Funding Basics of Retirement Programs

Monroe County Employees Retirement System
Monroe County Retiree Health Care Plan

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Agenda

- Background
- What is an Actuarial Valuation?
- Pre-Funding and Accounting Basics
- Retirement System
  - Highlights of the December 31, 2011 Valuation
  - Asset Performance
  - Looking Ahead

Agenda

- Retiree Health Plan
  - Highlights of the December 31, 2011 Valuation
  - Current Issues and Implications
  - Comparing Various Retiree Health Plans
  - Possible Steps for the County
  - What Others Have Done

Background

- The Retirement System and the Retiree Health Plan are defined benefit arrangements:
  - A promise made to employees, that benefits will be provided by the plan sponsor upon retirement
  - Retirement System benefits are clearly defined (i.e., in collectively bargained agreement, plan document, etc.)
  - Retiree Health benefits may not be clearly defined

Background

- In order for a benefits program to be self-sustaining, the following must hold:

$$C + I = B + E$$

- C - contributions
- I - investment income
- B - benefits
- E - expenses

Background

- What is the actuary's role?
  - Perform actuarial valuation to determine contributions such that the plan remains solvent
    - Contribution calculated by actuary is reasonable based on known past information and assumptions about future events
  - Estimate cost of proposed benefit changes
  - Be an advisor to policy makers with respect to the actuarial operations of the plan
  - Actuary performs these duties using:
    - Generally accepted actuarial principles and,
    - In accordance with standards of practice prescribed by the Actuarial Standards Board
  - Actuary is not a decision maker

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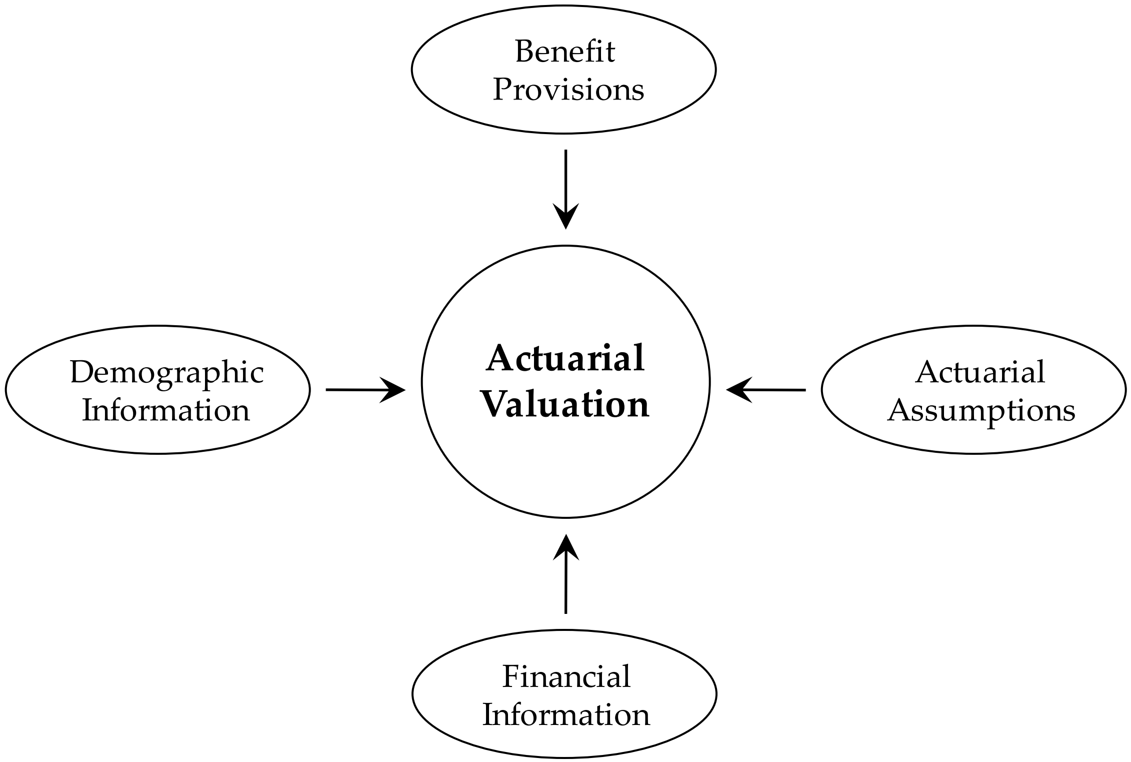
What is an Actuarial Valuation?

- A mathematical process used to project future benefit payments based on specified benefit provisions, assumptions and participant data.

- These projected benefit payments are converted to equivalent present value amounts and the annual contribution is determined.

What is an Actuarial Valuation?



Demographic information, Financial information and Benefit Provisions are provided by the plan sponsor.

Actuarial Assumptions are recommended by the actuary and approved by the plan sponsor or board.

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What is an Actuarial Valuation?

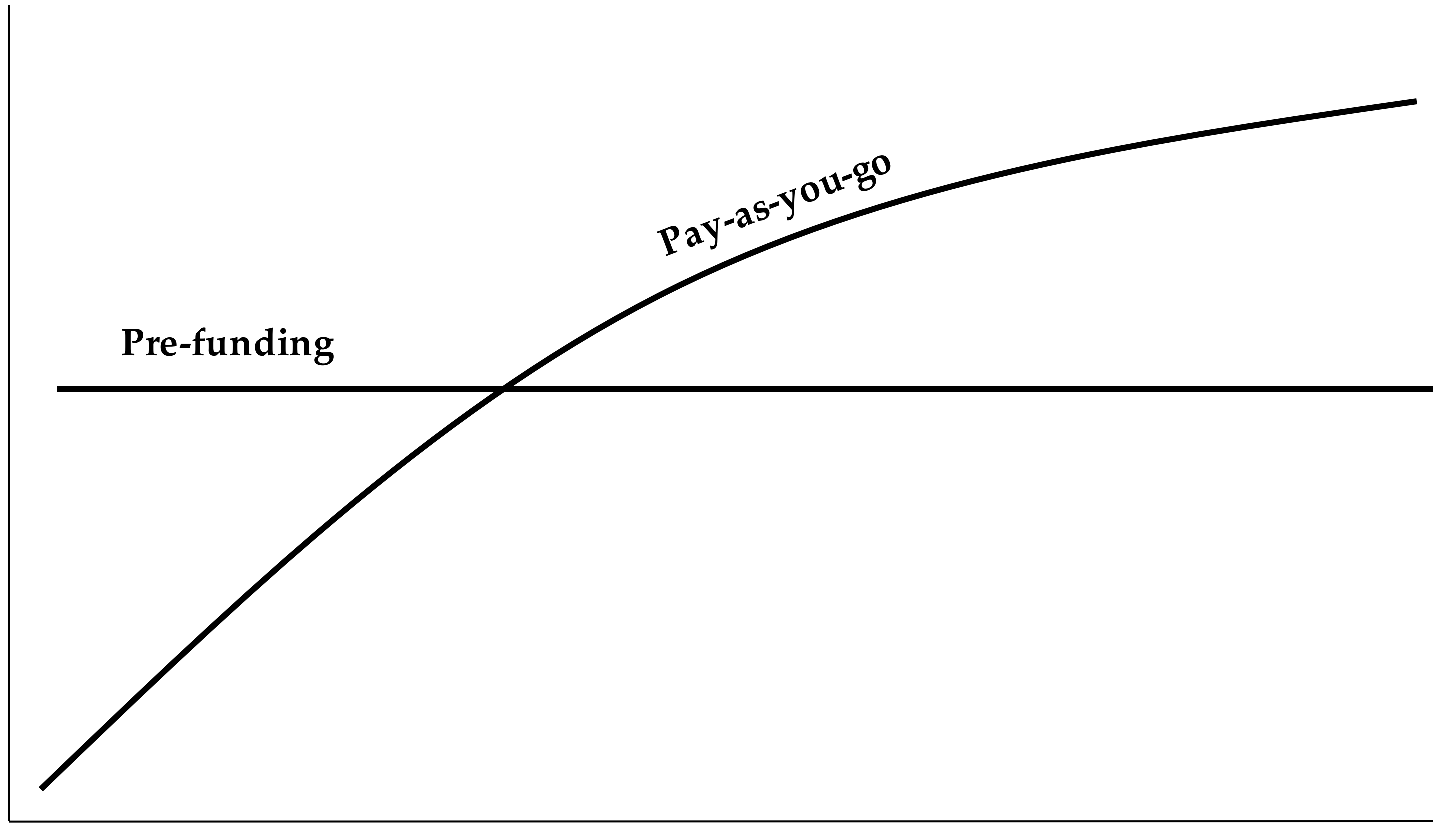
- Purpose of an actuarial valuation:
  - Understand the cost of the promise that has been made
  - Establish or maintain a funding program
  - Provide information for financial reporting
  - Assess long term cost implications of proposed benefit changes
  - Comply with legal and/or accounting requirements

Pre-Funding & Accounting Basics

- Pay-as-you-go funding
  - Pay benefits when they are due
  - Increasing cost method, as group matures and there are more retirees

- Pre-funding
  - Set aside money now, to pay for benefits later

Pre-Funding & Accounting Basics



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Pre-Funding & Accounting Basics

- Why pre-fund?
  - Benefit security for plan members
  - Assets can generate investment income to help pay for the benefits
  - More level contribution pattern, so future generations of taxpayers will not be obligated to higher costs than the current generation
  - Prudent thing to do

Pre-Funding & Accounting Basics

- Consequences of not pre-funding
  - May not have enough money to pay the benefits promised
  - Forgo investment returns that could help pay for the cost of the benefits
  - Higher costs to future generations of taxpayers
  - Would likely have to lower or eliminate the benefits

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Pre-Funding & Accounting Basics

- Retirement System
  - State law requires pre-funding
  - Subject to GASB Statements No. 25 and 27 (current)
  - Subject to GASB Statements No. 68 and 70 (future)

- Retiree Health Plan
  - There is no state or federal law that requires pre-funding
  - Subject to GASB Statements No. 43 and 45

Pre-Funding & Accounting Basics

- Retiree Health Accounting Standards
  - Statements No. 43 and 45 are accounting standards, not funding requirements
  - There is no state or federal law that requires pre-funding of retiree health plans
  - However, GASB Statements No. 43 and 45 encourage pre-funding
  - If the County contributes less than the amount under the GASB requirements:
    - There will eventually be a large liability on the financial statements (Net OPEB Obligation)
    - It could impact the County's ability to borrow

Retirement System – Highlights of the December 31, 2011 Valuation

	Computed Contributions for Fiscal Year as Percentage of Payroll	
Fiscal Year	2012	2013
Valuation Date	12/31/2010	12/31/2011
General County	22.23 %	23.75 %
County Agency	32.33	34.12
Sheriff's Office	24.11	26.26
County Library	11.23	13.11
Road Commission	18.35	19.15
Mental Health	10.42	9.92
Central Dispatch	20.48	19.42

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Retirement System – Highlights of the December 31, 2011 Valuation

December 31, 2011	General County	County Agency	Sheriff's Office	County Library	Road Commission	Mental Health	Central Dispatch	Total
Participants								
Actives	298	25	141	116	83	131	19	813
Retired	329	29	113	44	79	64	8	666
Terminated Vested	60	-	6	9	6	44	-	125
Total	687	54	260	169	168	239	27	1,604
Payroll	$13,172,137	$1,213,962	$8,896,323	$4,183,212	$4,420,722	$6,064,436	$941,196	$38,891,988
Actuarial Accrued Liability	99,680,702	11,009,637	59,762,734	16,000,359	28,410,037	22,235,817	3,786,539	240,885,825
Actuarial Value of Assets	76,925,002	6,730,788	44,772,276	14,626,308	22,470,866	23,502,554	2,986,096	192,013,890
Unfunded Actuarial Accrued Liability	22,755,700	4,278,849	14,990,458	1,374,051	5,939,171	(1,266,737)	800,443	48,871,935
Funded Ratio	77%	61%	75%	91%	79%	106%	79%	80%
Contribution Requirement								
Normal Cost	12.65%	11.46%	15.43%	11.00%	10.51%	12.27%	13.95%	12.80%
Amortization Payment	11.10	22.66	10.83	2.11	8.64	(2.35)	5.47	7.92
Total	23.75%	34.12%	26.26%	13.11%	19.15%	9.92%	19.42%	20.72%*
$ Contribution	$3,383,658	$448,003	$2,526,806	$593,170	$915,648	$650,682	$197,695	$8,715,662
$ Contribution from 12/31/2010 Valuation	$3,095,420	$405,952	$2,171,615	$574,497	$849,507	$697,120	$190,539	$7,984,650

* *Weighted average based on total payroll.*

Retirement System – Highlights of the December 31, 2011 Valuation

- Employer contribution rates have increased for most divisions since the 2010 valuation as a result of:
  - Unfavorable investment performance working its way through the asset smoothing method
  - Demographic experience varied by division

Retirement System – Asset Performance

	December 31,					
	2006	2007	2008	2009	2010	2011
Market Value of Assets	$177,532,251	$187,790,674	$148,763,118	$165,646,245	$176,702,630	$166,315,177
Rate of Return	11.36%	7.80%	-19.30%	14.47%	9.65%	(2.07)%
Actuarial Value of Assets	$169,283,765	$181,320,182	$184,967,843	$188,779,278	$192,859,386	$192,013,890
Rate of Return	6.34%	9.24%	3.74%	4.46%	4.71%	3.48%

Retirement System – Looking Ahead

- Contribution rates are expected to increase in the short term as a result of the unfavorable investment performance from 2008 and 2011
- In the long term, contribution rates are expected to approach the long term cost of the benefits, or the normal cost

Retirement System – Looking Ahead

- Retirement System
  - Funded ratio above national averages; varies by group
  - Has assets equal to 14 times benefit payments
  - Will continue to mature (not an issue for a pre-funded plan)
  - Is paying out more in benefits than is receiving in contributions; investment income pays for most of the benefits (this is the concept behind a pre-funded plan)
  - Actuarial assumptions are compliant with recent changes in Actuarial Standards of Practice.
    - Mortality table projected with improvements through 2020
    - Interest rate of 7.0% is still very reasonable

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Retiree Health Plan - Highlights of the December 31, 2011 Valuation

	Computed Contributions	
Fiscal Year	**2012**	**2013**
Valuation Date	**12/31/2010**	**12/31/2011**
General Billable	$1,374,952	$1,297,226
General Non-billable	3,557,282	3,471,081
Sheriff Billable	959,000	930,661
Sheriff Non-billable	2,367,667	2,404,819
Dispatchers	174,371	149,029
Subtotal	8,433,272	8,252,816
County Agency	654,134	615,902
Grand Total	9,087,406	8,868,718

- *These amounts represent the total contribution before adjustment for member contributions. Based on information provided by the County, the expected member contributions will be $402,398 for the fiscal year beginning January 1, 2013 ($286,303 for the fiscal year beginning January 1, 2012).*

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Retiree Health Plan - Highlights of the December 31, 2011 Valuation

	General County		Sheriff's Office				County	
	Billable	Non-Billable	Billable	Non-Billable	Dispatchers	Subtotal	Agency	Combined
A. Accrued Liability								
Retiree	$10,446,925	$33,120,851	$4,316,885	$20,093,144	$1,483,354	$69,461,159	$5,447,884	$74,909,043
Active	5,836,571	8,683,323	5,701,702	8,357,562	1,040,366	29,619,524	1,663,296	31,282,820
Total	16,283,496	41,804,174	10,018,587	28,450,706	2,523,720	99,080,683	7,111,180	106,191,863
B. Valuation Assets	4,967,730	9,456,548	3,620,085	8,531,323	1,673,158	28,248,844	1,507,456	29,756,300
C. Unfunded Accrued Liability: (A) - (B)	11,315,766	32,347,626	6,398,502	19,919,383	850,562	70,831,839	5,603,724	76,435,563
D. Funded Ratio: (B) ÷ (A)	30.5%	22.6%	36.1%	30.0%	66.3%	28.5%	21.2%	28.0%

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Current Issues and Implications

- It is our understanding
  - The County has not contributed the full actuarial amount in the last couple of years, and
  - Benefits for current retirees are paid from the retiree health care trust

Current Issues and Implications

- Implications
  - The 7.0% interest rate used in the calculations may no longer be appropriate (as defined by the GASB)
  - Lowering the interest rate will increase the liabilities and the Annual Required Contribution reported in the financial statements
  - May impact the County's ability to borrow

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Current Issues and Implications

- Implications
  - As of December 31, 2011, the liabilities for current retirees are 40% funded (i.e., for every $1 of retiree liability there is $0.40 in assets)
  - If no additional amounts are contributed to the trust and benefit payments for current retirees continue to be paid from the trust, the trust is expected to be depleted in roughly 5-6 years

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Current Issues and Implications

- Implications
  - Once the trust is depleted the retiree health care plan will be financed on a pay-as-you-go basis (i.e., no pre-funding, benefits are paid when due)
  - Pay-as-you-go benefits projected to exceed $12 million within about 20 years
  - As long as the plan is in place, liabilities continue to be reported on the employer's financial statements

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Recommended Steps for the County

- Continue pre-funding at the recommended level
- Continue to prepare annual actuarial valuations, because things can change significantly from one year to the next
- Monitor investment performance of the fund backing the promise
- Monitor whether the current retiree health benefits package is sustainable

What Others Have Done

- Some are pre-funding based on the full actuarial amount (this is the minority)
- Close the Defined Benefit retiree health plan to new hires and replace with a Defined Contribution Arrangement
  - Increases the Annual Required Contribution in the short term
  - Can be a long term savings if replacement plan is a cheaper plan

What Others Have Done

- Changes to the existing Defined Benefit health plan
  - Increase age and service requirement for receiving retiree health benefits
  - Reduce or eliminate spouse coverage
  - Introduce cost sharing features (i.e., retiree and/or spouse pay for a portion of the premium)
  - Cap on inflationary increases
  - Temporary benefit to Medicare eligibility
- Changes to the Underlying Medical Plan
  - Change in co-pays
  - Change in deductibles

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