Funding Basics of Retirement Programs

Monroe County Employee’s Retirement System

Monroe County Retiree Health Care Plan

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Agenda

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- Retirement System
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Agenda

- Retiree Health Plan
  - Highlights of the December 31, 2010 Valuation
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  - Possible Steps for the County
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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

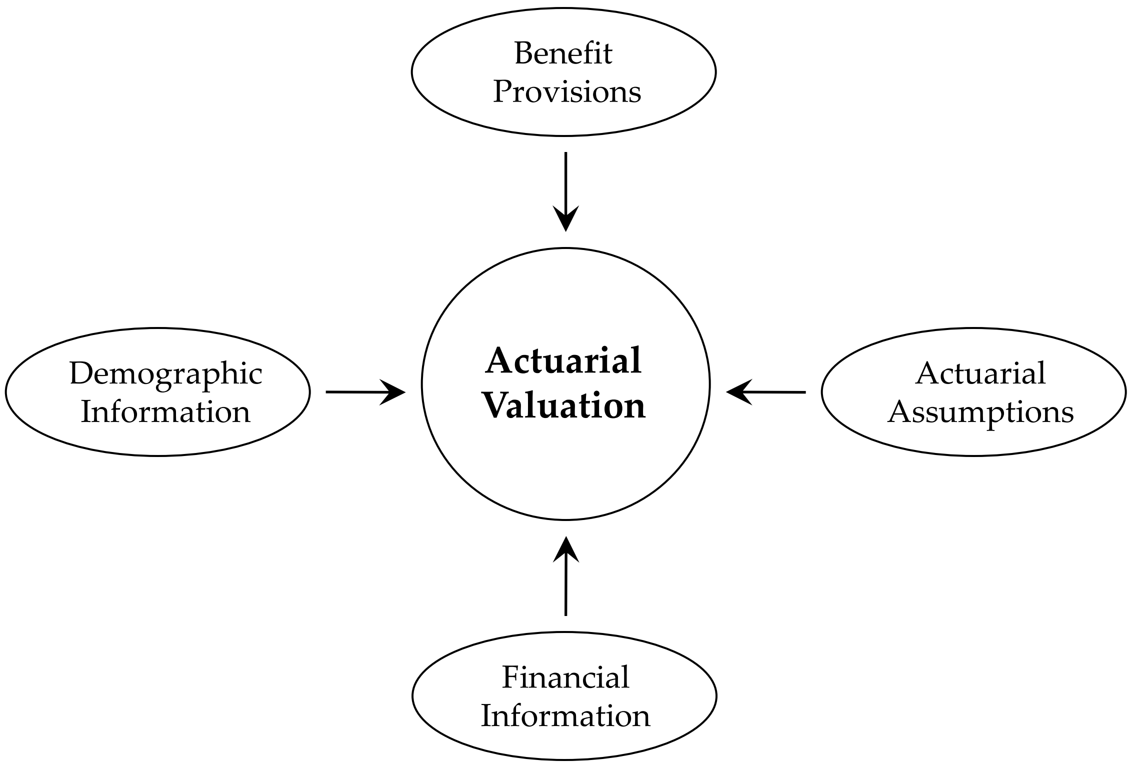
- What is the actuary's role?
  - Perform actuarial valuation to determine contributions such that the plan remains solvent
    - Contribution calculated by actuary is reasonable based on known past information and assumptions about future events
  - Estimate cost of proposed benefit changes
  - Be an 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

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.

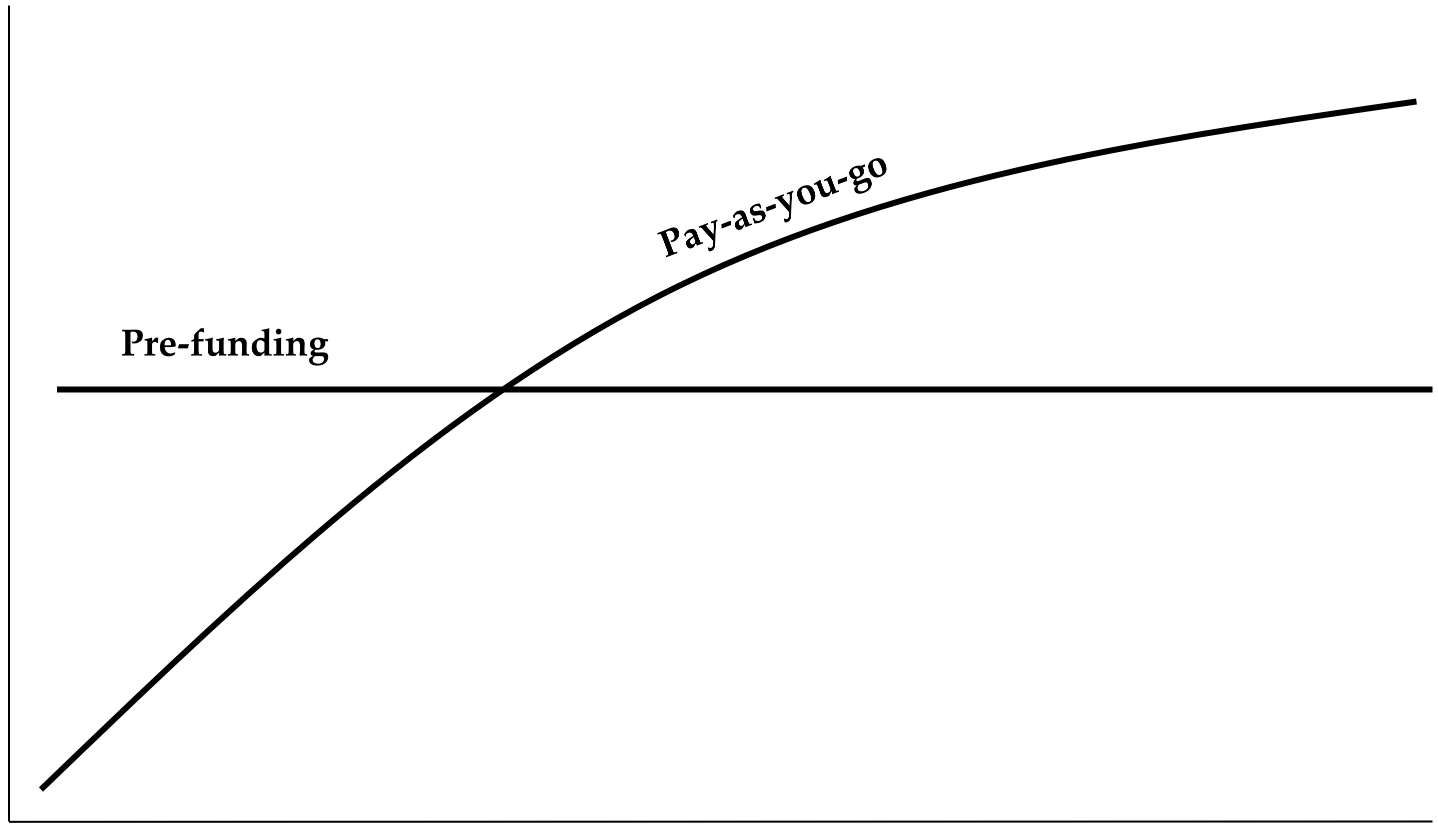
What is an Actuarial Valuation?

- 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



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

Pre-Funding & Accounting Basics

- Retirement System
  - State law requires pre-funding
  - Subject to GASB Statements No. 25 and 27
- Retiree Health Plan
  - There is no state or federal law that requires pre-funding
  - Subject to GASB Statements No. 43 and 45

Retirement System – Highlights of the December 31, 2010 Valuation

	Computed Contributions	
Division	Actual 12/31/2009	Actual 12/31/2010
General County	17.29 %	22.23 %
County Agency	17.39	32.33
Sheriff's Office	20.50	24.11
County Library	10.76	11.23
Road Commission	17.21	18.35
Mental Health	8.67	10.42
Central Dispatch	19.09	20.48

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Retirement System – Highlights of the December 31, 2010 Valuation

December 31, 2010	General County	County Agency	Sheriff's Office	County Library	Road Commission	Mental Health	Central Dispatch
Participants							
Actives	297	25	141	123	85	129	18
Retired	322	29	110	35	80	60	9
Terminated Vested	66	-	8	9	7	48	-
Total	685	54	259	167	172	237	27
Payroll	$12,873,997	$1,160,921	$8,327,582	$4,729,782	$4,280,204	$6,185,473	$860,176
Actuarial Accrued Liability	96,906,681	10,741,988	56,168,865	14,687,141	27,479,560	21,966,450	3,730,226
Actuarial Value of Assets	78,180,952	6,988,424	45,067,407	14,329,128	22,340,076	23,070,053	2,883,346
Unfunded Actuarial Accrued Liability	18,725,729	3,753,564	11,101,458	358,013	5,139,484	(1,103,603)	846,880
Funded Ratio	81%	65%	80%	98%	81%	105%	77%
Contribution Requirement							
Normal Cost	12.88%	11.55%	15.54%	10.74%	10.63%	12.43%	14.15%
Amortization Payment	9.35	20.78	8.57	0.49	7.72	-2.01	6.33
Total	22.23%	32.33%	24.11%	11.23%	18.35%	10.42%	20.48%
$ Contribution	$3,095,420	$405,952	$2,171,615	$574,497	$849,507	$697,120	$190,539
$ Contribution from 12/31/2009 Valuation	$2,780,443	$318,962	$2,192,433	$537,411	$848,408	$594,447	$191,496

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Retirement System – Highlights of the December 31, 2010 Valuation

- Employer contribution rates have increased for all divisions since the 2009 valuation as a result of:
  - Unfavorable investment performance working its way through the asset smoothing method
  - Early Retirement Incentive Program for certain divisions (General, County Agency, Sheriff, Central Dispatch)
  - Decrease in payroll

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Retirement System – Asset Performance

	December 31,					
	2005	**2006**	**2007**	**2008**	**2009**	**2010**
Market Value of Assets	$163,292,118	$177,532,251	$187,790,674	$148,763,118	$165,646,245	$176,702,630
Rate of Return	8.24%	11.36%	7.80%	(19.30)%	14.47%	9.65%
Actuarial Value of Assets	$163,151,579	$169,283,765	$181,320,182	$184,967,843	$188,779,278	$192,859,386
Rate of Return	3.30%	6.34%	9.24%	3.74%	4.46%	4.71%

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Retirement System – Looking Ahead

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

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Retirement System – Looking Ahead

- Retirement System
  - Continues to be well funded; funded ratio varies by group
  - Has assets equal to 15 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)

Retiree Health Plan - Highlights of the December 31, 2010 Valuation

	Computed Contributions	
	Actual	Actual
Division	12/31/2009	12/31/2010
General Billable	$1,044,781	$1,374,952
General Non-billable	2,678,405	3,557,282
County Agency	468,331	654,134
Sheriff Billable	647,703	959,000
Sheriff Non-billable	1,706,831	2,367,667
Dispatchers	206,662	174,371

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Retiree Health Plan - Highlights of the December 31, 2010 Valuation

	General County Billable	General County Non-Billable	County Agency	Sheriff's Office Billable	Sheriff's Office Non-Billable	Dispatchers	Combined
A. Accrued Liability							
1. For retirees and beneficiaries							
a. Health benefits	$10,806,907	$34,091,444	$5,718,329	$4,521,594	$20,430,171	$1,682,186	$77,250,631
b. Reserves	--	--	--	--	--	--	--
c. Totals	10,806,907	34,091,444	5,718,329	4,521,594	20,430,171	1,682,186	77,250,631
2. For vested terminated members	0	0	0	0	0	0	0
3. For present active members							
a. Value of expected future benefit payments	7,635,485	10,868,121	2,258,681	9,023,777	12,891,456	1,766,684	44,444,204
b. Value of future normal costs	1,809,728	2,640,052	712,152	3,587,094	4,956,410	789,637	14,495,073
c. Active member liability: (a) - (b)	5,825,757	8,228,069	1,546,529	5,436,683	7,935,046	977,047	29,949,131
4. Total	16,632,664	42,319,513	7,264,858	9,958,277	28,365,217	2,659,233	107,199,762
B. Valuation Assets	4,383,293	8,360,731	1,153,176	3,201,264	8,344,803	1,511,201	26,954,468
C. Unfunded Accrued Liability: (A.4) - (B)	12,249,371	33,958,782	6,111,682	6,757,013	20,020,414	1,148,032	80,245,294
D. Funded Ratio: (B) ÷ (A.4)	26.4%	19.8%	15.9%	32.1%	29.4%	56.8%	25.1%

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Retiree Health Plan - Highlights of the December 31, 2010 Valuation

- Contributions increased since the 2009 valuation as a result of:
  - Unfavorable investment performance from 2008 working through the asset smoothing method
  - Early Retirement Incentive Program offered to certain groups
  - All divisions, expect Dispatch received lower contributions than the recommended amounts
  - Based on information provided by the County, the Non-billable divisions received no employer contributions
  - Most of the Sheriff's division is closed to new hires; the financing method was changed to a method that is appropriate for a closed group

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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

Current Issues and Implications

- Implications
  - As of December 31, 2010, the liabilities for current retirees are 35% funded (i.e., for every $1 of retiree liability there is $0.35 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

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)
  - As long as the plan is in place, liabilities continue to be reported on the employer's financial statements

Current Issues and Implications

- If pre-funding does not continue at the recommended level or is completely eliminated:
  - The County will be faced with increasing costs (costs will be shifted to future taxpayers)
  - Benefits might have to be reduced or eliminated

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Comparing Various Retiree Health Plans

- Should consider both the liabilities and the assets when comparing plans
  - The liabilities indicate the value of the benefits that have been promised
  - The assets indicate the monies that have accumulated to back those benefits
  - Need to look at both when comparing plans (a plan that has more assets is not necessarily better off, if it also has higher liabilities)

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Comparing Various Retiree Health Plans

- Consider differences between the provisions of the underlying retiree health benefits (i.e., when do benefits begin, who is covered, is there any cost sharing, etc.)
- Consider the demographics of the groups covered (i.e., are there lots of retirees, is the plan open or closed to new hires, etc.)

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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