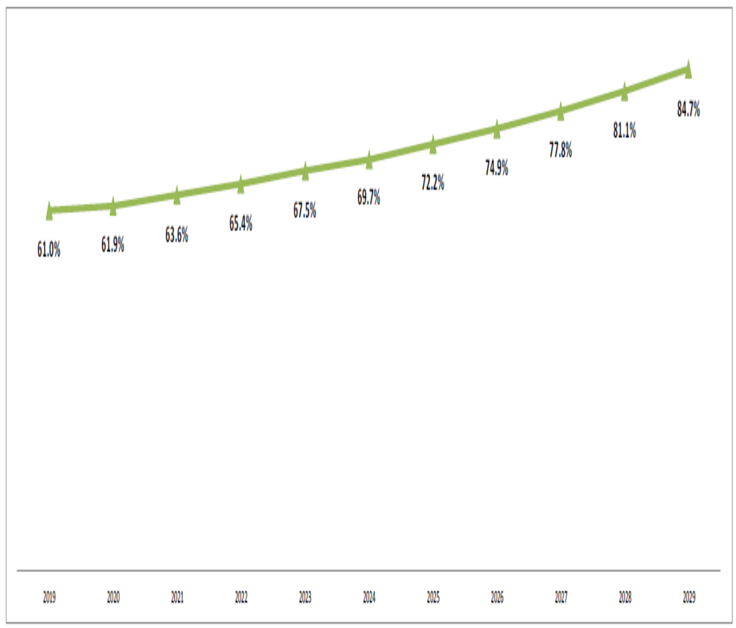
Additionally, DC Plan participants receive a disability pension from the DB Plan; yet those participants have not paid into the DB Plan for the pension they receive. According to the RRS Executive Director, these participants' drawing a disability pension from the DB plan, represent a bigger population of employees and corresponding disability payments in the future.

An experience study for the five year period of July 1, 2013 through June 30, 2018 was completed for the RRS. As a result of this experience study and an asset liability study, the assumed rate of return was lowered from 7.5% to 7.0% effective July 1, 2019. This change increased the employer contribution rate and decreased the system's funding percentage; however, it provided a more accurate representation of the system's funding and liabilities.

Based on a June 30, 2019 actuarial evaluation provided to a City Council committee in November 2019, the funded status was projected to improve if:

- 7% investment return is realized,
- The City continues to fund actuarially determined contributions, and
- The City does not do Ad-hoc Cost of Living Adjustments (COLA) or other benefit enhancements.

PROJECTED FUNDED STATUS



RRS Presentation to Council 11/4/2019

Chapter 22 of the City Code requires that City contributions to the RRS consists of a normal contribution (actuarially calculated ratio of the normal cost of all benefits and the gross annual payroll of all active members included in the valuation) plus an accrued liability contribution, which combined, equal the actuarially determined contribution. The accrued liability contribution is the amount necessary to amortize the unfunded actuarial liability and any increase or decrease in the unfunded actuarial liability in future years due to changes in actuarial assumptions, changes in RRS provisions, including the granting of Ad hoc COLAs, or actuarial gains or losses amortized over a closed period not exceeding 30 years.

Additionally, GASB 68, which was effective in fiscal years ending June 30, 2015 and later, changed how governments measure and report the long-term obligations and annual costs associated with the pension benefits they provide. It describes the procedures for measuring the total pension liability, which essentially involves the following three steps:

- Project total future benefit payments for current and former employees.
- Discount the projected benefit payments to their value at the time of measurement (present value).
- Attribute the present value of projected benefit payments to the periods when they were or will be earned – past, present, and future.

Statement No. 68 requires that all single employers use one actuarial cost method – entry age normal – applied as only a level percentage of payroll to attribute the present value of projected future benefits to past and future periods of employee service.

The City has historically allocated sufficient funding to cover actuarially determined contributions but needs several years of prudent fiscal management to reach a funded status similar to peer localities. VRIP programs impact the ability to improve the funded percentage. The City also allows DC plan participants to receive a disability pension from the DB plan even though those participants have not paid into the DB plan for the pension they receive.

The City's pension percent funded is much lower than peer localities. Continued funding of required contributions, additional funding, and careful evaluation of benefit enhancements can help improve the funded status of the RRS. The two VRIP programs over the last six years added approximately $20 million to the liability and impacted the funded percentage by approximately 1.3%. Additionally disability pensions for DC plan participants that are then added to the DB plan impact the funded percentage.

Recommendations:

1. ***We recommend the Chief Administrative Officer set aside additional funding for the pension liability in future Budgets presented to City Council.***

2. _We recommend the Chief Administrative Officer work with Human Resources to determine if an insured approach for disability benefits for Defined Contribution plan participants is a more efficient and cost-effective alternative._

Finding #2 – Pension Benefits

Most localities in Virginia provide retirement benefits through (VRS). The City of Richmond is one of the cities and urban counties that maintain their own retirement system. The City's DB and EDB Plans are closed to general employees hired on or after July 1, 2006. The DB plans are only available to full-time permanent sworn public safety employees and a select group of Senior Executives. Other employees are enrolled in a Defined Contribution (DC) Plan. Auditors compared the retirement and benefit provisions and benefits for these plans for new general and public safety employees to a group of other large non-VRS localities in Virginia as shown on the following tables:

Retirement Provisions for General Employees/Non-Public Safety Employees (New Members)

Locality	General Employee Contribution Rate	Normal Retirement Age	Average Comp-New Hires	Retirement Factors	DROP Years
City of Richmond - Defined Benefit	1.00%	Age 65 or 30 years of service	3 years	1.75%	N/A
City of Richmond - Enhanced Defined	4.57%	Age 65 or 30 years of service	3 years	2%	N/A
City of Charlottesville	5%	Age 65 with 5 yearsof service	5 years	1.60%	N/A
City of Norfolk	5%	Normal Social Security Age with 5 years OR Age + Service = 90 with 5 years of service	5 years	1.75%	N/A
City of Roanoke	5%	Age 65 with 5 years OR Age 55 with 30 years	5 years	2%	N/A
City of Newport News	5%	N/A New Employees - members of VRS Current members - Age 60 with 5 years or 30	3 years	N/A (Members of VRS)	N/A
Arlington County	4%	Age 62 with 5 years OR 30 years of service OR Age + Service = 80	3 years	1.70%	Up to 3 years
Fairfax County - General Employees Retirement	5.33%	Age 65 with 5 years OR Age 55 with 30 years (Service + Age = 85, min age 55)	3 years	2%	Up to 3 years
Virginia Retirement System	5%	Normal Social Security Age with 5 years OR Age + Service = 90	5 years	1% (Hybrid Plan)	N/A

Auditor Created Based on Information from Local Pension Systems Benefits Documentation

Senior executives contribute additional amounts depending on the benefits selected.

Retirement Provisions for Public Safety Employees (New Members)

Locality	Public Safety Employee Contrib Rate	Normal Retirement Age	Average Comp- New Hires	Retirement Factors	DROP Years
City of Richmond - Defined Benefit	1.50%	Age 60 or 25 years	3 years	1.65% + 0.75% to age 65	Up to 6 years
City of Richmond - Enhanced Defined Benefit	5.45%	Age 60 or 20 years	3 years	1.65% + 0.75% to age 65	Up to 6 years
City of Charlottesville	5%	Age 60 with 5 years	5 years	1.60%	N/A
City of Norfolk	5%	Age 60 with 5 years OR age 50 with 25 years, whichever occurs first	5 years	2.50%	Up to 4 years
City of Roanoke	5%	Age 65 with 5 years OR Age 50 with 25 years	5 years	2.00%	N/A
City of Newport News	5%	N/A New Employees - members of VRS Current members - Age 50 with 5 years or 25 years of service	3 years	N/A (Members of VRS)	N/A
Arlington County	7.50%	Age 52 with 5 years or 25 years or Age + Service = 80	3 years	2.5% and 2.7% until SS eligible	Up to 3 years
Fairfax County- Police Officers Retirement System	8.65%	Age 55 or 25 years of service	3 years	2.80%	Up to 3 years
Fairfax County- Uniformed Retirement System	7.08%	Age 55 with 6 years or 25 years of service	3 years	2.50%	Up to 3 years
Virginia Retirement System	5%	Age 60 with 5 years OR age 50 with 25 years	5 years	1.7% or 1.85%	N/A

Auditor Created Based on Information from Local Pension Systems Benefits Documentation

Based on the comparisons, the City's employee contribution rates are lower. The average years to calculate the Average Final Compensation (AFC) is three instead of five years and the Deferred Retirement Option Plan (DROP) is longer.

Early Retirement Reduction Factors

Locality	Early Retirement Reduction Factors- General Employees	Early Retirement Reduction Factors- Public Safety Employees
City of Richmond	5% per year up to 65 years old or 30 years of service whichever is smaller	5% per year up to 60 years old or 20/25 years of service whichever is smaller depending on plan selected.
City of Charlottesville	0.50% reduction for each month the actual retirement date is less than 30 years	0.50% reduction for each month the actual retirement date is less than 30 years (6% per year)
City of Norfolk	0.25% reduction for each month benefit payments precede normal service retirement	0.50% reduction for each month benefit payments precede normal service retirement (6% per year)
City of Roanoke	0.50% for each of the first 60 months before age or year requirements and 0.25% for each additional month in excess of 60 months.	0.50% for each of the first 60 months (6% per year) before age or year requirements and 0.25% for each additional month in excess of 60 months.
City of Newport News	0.50% reduction for each month benefit payments precede normal service retirement	N/A
Arlington County	0.50% for each month (6% per year) that retirement date precedes normal retirement eligibility	0.50% for each month (6% per year) that retirement date precedes normal retirement eligibility
Fairfax County - General Employees Retirement System	Benefits are reduced based on age in years and months from age 65- for example and age 50- receive 33.3% of full benefit, and age 64 receive 93.3%.	N/A
Fairfax County- Police Officers Retirement System	N/A	Benefits are reduced based on age and years of service in years and months
Fairfax County- Uniformed Retirement System	N/A	Benefits are reduced based on age and years of service in years and months
Virginia Retirement System	0.50% per month for the first 60 months away from normal retirement eligibility; 0.40% for next 60 months the member is away from retirement or an actuarially equivalent reduction factor for hybrid plan members.	0.50% per month for the first 60 months (6% per year) away from normal retirement eligibility; 0.40% for next 60 months (4.8% per year) the member is away from retirement or an actuarially equivalent reduction factor for hybrid plan members.

Auditor Created Based on Information from Local Pension Systems Benefits Documentation

COLAs

Locality	COLAS
City of Richmond	Ad hoc COLAs issued at the discretion of City Council
City of Charlottesville	No automatic COLAs
City of Norfolk	Ad hoc COLAs at the discretion of City Council
City of Roanoke	COLAs are provided to members that retire before 7/1/2014 and those members who retired after 7/1/2014 and have at least 15 years of creditable service. Members must be retired for at least one full year to be eligible. The amount is determined annually as 2/3rds of the US Average Consumer Price Index. The percentage increase for any one year shall not exceed the lesser of 4% or the pay raise generally awarded to active employees.
City of Newport News	1.26% in FY2019
Arlington County	Based on increases in the CPI-U and added to the benefit each July. 100% of the CPI-U increase up to a maximum of 3% plus one half of the CPI-U increase for the next 9%. This equates to a maximum of 7.5% for a 12% increase in the CPI-U
Fairfax County	Each year effective July 1, retirement benefits are increased by COLA based on the increase in the Washington-Arlington- Alexandria-DC-VA-MD-WV area consumer price index (CPI-U) for the 12 months ending March 31. This "automatic" COLA is equal to the CPI increase up to a maximum of 4.0%
Virginia Retirement System	Matches the first 2% increase in the Consumer Price Index for all Urban Consumers (CPI-U) and half any additional increase (up to 2%) up to a maximum COLA of 3% (Plan 2 and Hybrid Plan)

Auditor Created Based on Information from Local Pension Systems Benefits Documentation

Chapter 22 of the City Code lists eligibility for the DB Plans and the amounts of member contributions for both the DB and the EDB Plans. It also states the AFC is the average annual creditable compensation for the member's 36 highest consecutive months of creditable compensation. The Code also states that the duration of participation in the DROP for eligible public safety members shall not exceed six years.

The City has not modified pension benefits significantly since July 1, 2006 although the DROP period was lengthened in 2015. Many local governments in Virginia are members of the VRS, and VRS changed the mandatory 5% member contribution on local governments and school systems starting in July 2012 for employers who were paying all or part of the 5% member contribution. For new hires, the change started July 1, 2012. For existing employees, local governments and school systems had the option to phase in the 5% member contribution by 1% per year through July 1, 2016. The 2012 VRS legislation also provided offsetting salary increases to match the amounts existing employees began to pay. As discussed earlier, VRS also implemented a new plan (Plan 2) in July 2010 that increased the AFC formula from three to five years.

The City's collected amount from members in the DB Plans is less than peer local governments and VRS. If the City raises employee contributions as VRS did in 2012 for new hires **and** allocates this additional funding to the pension system, it would improve the system's funding over time. The City is contributing higher amounts to the pension system, where other localities have higher salaries but require larger contributions to their pension systems. The effect is shown in the following example of Police Officers' starting salaries, where gross salaries have a much larger difference than the net amounts.

Locality	Gross Salary After Completing the Academy Training	Mandatory Contribution to Pension System	Net Amount Before Taxes/Deductions
Chesterfield	$47,000	5%	$44,650
Henrico	$46,339	5%	$44,022
Richmond	$44,000	1.50%	$43,340

Auditor Created Based on Locality Public Salary Data

Recommendation:

3. *We recommend the Chief Administrative Officer create a cross functional team comprised of Human Resources, Finance, Budget, Public Safety and RRS staff to review the Pensions system as it pertains to member contributions, DROP, AFC and other factors, as appropriate to improve comparability in the marketplace with peer localities and improve long term funding of the Defined Benefit Plan. This review could also evaluate using VRS for new hires.*

Finding #3 – OPEB Funding

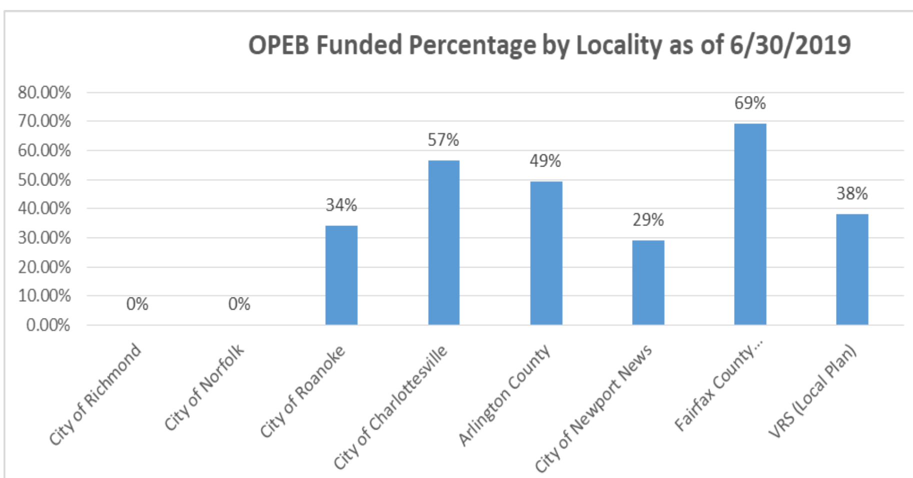
OPEB are benefits, such as health insurance, which have been promised to employees upon retirement. In years past, the cost of these benefits were primarily funded by local governments on a "pay as you go" basis. However, recent financial reporting standards now require disclosure of not only the OPEB liability but also reporting the liability in the financial statements along with required supplementary information. Annual Required Contributions needed to cover future and prior costs are also required to be listed.

The City's Net OPEB Liability has significantly increased in recent years. As of June 30, 2019 the balance was $83,978,162. The City has not been funding the annual contributions calculated for this liability. The City joined the Virginia Pooled OPEB Trust Fund in July 2018, which is managed by VML/VACO and has made three deposits totaling $750,000 ($250,000 each) in 2019 and 2020 to start reducing the liability. However these amounts are not sufficient to adequately address accumulated liabilities. The ARC has been significantly underfunded since 2015 as shown on the following table:

FY Ending June 30,	Total OPEB Liability	Annual Required Contributions	Contributions Paid by City	Difference
2010	$ 62,685,140	$ 9,538,680	$ 1,499,574	$ (8,039,106)
2011	$ 62,132,479	$ 6,413,437	$ 1,427,898	$ (4,985,539)
2012	$ 60,403,567	$ 5,292,027	$ 5,779,471	$ 487,444
2013	$ 57,808,421	$ 5,840,887	$ 5,558,153	$ (282,734)
2014	$ 68,014,890	$ 5,668,526	$ 5,422,850	$ (245,676)
2015	$ 68,014,890	$ 8,687,683	$ 3,607,535	$ (5,080,148)
2016	$ 69,995,667	$ 9,246,427	$ 3,585,780	$ (5,660,647)
2017	$ 72,394,963	$ 9,614,693	$ 3,854,714	$ (5,759,979)
2018	$ 80,416,926	$ 9,228,017	$ 2,958,026	$ (6,269,991)
2019	$ 83,978,162	$ 8,371,014	$ 3,397,610	$ (4,973,404)

Auditor Created Based on Information from City of Richmond CAFRs

Additionally, in comparison to some Virginia localities that also manage their own pension plans and their VRS local plan, the City's OPEB liability has not been adequately funded.



Auditor Created Based on Information from City/County CAFRs

GASB Statement NO. 75 identifies the methods and assumptions that are required to be used to project benefit payments:

- Discount projected benefit payments to their actuarial present value, and
- Attribute that present value to periods of employee service.

The net OPEB liability is measured as the portion of the present value of projected benefit payments to be provided to current active and inactive employees that is attributed to those employees' past periods of service (total OPEB liability), less the amount of the OPEB plan's fiduciary net position. This is generally determined by an actuarial valuation.

The City has not historically allocated sufficient funding to cover the liability. In 2020 the Budget Department proposed funding for $500,000 for the OPEB Trust, which was reduced to $250,000 in the final adopted budget. FY2018 was the first year that OPEB was required to be reported in the financial statements per GASB Statement No. 75 although information on this liability has been shown for many years in the financial statements' notes.

The OPEB liability has grown substantially in recent years and will continue to increase unless adequately funded. At some point negative bond rating agency impacts may occur if the City does not address this matter.

Recommendation:

4. ***We recommend the Chief Administrative Officer fully fund the OPEB Annual Required Contributions in future Budgets presented to City Council and set aside additional funding for the OPEB Trust.***

Finding #4 – OPEB Benefits

The City's liability for OPEB benefits was approximately $84 million as of June 30, 2019 and is increasing each year. The net OPEB liability is measured as the portion of the present value of projected benefit payments to be provided to current active and inactive employees that is attributed to those employees' past periods of service (total OPEB liability), less the amount of the OPEB plan's fiduciary net position. In comparison to some Virginia localities that also manage their own pension plans, and VRS (State Plan), the City's OPEB benefits have not been limited to reduce this liability as shown on the following table:

OPEB Benefits Provisions **Locality**	**Provisions**	**New Employees**	**Retirees / Current Members of Pension System**
Richmond	Only available for members of the Defined Benefit Plans- Under age 65 and has worked for COR for more than 15 years OR has worked for COR for more than 10 years with 5 years of continuous health insurance coverage to their effective retirement date. <10 years of service - 0% City Contribution 10-15 years- 50% City Contribution 15-25 year - 75% City Contribution 25 years or more - 100% City Contribution	**Variable Amount - Public Safety / Executives None- Regular General Employees**	**Variable Amount**
Charlottesville	Pension plan members **hired before 12/3/02**, received 100% of the City contributions towards the cost of medical and dental insurance. For pension plan members **hired on or after 12/3/2002**, the City contribution toward the cost of medical and dental is pro-rated based on vesting requirements and years of creditable service. Retired Before 7/1/2012 Must have 5 years of creditable service. Under Age 65: Can continue to participate in Health Care Program Over Age 65: Participates in program that provides Medicare Supplementary Insurance and certain wellness benefits. **Retired After 7/1/2012** Must have 10 years of creditable service. Under Age 65: Can continue to participate in Health Care Program. Health and Dental coverage end at Medicare eligibility age.	**Variable Amount**	**Variable Amount**
Norfolk	Per City CAFR- "City committed to a set contribution amount as an explicit subsidy if $25 or $35 per month for the City...". Effective 1/1/2014 eliminated post 65 healthcare coverage. Under age 65 with 15 years of continuous service with the City or retired from the City with accidental disability. Must have been enrolled as of their last day as an Active employee. Pre-65 retirees will continue to receive subsidy and will participate on the consortium with the active employees.	**Fixed Subsidy**	**Fixed Subsidy**
Roanoke	Retiree health insurance information was not available online. Per City CAFR- an additional monthly supplement equal to the greater of (a) $159 or (b) 75% of the amount the City contributes toward the cost of the a single active employee's health insurance shall be paid for eligible retirees terminating in the month in which the retiree attains age 65. Any member of the pension plan (excluding school board) and who retired with 20 or more years of service and prior to age 65 are eligible for this supplement. Employees hired after 6/30/2013 are not eligible for this supplement. Employees with 15 continuous years of active service and under the age of 65 may participate in the Employee's Post-Retirement Health Plan.	**Access Only**	**Variable Amount (75%) or Fixed Subsidy ($159 supplement)**

Newport News	**Not available to new employees after 3/1/2010 as these employees are members of VRS.** City retirees may continue only health/dental coverage, if any, that is in effect as of the date of retirement. When reaching age 65, city retirees and/or spouses are required to obtain Part A and B of Medicare, and the post-retirement benefit will consist of the Medicare carve-out plan. -Qualified city employees who are not eligible to retire based on age or service before 7/1/2005 are entitled to receive a graduated percentage of the premium paid by the fund, depending on years of city employment as follows: <10 years - 0%; 10, 11 - 5%; 12 - 10%; 13 - 15%; 14 - 20%; 15 - 25%; 16 - 31%; 17 - 37%; 18 - 43%; 19 - 49%; 20 - 55%; 21 - 64%; 22- 73%; 23 - 82%; 24 - 91%; 25+ - 100% -The dollar amount of the premium paid by the fund will be called 6/30/2005 with an annual COLA thereafter. -Employees hired on or after 3/1/2010 will participate in a Health Reimbursement Arrangement. The City will contribute 3% of the average city employee's salary. There will not be any city premium contribution at retirement. Funds are invested in the employee's name.	**None**	**Variable Amount**
Arlington	County pays a share of retiree health benefits based on retirement date. **Retired Before January 15, 2012** *6 Groups:* Max Subsidy ranges from $192 to $960 based on retirement chapter and years of service **Hired Before July 1, 2008 and Retired On or After January 15, 2012** *6 Groups:* Max Subsidy ranges from $120 to $600 based on retirement chapter and years of service **Hired On or After July 1, 2008** *6 Groups:* Max Subsidy ranges from $60 to $300 based on retirement chapter and years of service	**Fixed Subsidy**	**Fixed Subsidy**
Fairfax	**All Fairfax Retirement Systems -** Retirees pay the full cost of health and/or dental insurance. Retirees age 55 or older, or those retired on a service-connected disability, receive a monthly subsidy from the county toward the cost of a county health plan. 5-9 years at retirement- $40 10-14 years- $75 15-19 years- $165 20-24 years- $200 25+ years- $230	**Fixed Subsidy**	**Fixed Subsidy**
VRS	Retired state employees with at least 15 years of service credit are eligible for a tax-free reimbursement against qualified health insurance premiums retirees pay for single coverage, excluding any portion covering a spouse or dependents. The credit cannot exceed the amount of premiums and ends upon the retiree's death. Amount per year of service is dependent upon type of employee: State employees/ teachers/ professional school employees - $4 per year of service credit w/ no max credit per month; General registrars & their employees/ constitutional officers & their employees/ local social service employees - $1.50 per year w/ a $45 monthly cap OR $2.50 per year w/ a $75 monthly cap; Other political subdivision employees as elected by the employer - $1.50 per year w/ $45 monthly cap.	**Fixed Subsidy**	**Fixed Subsidy**

Auditor Created Based on Information from City/County CAFRs and Retiree Health Information from Various Localities

Additionally, we examined two of the large localities in the Richmond Region, Chesterfield and Henrico counties that are part of VRS for their primary pension plans. Chesterfield County provides an access benefit only for retiree health care for new hires after July 1, 2006. Henrico County provides a monthly supplement of $3 for each full year of service towards health care effective January 1, 2006.

There are two basic ways to manage the unfunded liability. One way is by allocating financial resources to fund the OPEB obligations, and another is to look at benefits offered and reduce liabilities for future benefits. The City has not funded the annual required contributions for OPEB for several years and is only one of two localities that still has a variable benefit amount for new hires eligible for the benefit (i.e. Public Safety/Execs).

The OPEB liability can be reduced by limiting future benefit payment costs either through only providing an access only benefit, fixed subsidy or controlling the amount of growth in the benefit costs with an inflation cap. OPEB liabilities can also be reduced by limiting the age an employee can begin to receive retiree healthcare (55 years). Once 65 years of age, retirees transition to Medicare coverage.

The City has not modified this benefit significantly since July 1, 2006. The City has not prioritized managing the long term liabilities of these benefits. Changing benefits especially for existing personnel can be challenging and changes can be easier to implement for new hires. The OPEB liability has grown substantially in recent years and will continue to increase unless adequately funded or benefit changes are implemented. At some point negative bond rating agency impacts may occur if the City does not address this matter.

Recommendation:

5. ***We recommend the Chief Administrative Officer create a cross functional team comprised of Human Resources, Finance, Budget and Public Safety staff to reduce the OPEB liability in future years to address OPEB benefits for health care for existing personnel and/or for new hires that can be proposed to City Council.***

APPENDIX A: MANAGEMENT RESPONSE FORM
2021-04 Pension & Other Post-Employment Benefits Audit

#	RECOMMENDATION	CONCUR Y/N	ACTION STEPS
1	We recommend the Chief Administrative Officer set aside additional funding for the pension liability in future Budgets presented to City Council.	Y	The Chief Administrative Officer will recommend additional funding for the RRS in future Mayor proposed Budgets to City Council.
#REF!	**TITLE OF RESPONSIBLE PERSON**		**TARGET DATE**
#REF!	Chief Administrative Officer		FY2022 Budget Year
#REF!	**IF IN PROGRESS, EXPLAIN ANY DELAYS**		**IF IMPLEMENTED, DETAILS OF IMPLEMENTATION**
#REF!			
#	**RECOMMENDATION**	**CONCUR Y/N**	**ACTION STEPS**
2	We recommend the Chief Administrative Officer work with Human Resources to determine if an insured approach for disability benefits for Defined Contribution plan participants is a more efficient and cost-effective alternative.	Y	The Chief Administrative Officer will work with Human Resources and RRS to perform an analysis of the insured approach for disability benefits for the Defined Contribution plan
#REF!	**TITLE OF RESPONSIBLE PERSON**		**TARGET DATE**
#REF!	Chief Administrative Officer		FY2022 Budget Year
#REF!	**IF IN PROGRESS, EXPLAIN ANY DELAYS**		**IF IMPLEMENTED, DETAILS OF IMPLEMENTATION**
#REF!			
#	**RECOMMENDATION**	**CONCUR Y/N**	**ACTION STEPS**
3	We recommend the Chief Administrative Officer create a cross functional team comprised of Human Resources, Finance, Budget, Public Safety and RRS staff to review the Pensions system as it pertains to member contributions, DROP, AFC and other factors, as appropriate to improve comparability in the marketplace with peer localities and improve long term funding of the Defined Benefit Plan. This review could also evaluate using VRS for new hires.	Y	The Chief Administrative Officer will create a cross functional team, as described, to review the Pensions system as it pertains to member contributions, DROP, AFC and other factors, as appropriate to improve comparability in the marketplace with peer localities and improve long term funding of the Defined Benefit Plan. This review could also evaluate using VRS for new hires.
#REF!	**TITLE OF RESPONSIBLE PERSON**		**TARGET DATE**
#REF!	Chief Administrative Officer		6-Oct-20
#REF!	**IF IN PROGRESS, EXPLAIN ANY DELAYS**		**IF IMPLEMENTED, DETAILS OF IMPLEMENTATION**
#REF!			
#	**RECOMMENDATION**	**CONCUR Y/N**	**ACTION STEPS**
4	We recommend the Chief Administrative Officer fully fund the OPEB Annual Required Contributions in future Budgets presented to City Council and set aside additional funding for the OPEB Trust.	Y	The Chief Administrative Officer will recommend fully funding the Annual Contribution in future Mayor proposed Budgets to City Council.
#REF!	**TITLE OF RESPONSIBLE PERSON**		**TARGET DATE**
#REF!	Chief Administrative Officer		FY2022 Budget Year
#REF!	**IF IN PROGRESS, EXPLAIN ANY DELAYS**		**IF IMPLEMENTED, DETAILS OF IMPLEMENTATION**
#REF!			
#	**RECOMMENDATION**	**CONCUR Y/N**	**ACTION STEPS**
5	We recommend the Chief Administrative Officer create a cross functional team comprised of Human Resources, Finance, Budget and Public Safety staff to reduce the OPEB liability in future years to address OPEB benefits for health care for existing personnel and/or for new hires that can be proposed to City Council.	Y	The Chief Administrative Officer will create a cross functional team comprised of Human Resources, Finance, Budget and Public Safety staff to reduce the OPEB liability in future years to address OPEB benefits for health care for existing personnel and/or for new hires that can be proposed to City Council.
#REF!	**TITLE OF RESPONSIBLE PERSON**		**TARGET DATE**
#REF!	Chief Administrative Officer		6-Oct-20
#REF!	**IF IN PROGRESS, EXPLAIN ANY DELAYS**		**IF IMPLEMENTED, DETAILS OF IMPLEMENTATION**
#REF!			