



# STAFF REPORT

## SAUSALITO CITY COUNCIL

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### AGENDA TITLE:

Actuarial Valuation of Postemployment Health Care Benefits (GASB 45)

### RECOMMENDED MOTION:

Accept and Approve the Actuarial Valuation of Postemployment Health Care Benefits (GASB 45) Report

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### SUMMARY

The City of Sausalito offers eligible permanent full-time employees who retire with the City medical and dental single coverage (dental for management employees only) for life. The City is required by the Governmental Accounting Standards Board Statement 45 (GASB 45), *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions (OPEB)*, to comply with GASB 45 in fiscal year 2008-09 and to disclose the unfunded retiree health care benefits cost as a liability on the Comprehensive Annual Financial Report (CAFR). The City selected Nicolay Consulting Group (Actuary) through the Request for Proposal process to prepare the actuarial study. Staff is recommending that the City Council accept and approve the actuarial valuation report prepared by the Actuary based on the valuation date of January 1, 2008.

### BACKGROUND

In July 2004, the Governmental Accounting Standards Board issued Statement 45 which requires governmental entities to begin accounting for the postemployment benefits on an accrual basis rather than the "pay-as-you-go" accounting method. The City of Sausalito currently offers permanent full-time employees who were members of the California Public Employees' Retirement System (CalPERS) through the City of Sausalito for twenty (20) or more years, and who were of the age of 50 for public safety employees (Fire and Police) and age 55 for nonpublic safety employees, the single rate monthly health insurance premium paid in full by the City until death. In addition to the medical benefits, management employees who previously retired plus three active management employees receive life time single dental coverage paid for by the City.

To comply with GASB 45, Nicolay Consulting Group prepared the actuarial study and determined that as of January 1, 2008, the City has an Unfunded Actuarial Accrued Liability (UAAL) of \$5,926,348. This actuarial determined liability is based on the "entry age normal" actuarial cost method, 30 year amortization of the UAAL (as a level percent of payroll), and a 5% discount rate.

## ISSUES

Just like the State of California and various governmental agencies that offer retiree health care benefits to eligible employees, the City of Sausalito is now faced with a huge UAAL and must come up with solutions and funding. Even though GASB 45 does not require funding of the UAAL, it does require that if an employer fails to fund the Annual Required Contribution (ARC) as determined by the Actuary to book the unfunded ARC as a net OPEB Obligation (liability) in the CAFR. The ARC as determined by the Actuary is \$571,637 per year until another study is performed, with funding to start in fiscal year 2008-09. GASB 45 requires the actuarial valuation report to be updated every three years for the City of Sausalito.

There are several funding approaches to pay off the UAAL including "pay as you go", level dollar 20 years, level dollar 30 years, level percent of payroll 20 years, and level percent of payroll 30 years. The level dollar 20 years and 30 years' options are more expensive at the beginning of funding years. Staff recommends that the City adopt the level percent of payroll 30 years for budgeting purposes. The level percent of payroll 30 years is consistent with the CalPERS retirement funding. Due to the budget constraint, the City of Sausalito for years has been using the "pay-as-you-go" to fund its OPEB. The pay-as-you-go funding for fiscal year 2007-08 is budgeted at \$122,123. To lessen the UAAL of \$5,926,348, the City has set aside \$50,000 in fiscal year 2004-05, \$150,000 in fiscal year 2006-07, and \$150,000 in fiscal year 2007-08.

In order for the set aside fund of \$350,000 to help reduce the UAAL, the City must place the \$350,000 set aside fund in an irrevocable trust. Currently, the Finance Committee is recommending that the City manage the fund without a trust. By not placing the fund in a trust, the Actuary is required by GASB 45 to ignore the asset set aside in the calculation of UAAL. Without the credit of asset set aside and full funding for ARC, the UAAL will grow significantly over the future years. If the City stops funding for ARC and use the "pay-as-you-go" funding method, the UAAL in fiscal year 2012-13 is projected to be \$7,959,133, an increase of over \$2,000,000. The current projected UAAL of \$5,926,348 is 48% of the fiscal year 2007-08 General Fund operating expenditure budget.

Staff is seeking City Council direction on the issue of how to handle the set aside fund. There are several options available including continuing City management of the fund, place the fund in the CalPERS 115 trust or with other investment companies that are set up for GASB 45 management.

In order for the City to maintain its fiscal health and fiduciary responsibilities to the employees and the community, it is important that the City and all employees groups work together to find solutions.

Several options are available and have been adopted by cities to help resolve this crisis. Options include a two-tier benefits system for future new hires, a dollar cap on benefits, converting the current defined benefits plan into a defined contribution plan. The defined contribution plan allows the employer or employer and employees to contribute into a retirement health saving plan, which provides an avenue for employees that may not be eligible for employer retiree health care benefits to use pre-tax earnings to fund future medical benefits upon retirement. Implementation of any of these options will require that the City meet and confer with all bargaining groups. Staff is seeking City Council direction on how to best address the solutions to the UAAL. It is one of the City's strategic goals to attract and retain qualified and talented staff. The retiree health care cost is a very difficult issue and needs special attention.

## **FISCAL IMPACT**

Based on the pay-as-you-go funding, the City budgeted \$122,123 in fiscal year 2007-08 to pay the actual premiums for retiree medical and dental benefits. With the ARC of \$571,637, the City will need to set aside an additional \$450,000 a year.

## **STAFF RECOMMENDATIONS**

Staff and the Finance Committee recommend that the City Council accept and approve the actuarial valuation of postemployment health care benefits report.

## **ATTACHMENTS**

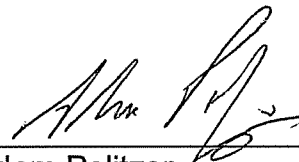
Draft Actuarial Valuation of Postemployment Health Care Benefits Report  
Funding Approach Schedule

PREPARED AND SUBMITTED BY:



Louise Ho  
Finance Director/Treasurer

APPROVED BY:



Adam Politzer  
City Manager

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Item #: 6B  
Meeting Date: 4-22-08  
Page No. 3

**ATTACHMENT NO. 1**

**CITY OF SAUSALITO**

**Actuarial Valuation of  
Postemployment Health Care Benefits  
Valuation Date: January 1, 2008**

**Item #:** 6B  
**Meeting Date:** 4-22-08  
**Page No.** 4

February 22, 2008

Ms. Louise Ho  
Finance Director/Treasurer  
City of Sausalito  
420 Litho Street  
Sausalito, CA 94965

Dear Ms. Ho:

**Re: Actuarial Valuation of Postemployment Medical Program**

The Nicolay Consulting Group is pleased to present the results of our January 1, 2008 actuarial valuation of the City of Sausalito postemployment health care program. In preparing this report, we relied on employee data and plan information provided by the City. On the basis of that information, this report has been prepared in accordance with generally accepted actuarial principles and methods. It is our opinion that the actuarial assumptions used are reasonably related to the actual experience of the plan and to anticipated future experience.

The financial projections presented in this report are intended for the City's internal use in evaluating the potential cost of the retiree medical program. Because future events frequently do not occur as expected, it should be recognized that there are usually differences between anticipated and actual results. These differences may be material, especially if there are significant changes in the employee or retiree population. Consequently, we can express no assurance that the projected values will occur. We recommend that the City obtain an updated actuarial valuation every two years.

We, the undersigned, meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Questions about the report should be directed to Doug Tokerud at (800) 998-7675 x220.

Sincerely,

Nicolay Consulting Group

By: \_\_\_\_\_  
Douglas Tokerud, F.S.A.  
Member, American Academy of Actuaries

By: \_\_\_\_\_  
Dennis Daugherty, F.S.A.  
Member, American Academy of Actuaries

Item #: 6B  
Meeting Date: 4-22-08  
Page No. 5

# CITY OF SAUSALITO

## Actuarial Valuation of Postemployment health Care Benefits

### Table of Contents

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SECTION	TITLE	PAGE
SECTION I	Introduction	1
SECTION II	Valuation Results	2
SECTION III	Plan Description and Demographic Summary	9
SECTION IV	Actuarial Method and Assumptions	12
SECTION V	Glossary	22

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*Valuation Date: January 1, 2008*

Item #: 6B  
Meeting Date: 4-22-08  
Page No. 6

# SECTION I

## Introduction

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The City of Sausalito provides postemployment medical benefits to certain retirees who satisfy plan eligibility requirements. This report provides a July 1, 2008 estimate of the present value of the City's postemployment medical benefits attributable to past service, illustrations of the impact of GASB 45 accounting requirements and a ten-year projection of the pay-as-you-go cost of providing the benefits. **Section II** contains valuation results. **Section III** describes the plan and presents a demographic summary. **Section IV** describes the actuarial assumptions used to complete the valuation. **Section V** is a Glossary of several of the terms used in this report.

### Accounting Requirements

In July 2004 the Governmental Accounting Standards Board issued **Statement 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions**. This statement requires governmental entities to begin accounting for postemployment benefits on an accrual basis rather than the more common pay-as-you-go accounting. Each employee's benefit will "accrue" throughout their working lifetime and employers will be required to show the annual accruals as a current year expense.

Employers must adopt Statement 45 no later than the plan year that begins after December 15, 2006, 2007 or 2008 depending on the annual revenues of the entity. We understand the City of Sausalito will adopt Statement 45 during the 2008/09 fiscal year.

## SECTION II

### Valuation Results

Table 2-1 contains estimates of the present value of the cost of postemployment medical and dental benefits for current retirees and employees who are expected to receive the benefit. The estimates in Table 2-1 are based on a 5.0% discount rate. The valuation date was January 1, 2008. The results were then "rolled forward" (slight upward adjustment) to July 1, 2008 in order to coincide with the City's fiscal year.

Tables 2-3 and 2-4a and 2-4b are based on the "entry age normal" actuarial cost method, and on 30 year amortization of the actuarial accrued liability (as a level percent of payroll.) Table 2-4a shows 5 years of estimated costs assuming continuation of "pay-as-you-go." Table 2-4b assumes full annual ARC funding to a trust. In Table 2-5, for comparison, we show the actuarial accrued liability and first year estimated cost under several alternative approaches.

Table 2-1					
Present Value of Future Postemployment Health Benefits Attributable to Past Service					
As of July 1, 2008					
Entry Age Normal Actuarial Cost Method					
Discount Rate: 5.0%					
	Fire	Police	SEIU	Unrepresented Employees	Total
Actives	\$1,607,677	\$691,405	\$503,153	\$840,408	\$3,642,643
Retirees and Spouses	<u>\$350,328</u>	<u>\$606,404</u>	<u>\$345,277</u>	<u>\$981,696</u>	<u>\$2,283,705</u>
Actuarial Accrued Liability	\$1,958,005	\$1,297,809	\$848,430	\$1,822,104*	\$5,926,348
Actuarial Value of Assets					\$0
Unfunded Actuarial Accrued Liability					<u>\$5,926,348</u>
Annual Level Percent of Payroll Amortization of Unfunded AAL					\$261,880
Normal Cost (based on Entry Age Normal Cost Method)					<u>\$309,757</u>
Annual Required Contribution (ARC)					<u>\$571,637</u>
<i>*Includes dental of \$107,076</i>					

Comment: As discussed later in this report, we have assumed that the CalPERS medical plan is what is known as a "community rated" plan under GASB 45. This view is held by CalPERS and is, we believe, widely supported at present. In the



event the accounting and/or actuarial professions, or CalPERS, should change this position in the future, or if CalPERS changes how it determines premium rates to more of an age based method, the estimated liabilities and costs would increase.

## Projected Health Benefit Costs

Table 2-2 contains a ten-year projection of the City's pay-as-you-go cost to provide postemployment benefits to current and future retirees.

Table 2-2 Projected Future Annual pay-as-you-go Plan Cost of Postemployment Medical Benefits	
<u>Year</u>	<u>Estimated City Cost</u>
2008/09	\$134,885
2009/10	\$147,460
2010/11	\$159,823
2011/12	\$175,818
2012/13	\$192,648
2013/14	\$209,035
2014/15	\$227,523
2015/16	\$248,927
2016/17	\$270,050
2017/18	\$291,126

## Illustrative Health Benefit Costs Under GASB 45

The first year Annual Required Contribution (ARC) consists of the Normal Cost plus the current period amortization of the Unfunded Actuarial Accrued Liability.

Normal Cost is the portion of the actuarial present value of future benefits that is allocated to a particular year. Another interpretation is that the Normal Cost is the present value of future benefits that are "earned" by employees for service rendered during the current year. This valuation is based on the Entry Age Normal actuarial cost method and an attribution period that runs from date of hire until the expected retirement date.

In the year the new accounting rules become effective an employer is allowed to commence amortization of the Unfunded Actuarial Accrued Liability, over a period not to exceed 30 years. The following Tables are based on a level percent of projected

payroll amortization over a closed 30-year period. Note: Statement 45 also allows amortization using a level dollar method.

Table 2-3 presents the City's 2008/09 GASB 45 ARC. For this illustration we assumed that the City has not pre-funded any portion of the obligation.

Table 2-3	
Development of Illustrative Fiscal Year 2008/09 OPEB Annual Required Contribution – based on a 5.0% discount rate	
Actuarial Accrued Liability	\$5,926,348
Actuarial Value of Assets	<u>          \$0</u>
Unfunded Actuarial Accrued Liability	\$5,926,348
Illustrative Amortization Period	30 years
Level percent of pay Amortization Factor (based on a 5.0% discount rate and a 3.25% annual increase in payroll)	22.630
Annual Level Percentage of Pay Amort. of Unfunded AAL	\$261,880
Normal Cost (based on the Entry Age Normal Method)	<u>\$309,757</u>
Annual Required Contribution	\$571,637

Table 2-4a presents a five-year projection under the assumptions that the City continues to contribute the pay-as-you-go cost, the discount rate remains 5.0% and the Normal Cost component of the ARC increases by 5.0% per year.

		Table 2-4a City of Sausalito				
		Five-year Projection of Annual OPEB Cost and Net OPEB Obligation				
		Based on the Entry Age Normal Actuarial Cost Method, a 5.0% discount rate and assuming pay-as-you-go funding				
		2008/09	2009/10	2010/11	2011/12	2012/13
Actuarial Accrued Liability (AAL)		\$5,926,348	\$6,394,206	\$6,888,060	\$7,410,200	\$7,959,133
Actuarial Value of Assets at beginning of year		\$0	\$0	\$0	\$0	\$0
Unfunded Actuarial Accrued Liability (UAAL)		\$5,926,348	\$6,394,206	\$6,888,060	\$7,410,200	\$7,959,133
Remaining Amortization Period		30	29	28	27	26
Normal Cost		\$309,757	\$325,245	\$341,507	\$358,582	\$376,512
Amortization of UAAL		\$261,880	\$290,052	\$321,122	\$355,491	\$393,432
Annual Required Contribution (ARC)		\$571,637	\$615,297	\$662,629	\$714,073	\$769,944
Annual Required Contribution (ARC)		\$571,637	\$615,297	\$662,629	\$714,073	\$769,944
Interest on net OPEB Obligation		\$0	\$21,838	\$45,331	\$70,624	\$97,680
Adjustment to ARC		\$0	(\$19,812)	(\$42,266)	(\$67,761)	(\$96,570)
Annual OPEB Cost		\$571,637	\$617,323	\$665,694	\$716,936	\$771,054
City Contributions		(\$134,885)	(\$147,460)	(\$159,823)	(\$175,818)	(\$192,648)
Increase in net OPEB Obligation		\$436,752	\$469,863	\$505,871	\$541,118	\$578,406
Net OPEB Obligation - Beginning of Year		\$0	\$436,752	\$906,615	\$1,412,486	\$1,953,604
Net OPEB Obligation - End of Year		\$436,752	\$906,615	\$1,412,486	\$1,953,604	\$2,532,010

Note: the ARC adjustment is calculated by dividing the beginning of year net OPEB obligation by the same amortization factor used to amortize the Unfunded Actuarial Accrued Liability.

Table 2-4b presents a five-year projection under the assumptions that the City contributes the full Annual Required Contribution to a Trust, the Trust Fund earns 5.0% per year, the discount rate remains 5.0% and the Normal Cost component of the ARC increases 5% per year throughout the five year period. We assumed mid-year additions to and subtractions from the Trust.

Table 2-4b City of Camarillo					
Five-year Projection of Annual OPEB Cost and Net OPEB Obligation					
Based on a 5.0% discount rate and assuming full ARC funding					
	2008/09	2009/10	2010/11	2011/12	2012/13
Actuarial Accrued Liability (AAL)	\$5,926,348	\$6,394,206	\$6,888,060	\$7,410,200	\$7,959,133
Actuarial Value of Assets at beginning of year	\$0	\$447,671	\$928,773	\$1,446,205	\$1,999,113
Unfunded Actuarial Accrued Liability (UAAL)	\$5,926,348	\$5,946,535	\$5,959,287	\$5,963,995	\$5,960,020
Remaining Amortization Period	30	29	28	27	26
Normal Cost	\$309,757	\$325,245	\$341,507	\$358,582	\$376,512
Amortization of UAAL	\$261,880	\$269,745	\$277,822	\$286,112	\$294,613
Annual Required Contribution (ARC)	\$571,637	\$594,990	\$619,329	\$644,694	\$671,125
Annual Required Contribution (ARC)	\$571,637	\$594,990	\$619,329	\$644,694	\$671,125
Interest on net OPEB Obligation	\$0	\$0	\$0	\$0	\$0
Adjustment to ARC	\$0	\$0	\$0	\$0	\$0
Annual OPEB Cost	\$571,637	\$594,990	\$619,329	\$644,694	\$671,125
Contributions to the Trust	(\$571,637)	(\$594,990)	(\$619,329)	(\$644,694)	(\$671,125)
Increase in net OPEB Obligation	\$0	\$0	\$0	\$0	\$0
Net OPEB Obligation - Beginning of Year	\$0	\$0	\$0	\$0	\$0
Net OPEB Obligation - End of Year	\$0	\$0	\$0	\$0	\$0
Projected pay-as-you-go cost	\$134,885	\$147,460	\$159,823	\$175,818	\$192,648

Table 2-5

**Annual Cost for Fiscal Year Beginning July 1, 2008  
Under Alternative Actuarial and Amortization Methods**

	<u>Actuarial Accrued Liability (prior service)</u>	<u>Prior Service Amortization</u>	<u>Normal Cost</u>	<u>Total Cost Fiscal yr. Beg July 1, 2008</u>
1. <b>Baseline valuation</b> shown in this report (Entry Age Normal method, 30 year amortization of prior service liability as level percentage of payroll)	\$5,926,348	\$261,880	\$309,757	\$571,637
<b>Alternatives:</b>				
2. Same as 1 but <b>20</b> year amortization	\$5,926,348	\$363,288	\$309,757	\$673,045
3. Same as 1 but 30 year <b>level dollar</b> amortization	\$5,926,348	\$385,517	\$309,757	\$695,274
4. <b>Project Unit Credit method</b> , 30 year amortization of prior service liability as level percentage of payroll	\$5,327,618	\$235,426	\$287,354	\$522,780
5. Same as 4 but <b>20</b> year amortization	\$5,327,618	\$326,586	\$287,354	\$613,940
6. Same as 4 but 30 year <b>level dollar</b> amortization	\$5,327,618	\$346,569	\$287,354	\$633,923

Item #: 6B  
 Meeting Date: 4-22-08  
 Page No. 14

## SECTION III

### Plan Description and Demographic Summary

#### **Eligibility and Contribution Requirements**

We valued separately four employee groups: police, fire, SEIU Local 1021 and unrepresented employees. Fire employees and retirees are covered under a Marin County medical plan. The other groups are covered under the CalPERS medical program.

The three groups covered under CalPERS who retire at age 50 or over with at least 5 years of service receive benefits at least equal to the CalPERS minimum, which is equal to \$97 per month in 2008.

In addition, employees who retire after 20 years of service at or after age 50 for police and fire, and at or after age 55 for other employees, receive total medical benefits up to the Kaiser single retiree premium (including the CalPERS minimum if applicable.)

Spouses of retirees can also be covered, but the retiree is required to pay the spousal premiums. However, upon the death of a retiree covered under CalPERS, a surviving spouse continues to receive the CalPERS minimum benefit at no cost.

The City also pays/will pay for dental benefits for certain unrepresented retirees, and for three current active management employees after retirement. No other future retirees will receive City paid dental benefits.

### Medical Plan Options

Eligible retirees may enroll in any of the available CalPERS medical plans or in the case of Fire retirees, any of the available Marin County plans.

### Duration of Benefits

City provided benefits continue for the life of the retiree and surviving spouse.

### Demographic Data

Tables 3-1 and 3-2 contain summaries of the demographic information provided by the City.

Table 3-1							
Age and Service Table of Active Employees included in the valuation as of January 1, 2008							
Age	Years of Service						Total
	<5	5-9	10-14	15-19	20-24	25+	
Under 25	3	0	0	0	0	0	3
25-29	7	2	0	0	0	0	9
30-34	3	2	1	0	0	0	6
35-39	5	4	4	2	0	0	15
40-44	6	2	1	2	0	0	11
45-49	4	0	0	0	2	0	6
50-54	4	4	1	0	1	3	13
55-59	0	1	1	1	0	3	6
60-64	0	2	0	0	1	0	3
65-69	0	0	0	1	0	0	1
70+	0	1	0	0	0	0	1
<b>Total</b>	<b>32</b>	<b>18</b>	<b>8</b>	<b>6</b>	<b>4</b>	<b>6</b>	<b>74</b>



Table 3-2

**Age Table for  
Retirees and Surviving Spouses Receiving Benefits  
as of January 1, 2008**

<u>Age</u>	<u>Male</u>	<u>Female</u>	<u>Total</u>
Under 50	1	0	1
50-54	2	2	4
55-59	3	1	4
60-64	5	0	5
65-69	5	2	7
70-74	1	0	1
75-79	2	2	4
80-84	0	1	1
85+	<u>0</u>	<u>2</u>	<u>2</u>
<b>Total</b>	<b>19</b>	<b>10</b>	<b>29</b>

## SECTION IV

### Actuarial Method and Assumptions

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In order to project the City's liabilities into the future, a number of economic, demographic, and baseline cost assumptions are necessary. We used the same demographic actuarial assumptions as those used in the most recent California PERS pension valuations.

#### Valuation Date

The valuation date is January 1, 2008. This date is the starting point from which current costs are increased according to the assumed annual rates of health care cost trend. The City census is projected from the valuation date to the anticipated date of the final benefit payment for each employee and retiree on the census. After calculating future costs for the projected retiree and dependent population, all liabilities are discounted back to the valuation date to obtain the present value of future costs. As mentioned earlier, our valuation results were then rolled forward to July 1, 2008, the effective date of GASB 45 for the City of Sausalito.

#### Economic Assumptions

##### Discount Rate

A discount rate is required to calculate the present value of future benefit payments which are used to determine financial statement expense. We used a 5.0% discount rate for this valuation. We assumed that this rate is representative of the long term rate of return the City could expect to achieve on funds used to pay its postemployment healthcare obligation.

##### Baseline Cost

Estimates of retiree health benefit obligations are normally based on current costs for a one year period. We refer to this as the *baseline cost*. The components of baseline cost, such as average per capita cost, and the current plan population are projected into the future to estimate the cost of future benefits.

The large majority of City employees and retirees have elected Kaiser medical coverage. Also, the City paid benefits of all future retirees will be capped at Kaiser rates. Therefore, we have assumed that all future retirees will elect Kaiser coverage. For current retirees receiving a more expensive City paid coverage, we have included in our calculations such more expensive benefits.

Kaiser medical premiums for 2008 are shown in Table 4-1 below.

	Before Age 65		After Age 65	
	<u>Single</u>	<u>Married</u>	<u>Single</u>	<u>Married</u>
Fire	\$475.04	\$950.08	\$371.41	\$742.82
Other (CALPERS Bay Area)	470.67	941.34	273.36	546.72

For the few individuals who are receiving, or may receive in the future, City paid retiree dental coverage, we assumed the rate of \$40.82 per month for 2008, and that future dental premiums will increase 5% per year.

CalPERS has indicated that its medical program is a “community rated” plan as described in GASB 45. This means that all participating employers located in the same geographical region pay the same premium rates even though older employees and early retirees generally have higher medical costs than younger employees. If CalPERS changes its present practice and at a future date decides to modify the premium structure so that it charges more on average for non-Medicare retirees than for active employees, then higher costs would need to be allocated to retirees, and this could result in a substantial increase in the City’s Actuarial Accrued Liability and Annual Required Contribution. Please also see the related comment on page 2.

For the Fire retirees, we have *not* treated the medical plan as community rated, since it is a local (Marin County) plan. GASB 45 requires that, for plans which are not community rated, medical premium rates need to be “age graded” in order to reflect the fact that younger people have lower medical costs than older people. We used the following age graded premium rates to value the fire group, based on our own database and on a 2003 study sponsored by the Society of Actuaries.

Table 4-2

Rate charged for Employees and Retirees under Age 65	<u>Monthly</u> \$475.04
Corresponding Age Graded Rates	
<u>Age</u>	
25	\$270.08
35	\$389.50
45	\$537.83
55	\$738.67
60	\$881.58
64	\$1,039.25
65 and over*	\$371.41

\*Since a separate rate is charged for retirees 65 and older (\$371.41) and there is much less cost variance after that age, the \$371.41 amount was used at ages 65 and over.

### Contributions

Retirees are responsible for any premium costs in excess of the City's contribution.

### Health Care Trend

The rate of increase in per capita health care costs is commonly referred to as the *health care trend* rate. Although the term "health care inflation" is sometimes used synonymously with the trend rate, health care inflation is only one of several components of the trend rate. The analysis recognizes the following influences on health care trend: pure medical inflation, utilization changes, technological changes, regulatory requirements, Medicare cost shifting, and aging.

We assumed the following annual rates of increase in Kaiser medical premiums.

<u>the Plan Year Beginning</u>	<u>Estimated Increase</u>
January 1, 2009	8.5%
January 1, 2010	8.2%
January 1, 2011	7.9%
January 1, 2012	7.6%
January 1, 2013	7.3%
January 1, 2014	7.0%
January 1, 2015	6.7%
January 1, 2016	6.4%
January 1, 2017	6.1%
January 1, 2018	5.8%
January 1, 2019 and thereafter	5.5%

We assumed the CalPERS minimum benefit (\$97 for 2008) will increase 5% per year.

### **Payroll Increases**

In this valuation we assumed a 3.25% annual rate of increase in City payroll. This rate is a component of the Entry Age Normal Actuarial Cost Method and is used in the calculation of the amortization component of the Annual Required Contribution and in calculation of the Normal Cost.

### **Amortization Methodology**

GASB 45 allows amortization of the Unfunded Actuarial Accrued Liability based on a level dollar approach or as a level percentage of covered payroll. The maximum amortization period is 30 years. This valuation is based on a closed, 30-year amortization of the Unfunded Actuarial Accrued Liability as a level percentage of payroll; increasing each year as the payroll increases.

### **Plan Assets**

We understand that as of January 1, 2008, no portion of this obligation had been prefunded.

## Demographic Assumptions

In estimating this obligation, a number of demographic assumptions are needed. These assumptions are the same as those used in the most recent California PERS valuation.

## Withdrawal

For the Fire and Police valuations we used the same withdrawal rates as those used in the most recent California PERS Fire and Police retirement plan valuations. Selected rates are shown below.

Completed Years of Service	Fire	Police
0	0.09470	0.12990
1	0.07390	0.08160
2	0.05310	0.03480
3	0.03230	0.03310
4	0.02900	0.03140
5	0.02570	0.02970
6	0.02230	0.02810
7	0.01890	0.02630
8	0.01560	0.02470
9	0.01230	0.02300
10	0.00900	0.02130
15	0.00790	0.01290
20	0.00690	0.00970
25	0.00570	0.00820
30	0.00540	0.00760
35	0.00090	0.00120

For all other City employees we used withdrawal rates that match those used in the most recent California PERS Public Agency Miscellaneous retirement plan valuations. Sample rates are shown below.

Table 4-5  
Annual Withdrawal Rates

<u>Service</u>	----- Entry Age -----						
	20	25	30	35	40	45	50
0	0.17600	0.16910	0.16220	0.15525	0.14830	0.14140	0.13450
1	0.15610	0.14920	0.14230	0.13535	0.12840	0.12150	0.11460
2	0.13620	0.12930	0.12240	0.11545	0.10850	0.10160	0.09470
3	0.11630	0.10940	0.10250	0.09555	0.08860	0.08170	0.07480
4	0.09640	0.08950	0.08260	0.07565	0.06870	0.06180	0.05490
5	0.07650	0.06965	0.06270	0.05575	0.04880	0.03085	0.01290
6	0.07270	0.06580	0.05880	0.05190	0.04500	0.02810	0.01120
7	0.06890	0.06190	0.05500	0.04815	0.04110	0.02535	0.00960
8	0.06500	0.05805	0.05120	0.04425	0.03730	0.02265	0.00800
9	0.06120	0.05430	0.04730	0.04040	0.03350	0.02000	0.00650
10	0.05740	0.05045	0.04350	0.03660	0.00950	0.00730	0.00510
15	0.04460	0.03755	0.03070	0.00645	0.00460	0.00270	0.00080
20	0.03180	0.02490	0.00410	0.00250	0.00090	0.00055	0.00020
25	0.01900	0.00215	0.00090	0.00055	0.00020	0.00020	0.00020
30	0.00100	0.00060	0.00020	0.00020	0.00020	0.00020	0.00020
35	0.00020	0.00020	0.00020	0.00020	0.00020	0.00010	0.00000

**Retirement Rates**

For Fire employees we used the same retirement rates as those used in the most recent California PERS 3% @55 Firefighter retirement plan valuation. Sample rates are shown below.

Table 4-6  
Fire  
Annual Rates of Retirement

Age	----- Years of Service -----						
	5	10	15	20	25	30	35
50	0.00240	0.00240	0.00240	0.00350	0.00550	0.00650	0.00650
51	0.00480	0.00480	0.00480	0.00700	0.01100	0.01280	0.01280
52	0.01470	0.01470	0.01470	0.02150	0.03390	0.03960	0.03960
53	0.04250	0.04250	0.04250	0.06210	0.09790	0.11420	0.11420
54	0.05670	0.05670	0.05670	0.08280	0.13060	0.15230	0.15230
55	0.09150	0.09150	0.09150	0.13370	0.21090	0.24590	0.24590
56	0.08110	0.08110	0.08110	0.11840	0.18680	0.21780	0.21780
57	0.09960	0.09960	0.09960	0.14550	0.22950	0.26760	0.26760
58	0.08140	0.08140	0.08140	0.11890	0.18740	0.21850	0.21850
59	0.07750	0.07750	0.07750	0.11310	0.17840	0.20800	0.20800
60	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000

For Police employees we used the same retirement rates as those used in the most recent California PERS 3% @55 Police retirement plan valuation. Sample rates are shown below.

Table 4-7  
Police  
Annual Rates of Retirement

Age	----- Years of Service -----						
	5	10	15	20	25	30	35
50	0.01930	0.01930	0.01930	0.01930	0.03970	0.06000	0.06000
51	0.01570	0.01570	0.01570	0.01570	0.03240	0.04900	0.04900
52	0.01630	0.01630	0.01630	0.01630	0.03370	0.05100	0.05100
53	0.05870	0.05870	0.05870	0.05870	0.12080	0.18290	0.18290
54	0.06910	0.06910	0.06910	0.06910	0.14220	0.21540	0.21540
55	0.11640	0.11640	0.11640	0.11640	0.23970	0.36300	0.36300
56	0.07560	0.07560	0.07560	0.07560	0.15560	0.23570	0.23570
57	0.05810	0.05810	0.05810	0.05810	0.11960	0.18120	0.18120
58	0.05080	0.05080	0.05080	0.05080	0.10450	0.15830	0.15830
59	0.06250	0.06250	0.06250	0.06250	0.12870	0.19490	0.19490
60	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000



For all other City employees we used the retirement rates that were be used in the most recent California PERS 2.5% @55 Miscellaneous employees retirement plan valuation. Selected rates are shown below.

**Table 4-8  
Annual Rates of Retirement**

<b>Age</b>	<b>Male</b>	<b>Female</b>
50	0.05	0.07
55	0.08	0.09
60	0.16	0.12
61	0.15	0.10
62	0.26	0.21
63	0.22	0.18
64	0.15	0.13
65	0.25	0.25
67	0.12	0.14
70	1.00	1.00

## Mortality

The mortality rates used in this valuation are the rates used in the most recent California PERS retirement plan valuation. Annual mortality rates for selected ages are shown below.

Table 4-9  
Sample Mortality Rates

<u>Age</u>	<u>Active Employees</u>		<u>Retired Employees</u>	
	<u>Male</u>	<u>Female</u>	<u>Male</u>	<u>Female</u>
55	0.248%	0.178%	0.429%	0.253%
60	0.344%	0.256%	0.721%	0.442%
65	0.480%	0.369%	1.302%	0.795%
70	0.671%	0.537%	2.135%	1.276%
75			3.716%	2.156%
80			6.256%	3.883%
85			10.195%	7.219%
90			17.379%	12.592%

## Disability Retirement

Sample disability rates for Fire and Police employees are shown in Table 4-9. These rates match those used in the most recent California PERS pension valuations.

Because of the low incidence of disability retirements for non-Safety employees we did not value disability retirement for non-Safety employees.

Table 4-9  
Annual Rates of Disability

<u>Age</u>	<u>Fire</u>	<u>Police</u>
25	0.21%	0.56%
30	0.21%	0.56%
35	0.41%	1.12%
40	0.41%	1.12%
45	0.62%	1.67%
50	0.62%	1.67%
55	6.00%	5.81%

## Health Plan Participation

We assumed that 100% of future eligible retirees will enroll in one of the offered medical plans and that 70% of future retirees will enroll a spouse.

## Medicare Coverage

We assumed that all retirees will be eligible for Medicare when they reach age 65.

# SECTION V

## Glossary

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- Accrual Accounting – A method of matching the cost of an employee’s service, including long term obligations such as OPEB, to that employee’s period of active service.
- Actuarial Accrued Liability (AAL) – The Actuarial Present Value of all postemployment benefits attributable to past service. Note: the AAL is sometimes referred to as the Past Service Liability.
- Actuarial Cost Method – A procedure for allocating the actuarial present value of benefits and expenses and for developing an actuarially equivalent allocation of such value to time periods, usually in the form of a Normal Cost and an Actuarial Accrued Liability.
- Actuarial Present Value – The value of an amount or series of amounts payable or receivable at various times. Each such amount or series of amounts is:
  - a. adjusted for the probable financial effect of certain intervening events (such as changes in healthcare costs, compensation levels, Medicare, marital status, etc.)
  - b. multiplied by the probability of the occurrence of an event (such as survival, death, disability, termination of employment, etc.) on which the payment is conditioned, and
  - c. discounted according to an assumed rate (or rates) of return to reflect the time value of money
- Actuarial Valuation – The determination, as of a valuation date, of the Normal Cost, Actuarial Accrued Liability, Actuarial Value of Assets and related Actuarial Present Values.

- Actuarial Value of Assets – The value of cash, investments and other property belonging to a plan. These are amounts that may be applied to fund the Actuarial Accrued Liability. Note: assets must be segregated and placed in a Trust in order to be considered OPEB assets
- Amortization Payment – That portion of the Annual OPEB cost which is designed to pay interest on and to amortize the Unfunded Actuarial Accrued Liability.

In the year that Statement 45 becomes effective an employer is allowed to commence amortization of the Unfunded Actuarial Accrued Liability, over a period not to exceed 30 years.

- Annual Other Postemployment Benefit (OPEB) Cost - An accrual-basis measure of the periodic cost of an employer's participation in a defined benefit OPEB plan. The annual OPEB cost is the amount that must be calculated and reported as an expense.

When an employer has no net OPEB obligation (e.g., in the year of implementation) the annual OPEB cost is equal to the Annual Required Contribution (ARC).

In subsequent years the Annual OPEB cost will include:

- the ARC (equal to the Normal Cost plus one year's amortization of the Unfunded Actuarial Accrued Liability);
- one year's interest on the net OPEB obligation at the beginning of the year using the valuation discount rate; and
- an adjustment to the ARC. This adjustment is intended to provide a reasonable approximation of that portion of the ARC that consists of interest associated with past contribution deficiencies. GASB Statement No. 45 specifies that this adjustment should be equal to an amortization of the discounted present value of the net OPEB obligation at the beginning of the year. The amortization should be calculated using the same amortization method and period used in determining the ARC for that year. If the net OPEB obligation is positive the adjustment should be deducted from the ARC.
- Note: As long as the net OPEB obligation is zero, there will not be any interest charge or adjustment to the ARC. However, if an employer does not contribute the full amount of the ARC, a net OPEB obligation will emerge.
- Annual required contributions of the employer (ARC) - The employer's periodic required contributions to a defined benefit OPEB plan, calculated in accordance with the parameters.

- Defined benefit OPEB plan - An OPEB plan having terms that specify the *benefits* to be provided at or after separation from employment. The benefits may be specified in dollars (for example, a flat dollar payment or an amount based on one or more factors, such as age, years of service, and compensation), or as a type or level of coverage (for example, prescription drugs or a percentage of healthcare insurance premiums).
- Defined contribution plan - A pension or OPEB plan having terms that (a) provide an individual account for each plan member and (b) specify how contributions to an active plan member's account are to be determined, rather than the income or other benefits the member or his beneficiaries are to receive at or after separation from employment. Those benefits will depend only on the amounts contributed to the member's account, earnings on investments of those contributions, and forfeitures of contributions made for other members that may be allocated to the member's account. For example, an employer may contribute a specified amount to each active member's postemployment healthcare account each month. At or after separation from employment, the balance of the account may be used by the member or on the member's behalf for the purchase of health insurance or other healthcare benefits.
- Employer's contributions - Contributions made in relation to the annual required contributions of the employer (ARC). An employer has made a contribution in relation to the ARC if the employer has (a) made payments of benefits directly to or on behalf of a retiree or beneficiary, (b) made premium payments to an insurer, or (c) irrevocably transferred assets to a trust, or an equivalent arrangement, in which plan assets are dedicated to providing benefits to retirees and their beneficiaries in accordance with the terms of the plan and are legally protected from creditors of the employer(s) or plan administrator.
- Entry Age Normal Actuarial Cost Method – An actuarial cost method under which the Actuarial Present Value of the Projected Benefits of each individual included in the valuation is allocated on a level basis over the earnings or service of the individual between entry age and assumed exit age(s). The portion of this Actuarial Present Value allocated to a valuation year is called the Normal Cost.
- Healthcare cost trend rate - The rate of change in per capita health claims costs over time as a result of factors such as medical inflation, utilization of healthcare services, plan design, and technological developments.
- Investment return assumption (discount rate) - The rate used to adjust a series of future payments to reflect the time value of money.
- Net OPEB obligation - The cumulative difference since the effective date of GASB Statement 45 between annual OPEB cost and the employer's contributions to the plan, including the OPEB liability (asset) at transition, if any, and excluding (a)

short-term differences and (b) unpaid contributions that have been converted to OPEB-related debt.

Most employers will have no net OPEB obligation at the beginning of the year in which Statement 45 is implemented.

If an employer contributes the annual OPEB cost to the plan each year, and there are no actuarial or investment gains or losses then the net OPEB Obligation will remain zero.

- Normal Cost - That portion of the Actuarial Present Value of benefits and expenses which is allocated to a valuation year by the Actuarial Cost Method. Another interpretation is that the Normal Cost is the present value of future benefits that are "earned" by employees for service rendered during the current year.
- OPEB assets - The amount recognized by an employer for contributions to an OPEB plan greater than OPEB expenses.
- OPEB expense - The amount recognized by an employer in each accounting period for contributions to an OPEB plan on the accrual basis of accounting.
- Other postemployment benefits (OPEB) - Postemployment benefits other than pension benefits. Other postemployment benefits (OPEB) include postemployment healthcare benefits, regardless of the type of plan that provides them, and all postemployment benefits provided separately from a pension plan, except benefits defined as special termination benefits.
- Plan assets - Resources, usually in the form of stocks, bonds, and other classes of investments, that have been segregated and restricted in a trust, or in an equivalent arrangement, in which (a) employer contributions to the plan are irrevocable, (b) assets are dedicated to providing benefits to retirees and their beneficiaries, and (c) assets are legally protected from creditors of the employer(s) or plan administrator, for the payment of benefits in accordance with the terms of the plan.
- Present Value – See Actuarial Present Value.
- Projected Unit Credit Cost Method – An actuarial cost method under which the projected benefits of each individual included in an Actuarial Valuation are separately calculated and allocated to each year service by a consistent formula.
- Substantive plan - The terms of an OPEB plan as understood by the employer(s) and plan members.
- Unfunded Actuarial Accrued Liability (UAAL) – The excess of the Actuarial Accrued Liability over the Actuarial Value of Assets.

- Valuation date – The date as of which the postemployment benefit obligation is determined.





## City of Sausalito Retiree Healthcare GASB 45 Valuation

## Some Different Funding Approaches

Illustrated below are five different approaches to funding, for all present retirees and employees, the estimated total present value of all future benefits (\$9.5 million) for all current and retired employees and spouses. GASB 45 does not require any particular funding approach, so many other approaches would of course also be possible.

Fiscal Year Beginning July 1:	Current "Pay as You Go"	<i>Estimated Annual Funding in \$Thousands</i>		Level Percent of Payroll 20 Years	Level Percent of Payroll 30 Years
		Level Dollar 20 Years	Level Dollar 30 Years		
2008	135	760	616	581	419
2009	147	760	616	600	432
2010	160	760	616	619	447
2011	176	760	616	640	461
2012	193	760	616	660	476
2013	209	760	616	682	491
2014	228	760	616	704	507
2015	249	760	616	727	524
2016	270	760	616	750	541
2017	291	760	616	775	559
2018	312	760	616	800	577
2019	314	760	616	826	595
2020	321	760	616	853	615
2021	349	760	616	881	635
2022	373	760	616	909	655
2023	401	760	616	939	677
2024	450	760	616	969	699
2025	513	760	616	1,001	721
2026	575	760	616	1,033	745
2027	644	760	616	1,067	769
2028	718		616		794
2029	782		616		820
2030	838		616		847
2031	898		616		874
2032	959		616		902
2033	993		616		932
2034	1,006		616		962
2035	1,013		616		993
2036	1,009		616		1,026
2037	968		616		1,059
2038	937				
2039	945				
2040	936				
2041	925				
2042	934				
2043	919				
2044	889				
2045	878				
2046	859				
2047	840				
2048	833				
2049	816				
2050	798				
2051	785				
2052	770				
2053	753				
2054	732				
2055	709				
2056	682				
2057	652				

2058-2082 Avg. 260

Item #: 6B  
Meeting Date: 4-22-08  
Page No. 33

