



THE CITY OF SAN DIEGO

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## OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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**Date Issued:** May 28, 2015

**IBA Report Number:** 15-21

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**Item Number:** 200

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# Status of Other Post-Employment Benefits

## OVERVIEW

On June 1, 2015 the City Council is scheduled to be presented with an informational report (Council meeting agenda Item 200) on the status of the City's Other Post-Employment Benefits (OPEB). The City's OPEB consists of retiree health benefits, which are afforded to eligible employees based on negotiated agreements with the City's recognized employee organizations. Currently, the City provides retiree health benefit options for employees hired before July 1, 2005.

The information to be presented with Item 200 includes the City's "Postretirement Health Plan Actuarial Valuation Report as of June 30, 2014." Item 200 refers to the status of the "GASB 45" OPEB liability, a reference to the Governmental Accounting Standards Board reporting requirements for OPEB in the City's financial statements.

This report provides supplemental cost information which is not included in the valuation report, as well as additional background information. The costing figures contained in the valuation report apply to the City's defined benefit (DB) retiree health obligations. However, there are other retiree health benefit costs that the City is obliged to cover, per agreements with its employee organizations. These costs are related to the defined contribution (DC) retiree health benefits afforded to eligible employees. The combined DB and DC cost estimates for FY 2016 total \$74.0 million; and these cost components are discussed later in this report.

## DISCUSSION

### Background

As mentioned previously, City employees hired before July 1, 2005 are eligible to receive retiree

health benefits.<sup>1</sup> Prior to the benefit restructure in 2012, this benefit was in the form of a DB plan.<sup>2</sup> In a DB retiree health benefit, vested employees are provided a specific health benefit at retirement. Note that effective July 1, 2009 the vesting time requirement for the full DB benefit is 20 years.

The retiree health DB plan was restructured for employees effective April 1, 2012. There are three options associated with this restructured retiree health benefit:

- Option A is a DB plan with a full annual allowance (at 20 years of service) equal to \$8,883 per year, with a 2 percent annual escalator beginning FY 2014. This option was available to eligible employees on City payroll as of April 1, 2012 who had either 25 years of service credit or who were eligible to retire (age and service eligible). Additionally, this option requires that employees make nonrefundable contributions.
- Option B is a DB plan with a full annual allowance (at 20 years of service) equal to \$5,500 per year, with no escalator. This option requires that employees make nonrefundable contributions.
- Option C is a DC plan projected to yield \$8,500 annually with 20 years of service. There are no employee contribution requirements for this option. Employees who chose Options A or B but terminate employment prior to retirement will receive the Option C plan upon retirement eligibility.

### **Fiscal Effects of Restructuring the Retiree Health Benefit**

The effect of the 2012 retiree health benefit restructure on the City's DB retiree health plans is evident in the most recent actuarial valuation for the City, for the period ending June 30, 2014. The OPEB Unfunded Actuarial Liability (UAL) at June 30, 2014 is \$479.5 million, down from \$1.1 billion at June 30, 2011.

The June 30, 2014 OPEB Annual Required Contribution (ARC) projected for FY 2016 is \$41.7 million, down from the \$94.4 million projected at June 30, 2011. However, the ARC figure does not reflect the payment components the City plans to make with respect to its restructured retiree health benefits. In addition to the DB retiree health plans, there is also a DC plan that must be funded (Option C).

Additionally, despite its name, the City is not required to pay the ARC; but as of FY 2008 an accumulated liability based on unpaid ARC amounts has been booked on the financial statements in accordance with Governmental Accounting Standards Board (GASB) requirements. Information regarding the ARC and UAL are available in the June 30, 2014 valuation – which was performed by Buck Consultants and provided to the City in November 2014.

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<sup>1</sup> Additionally, for General Members there is a separate defined contribution Retiree Medical Trust for employees hired on or after July 1, 2009. The plan requires both an employee contribution and City match of 0.25% of an employee's base compensation. The FY 2016 Proposed Budget amount for this plan is \$287,000 (\$159,000 for the General Fund).

<sup>2</sup> For employees retiring before the DB retiree health benefit restructure became effective (April 1, 2012), the City has frozen the automatic escalator on the retiree health benefit for POA and AFSCME Local 127 employees who retired on or after July 1, 2009 and before April 1, 2012. The benefit is frozen at \$8,883 per year.

The table below shows estimates for the different components of the restructured retiree health benefits. These are the amounts the City estimates it will make through FY 2020 and are based on estimates provided by Buck Consultants.

Note that the table below reflects the citywide fiscal impact of the restructured retiree health benefit at \$57.8 million through FY 2015, with anticipated annual increases of no more than 2.5% thereafter. Accordingly, retiree health obligations total \$59.2 million (\$39.0 million for the General Fund) in the FY 2016 Proposed Budget.

<b>OPEB/Retiree Health Forecast (in millions)</b>	<b>FY 2015 Forecast</b>	<b>FY 2016 Forecast</b>	<b>FY 2017 Forecast</b>	<b>FY 2018 Forecast</b>	<b>FY 2019 Forecast</b>	<b>FY 2020 Forecast</b>
1 PAYGO	\$ 41.8	\$ 43.2	\$ 44.7	\$ 46.4	\$ 48.2	\$ 48.9
2 CalPERS Trust Contribution/(Withdrawal)	(10.1)	(14.4)	(15.7)	(14.3)	(14.5)	(14.9)
3 Contribution to HRA Accounts	26.9	30.8	31.8	30.0	29.9	31.1
4 Benefit Administration by SDCERS	0.5	0.6	0.6	0.6	0.6	0.6
5 Less: Employee Contributions	(1.3)	(1.0)	(0.7)	(0.5)	(0.4)	(0.3)
<b>Total City Contribution</b>	<b>\$ 57.8</b>	<b>\$ 59.2</b>	<b>\$ 60.7</b>	<b>\$ 62.2</b>	<b>\$ 63.8</b>	<b>\$ 65.4</b>

Again, the table above shows the estimated retiree health payment components for the restructured benefit, which include the following:

- The first row contains the pay-go estimates associated with retiree health benefit payments for eligible retirees under the City's retiree health DB plans. Note that there is a DB plan for eligible employees retiring before April 1, 2012, as well as the restructured DB options effective April 1, 2012.
- The second row contains estimated amounts that will either be paid into or withdrawn from the CalPERS OPEB Trust Fund for the City's retiree health benefits. When funds are needed to cover expenses above the City's budgeted retiree health contribution amount, they will be withdrawn from the trust fund (to fund pay-go). This occurs in FY 2015 through 2020.
- The third row contains estimated City contributions to Health Reimbursement Arrangement (HRA) accounts. These amounts will fund HRA accounts for eligible employees retiring on or after April 1, 2012 who selected the DC retiree health plan (restructured retiree health benefit Option C).
- The fourth row contains cost estimates for administration payments to SDCERS to manage the retiree health benefit program.
- The fifth row contains estimates for contributions that will be made by employees retiring on or after April 1, 2012 who selected the DB retiree health plan options (restructured retiree health benefit Options A and B).

- The last row is the sum of the first five rows and equals the total citywide payments to be made each fiscal year.

For FY 2016 the estimated retiree health benefit cost components total \$74.0 million: which include the \$43.2 million pay-go related to the DB plans (row 1 in the table on the previous page) and the \$30.8 million DC plan contributions to HRA accounts (row 3).


## CONCLUSION

This report provides supplemental cost information which is not included in the June 30, 2014 OPEB actuarial valuation report, as well as additional background information related to Item 200 on the June 1, 2015 City Council meeting agenda. The costing figures contained in the valuation report apply to the City's DB retiree health obligations. However, there are other retiree health benefit costs that the City is obliged to cover, per agreements with its employee organizations. These costs are related to the DC retiree health benefits afforded to eligible employees.

Again, for FY 2016 the estimated retiree health benefit cost components total \$74.0 million: which include \$43.2 million in pay-go related to the DB plans (row 1 in the table on the previous page) and \$30.8 million for DC plan contributions to HRA accounts (row 3).

The parameters for retiree health benefits for eligible employees hired before July 1, 2005 are included in 15-year agreements with the City's six recognized employee organizations. Per these agreements, the retiree health benefit can be modified after June 30, 2014.

  
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