ROANOKE, VIRGINIA, Ensures a Financially Sustainable Retirement Plan

BY ANN SHAWVER
The City of Roanoke’s “Ensuring a Financially Sustainable Retirement Plan” initiative won a GFOA Award for Excellence in 2013.

The City of Roanoke, Virginia, revised its retirement benefits for future employees, giving them a choice between two new plans. The project—a smooth and successful process that involved stakeholders from beginning to end—had the full support of the seven-member city council. Although these benefit modifications are not drastic, the changes are expected to ultimately lower the city’s long-term contribution rate by 10 percentage points, to 15 percent of wages. In today’s dollars, that amounts to approximately $6 million. The main reasons for the project’s success are stakeholder involvement, good timing, and transparency.

**BACKGROUND**

Roanoke is one of about a dozen communities in the state that provides its own defined benefit pension plan instead of participating in the Virginia Retirement System. (See Exhibit 1 for key elements of the retirement benefits provided before and after the plan modifications.) The city has more than 1,800 retirees, compared to an active workforce of approximately 1,700. The average active employee earns a little more than $40,000 and has been employed for 11 years, and the average retiree served Roanoke for 28 years.

The plan’s funded rate was consistently at 80 percent or greater, and Roanoke had always made its full actuarially required contribution, but contribution rates had risen steadily since fiscal 2001 (see Exhibit 2). A 2009 forecast by the city’s actuary indicated that rates could climb to 35 percent within a decade. Contributing to this trend were benefit

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<thead>
<tr>
<th>Component</th>
<th>Original Benefit</th>
<th>New Benefit</th>
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<tbody>
<tr>
<td>Plan Type</td>
<td>Defined Benefit</td>
<td>Choice of Defined Benefit (Plan A) or Hybrid (Plan B)</td>
</tr>
<tr>
<td>Multiplier</td>
<td>2.1%</td>
<td>2% (Plan A) or 1 Percent (Plan B)*</td>
</tr>
<tr>
<td>Maximum Replacement Percent</td>
<td>63% (2.1 Percent x 30 Years)</td>
<td>63% (2 Percent x 31.5 years)</td>
</tr>
<tr>
<td>Average Final Compensation</td>
<td>Highest 36 Months</td>
<td>Highest 60 Months</td>
</tr>
<tr>
<td>Vesting</td>
<td>5 Years</td>
<td>5 years (City Contribution to Pension, Retirement Health Savings Account)</td>
</tr>
<tr>
<td>Employee Contribution</td>
<td>None</td>
<td>5% of Salary (Pretax) toward DB (Plan A) or DC (Plan B)</td>
</tr>
<tr>
<td>Retirement Eligibility — Normal (General/Public Safety)</td>
<td>Age 50/45 with Age + Service 80/70, or Age 65 with 5 Years’ Service</td>
<td>Age 55/50 with Age + Service 85/75, or Age 65 with 5 Years’ Service</td>
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<tr>
<td>Retirement Eligibility — Early (General/Public Safety)</td>
<td>Age 55 with 5 Years’ Service (Reduced Benefit)</td>
<td>Age 55/50 with 15 Years’ Service (Reduced Benefit)</td>
</tr>
<tr>
<td>Retirement Eligibility — Deferred Vested (General/Public Safety)</td>
<td>Age 65 or Age 55 with Reduced Benefit</td>
<td>Age 65 or Age 60 with Reduced Benefit</td>
</tr>
<tr>
<td>Cost of Living Adjustments</td>
<td>Ad Hoc (Determined Annually Based on Funding Availability, Trends in other Systems)</td>
<td>Policy Established: COLA of 2/3 CPI, not to Exceed 4%, Not to Exceed Active Employee Pay Raise; Payable to Retirees with 15 Years’ Creditable Service</td>
</tr>
<tr>
<td>Pension Plan Supplement</td>
<td>Monthly Cash Supplement of $330*** for Retirees with 20 Years’ Service until Age 65 (Taxable)</td>
<td>None</td>
</tr>
<tr>
<td>Retirement Health Savings Account</td>
<td>None</td>
<td>Eligible for City Pension Plan Members: 1% of Salary, Paid by Employee and 1% of Salary, Paid by City (Pretax)</td>
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* Plan B benefit is actuarially equivalent to Plan A via a deferred compensation component

** -75% city contribution toward active employee health care
enhancements, the practice of awarding ad hoc cost-of-living adjustments (COLAs), and the increasing longevity of retirees. The city’s director of finance felt that long-term financial planning was needed before contribution rates became a public and political issue.

GETTING STARTED

To get the project underway, the Roanoke city council’s agreement was obtained, a core team was appointed, goals were set, and a financial advisor was selected to provide any expertise needed to augment core team members’ skills. The core team initially comprised the Roanoke city manager, both assistant city managers, the director of finance, assistant director of finance, director of human resources, director of management and budget, director of general services, and retirement supervisor.

While the core team had significant experience and expertise in relevant areas, it was also entirely made up of individuals who were 45 or older, most of whom had been employed by the city for ten years or more. To make sure the views of incoming employees were considered, the team added an accountant who was in her mid-twenties and had less than five years of service. To make team activities as efficient and effective as possible, only individuals who had relevant professional expertise were included — although this also made the group fairly homogenous. Therefore, the team was careful to use a variety of methods for making sure input from other city employees was considered.

The first thing the team did was establish project goals, even before it engaged a retirement benefits financial advisor. Once the advisor was chosen, he helped review the goals and assisted in finalizing them, as shown in Exhibit 3.

Outside expertise was an invaluable part of the project. Over the first few meetings, the benefits advisor provided a number of ideas about retirement benefits for future employees. (The changes went into effect July 2014.) His specialized expertise in benefits, coupled with the team’s deep knowledge of city employees, led Roanoke to the best set of recommended changes. The benefits advisor provided information about trends in retirement benefits and explained

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**Exhibit 2: Annual Increase in Pension Contribution Rates**

Every 1% Now Costs $600,000 Annually

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<tbody>
<tr>
<td>Percent</td>
<td>2</td>
<td>4</td>
<td>6</td>
<td>8</td>
<td>10</td>
<td>12</td>
<td>14</td>
<td>16</td>
<td>18</td>
<td>20</td>
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Source: Roanoke Pension Plan Comprehensive Annual Financial Reports

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The main reasons for the project’s success are stakeholder involvement, good timing, and transparency.
which benefit modifications had the greatest impact in reducing cost, and he led the group through several brainstorming sessions aimed at developing a list of potential benefit modifications. Other outside professionals involved in the project included legal counsel, who reviewed changes for Internal Revenue Service and Department of Labor compliance, and actuaries, who calculated future contribution rates in light of the options under consideration.

TRANSPARENCY AND COMMUNICATION

Employee input was a large part of the project and an element that directly contributed to its success. Although the retirement benefit changes would be enacted for future employees, not current employees, input from the existing workforce was valuable to the team. This input was gathered in a variety of ways, initially via focus groups. The team selected focus group members by taking a sample of employees from throughout the organization, ensuring adequate representation by age, gender, department, supervisory status, pay grade, and race. The team held 12 focus groups that were attended by 129 employees, or 8 percent of the workforce. These discussions centered on:

- The age and service level at which an employee should be granted a retirement benefit.
- The importance of key benefit features like defined benefit versus defined contribution or hybrid plans, and cost-of-living increases.
- The age at which a benefit should be provided for normal retirement and early retirement, and for individuals with a vested benefit who were no longer employed by the city.

The team also offered sessions that could be attended by anyone who was curious about the retirement benefits project. In these sessions, employees were updated about the project and were encouraged to ask questions. By the end of the project, several hundred employees had been briefed about the modifications.

Of course, city leadership had to be kept in the loop, as well. The team provided monthly updates at directors’ meetings and additional outreach sessions targeting influential organizational leaders (such as the city’s five elected constitutional officers). And the team made a special effort to maintain a dialogue with the police and fire chiefs — a proactive approach that helped keep the city’s efforts from running aground when it proposed benefits modifications that would affect public safety employees, a significant component of the workforce.

Exhibit 3: Goals of the Retirement Benefits Financial Planning Project

Comprehensively evaluate and make recommendations on retirement benefits provided to city employees with goals of:

1. Providing retirement benefits that, in conjunction with other compensation, will be competitive in the Roanoke market.
2. Providing retirement benefits that will successfully attract, motivate, and retain employees.
3. Ensuring that such benefits are sustainable and acceptable to the community, employees, and elected officials.
4. Maximizing the amount of return on assets to provide the best benefit possible for a given amount of investment.

Benefits under examination include the Roanoke Pension Plan, deferred compensation plan, and retiree medical plan.
Successful pension reform projects depend on a consistent message, and the team also held outreach sessions with other stakeholders in an effort to reach as many interested parties as possible. Doing so required an investment of time, but meeting with key individuals honored their importance and helped relay project facts. Spending time with key stakeholders such as the leadership of the Retiree’s Association and of other employers that participate in the Roanoke Pension plan (including the Roanoke Valley Detention Commission and the Roanoke Regional Airport Commission) helped ensure that the right message was being shared about the project and dispel any rumors.

The assistant director of finance or the retirement supervisor, or both, also met with anyone who asked. Doing so involved a major time commitment, but it did a lot of good, demonstrating the team’s confidence in its work to the organization, and its dedication to doing the project the right way. These efforts toward openness and transparency heightened employee acceptance.

Another key element of stakeholder involvement was in keeping city council members informed. While the routine work on this project was done by the team, the city council’s support was crucial. City council members were briefed in public session in December 2011, when initial recommendations were made, and again in July 2012, when revised recommendations were presented. Transparency is best advanced through public sessions, but more regular private discussions kept elected officials updated, and both means of communication were important.

**TIME AND TIMING**

A major theme of the Roanoke project is that patience paid off. The effort took a long time — more than two years from commencement to the city council’s approval of the benefit changes. Conservative choices about timing and a willingness to invest staff resources in the project were essential to its success. For instance, additional phases of employee involvement were added in response to feedback, and core team members contributed hundreds of hours to the project.

An effort of this nature needs to be timed carefully to make sure it doesn’t become a hot-button issue, leading to emotional reactions among the community, elected officials, and the media, which can derail a project immediately. Because Roanoke’s pension plan was strong when it started on this endeavor, there was never any rush to make changes. The project team was able to time its work in a way that kept the effort moving forward while avoiding any potential turbulence.

Timing was also important when it came to implementing the approved modifications. Changes were staggered to help Roanoke’s relatively small retirement benefits and human resources staff conduct the employee training and outreach needed.

**THE RESULT**

The recommended changes are working to stabilize future contribution rates (see Exhibit 4), which are expected to fall by approximately 10 percent. One reason the changes were

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Roanoke had always made its full actuarially required contribution, but the 2009 forecast indicated that rates could climb to 35 percent within a decade.
so well accepted was their theme of give and take. Employees gained a choice among two plans, defined benefit or hybrid; the previously ad hoc COLA was formalized, and employees were enrolled in a health savings account. In exchange, new hires would no longer be eligible for a costly supplement that had been provided to retirees with more than 20 years of service, up to age 65, to cover health care — although the supplement was part of the monthly pension payment, with no requirements on its use. This provision had been added to remain competitive with the Virginia Retirement System, which offered a similar benefit, and it provided the greatest income to the employees who left the organization the earliest. This was not the type of incentive current leadership wanted to provide its loyal employees, and in addition, it cost nearly 3 percent of payroll. Replacing this supplement with a health savings plan more equitably rewarded employees for service to the city. Another item that reduces the city’s costs is a longer period over which the average final compensation was determined — from 36 to 60 months, consistent with many other plans. Finally, introducing a 5 percent required contribution for all new hires meant employees would begin sharing the costs of the pension plan, a model that is much more acceptable to the public.

Some critics might question the wisdom of formalizing a COLA. The city did consider adopting a no-COLA policy, but team members felt that in reality, the COLA was not going away in a normal economic environment. Team members knew that the requirements of Governmental Accounting Standards Board Statement No. 68, Accounting and Financial Reporting for Pensions — An Amendment of GASB Statement

### Exhibit 4: Changes Stabilize Future Contribution Rates

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>2012*</th>
<th>2017</th>
<th>2022</th>
<th>2027</th>
<th>2032</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost 18.04%</td>
<td>25</td>
<td>20</td>
<td>15</td>
<td>10</td>
<td>15</td>
</tr>
<tr>
<td>Cost 15.47%</td>
<td>18</td>
<td>15</td>
<td>10</td>
<td>5</td>
<td>5</td>
</tr>
</tbody>
</table>

Source: 2011 Actuarial Study — Millian, Inc.

*in 2012, there is no funding for a COLA. Future years include a COLA

### The Role of the Finance Officer

Roanoke’s retirement sustainability project is an example of what finance officers can do to help lead their organizations. In this case, the finance officer studied an area of the organization — retirement benefits — to ensure that the organization’s long-term planning goals were being met. Though projects like this can pose political risk, the professional skills the finance officer brings to the table can help ensure a data-driven process where information can be presented in a logical manner to aid decision makers. The finance officer understands the need for transparency in working on this kind of project and has the financial and analytical skills to successfully navigate some of its more technically complex aspects.
No. 27, would mandate consideration of the ad hoc COLA in actuarial computations. The team viewed this as an opportunity to tie the COLA to a formula and to limit the number of retirees to whom it applied. The COLA formula provides two thirds of the urban Consumer Price Index figure, not to exceed 4 percent and not to exceed the pay raise granted to active employees. The COLA will be provided only to retirees who have served the city for 15 years or more. These limitations made the new COLA cost less than the prior ad hoc COLA.

LESSONS LEARNED

The best thing the Roanoke team did was to be patient and willing to go back to the drawing board and consider new options, even though it would have been easier not to. This obvious commitment to a good product and professionalism gave stakeholders confidence, and the city achieved a better result because of some of those suggestions and input. An example of this is a modification to the team’s initial recommended age at which employees could retire. The initial recommendation was age 60 (55 for public safety), with combined age and years of service totaling 85 (75 for public safety). Based on feedback from the police and fire chiefs, however, these ages were changed to 55 and 50 because the Virginia Retirement System offered public safety employees a retirement age of 50. All the surrounding jurisdictions participated in that plan, so having a greater retirement age could have adverse effects on Roanoke’s recruitment and retention results.

Roanoke team members gained some valuable insights that might benefit other jurisdictions considering a similar project. One suggestion: Do not change actuaries while implementing changes. Roanoke used one actuarial firm during the project phase, and it was using a different firm by implementation phase. This best met procurement standards, but Roanoke team members quickly learned that different actuaries arrive at different conclusions. After the project, the new actuary arrived at a higher contribution rate than the former actuary had, based on the same underlying data. This put unnecessary budgetary pressures on the community. Working with purchasing and legal staff to extend the city’s agreement with the initial actuary could have mitigated a certain amount of organizational distress.

Pension reform efforts are long term in nature, but to succeed, jurisdictions also need to consider the short term. City officials realized this during Roanoke’s fiscal 2015 budget preparation process. Because the COLA formula was implemented before any cost-savings measures took effect, fiscal 2015 contribution rates increased enough to place pressure on the fiscal 2015 budget balancing process. While formalizing the COLA was a wise decision in the long run, the resulting $60 million liability increase was challenging in the short run. It might have been helpful to delay the COLA implementation until the pension plan had recognized some of the most recession-related investment returns and until the project’s cost-saving measures began lowering contribution rates. By carefully examining both the long-term and short-term impacts of pension reform, organizations can optimize the timing of benefit changes.

CONCLUSIONS

Only two speakers voiced concerns at the city council meeting where a unanimous vote amended the Roanoke City Pension Code — in stark contrast to a public budget hearing just a few years before where public safety employees had filled the city council chamber because reductions in fire stations had been included as part of the recommended budget. Roanoke leaders cite an inclusive, thorough, well-timed, communication-driven process as the reason for the acceptance of the pension reform measures.

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