

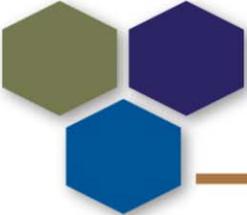


Michigan State Police

Retiree Health Actuarial Valuation Results as of September 30, 2009

GRS

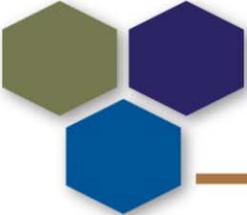
Gabriel Roeder Smith & Company
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Retiree Health Benefits

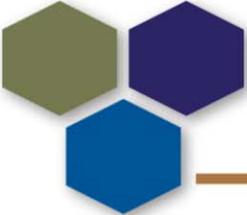
The Funding Issue

- ◆ Unlike pensions, health benefits have not been pre-funded (most pension plans nationwide have not pre-funded health benefits either)
 - ▶ No investment income to help pay the costs
- ◆ Costs rise as more members retire, and health inflation outpaces general inflation
- ◆ Pre-funding contribution rates have been calculated since 1999 – but pre-funding contributions have not been made



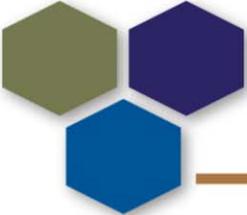
Governmental Accounting Standards Board

- ◆ Beginning with the 2007 CAFR, GASB Statements No. 43 and No. 45 specify how retiree health benefit liabilities and expenses are reported in financial statements
- ◆ The reported annual expense is called the Annual Required Contribution (ARC)
- ◆ If the employer fully funds the actuarially computed ARC, in a qualified trust with a long-term investment policy, then the liabilities and ARC are based on a long range investment return assumption (approximately 8%)
- ◆ If the employer only pays the cash benefits, with no pre-funding, the liabilities and ARC are based on a short term investment return assumption, like that earned on the employer's general accounts (approximately 4%) – and the liabilities and ARC are much larger



Governmental Accounting Standards Board

- ◆ The reported liability and ARC depend on how the employer is funding the benefits
- ◆ If the employer funds more than the cash benefits but less than the full actuarial contribution (partial pre-funding), the liabilities and ARC will lie somewhere between the pre-funding and cash funding results
- ◆ Existing employer contributions to pay the cash benefits count as contributions toward meeting the ARC
 - ▶ Medicare Part D Retiree Drug Subsidy (RDS) payments received during the year also count as employer contributions toward meeting the ARC



SPRS – GASB Compliant Valuation

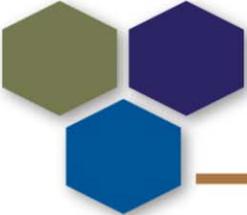
- ◆ Annual Expenditures for Retiree Health Care Benefits:

- ▶ FY 2009: \$31.6 million

- ◆ 2009 Potential Unfunded Accrued Liability and ARC:

	<u>Unfunded Liability</u>	<u>ARC - FY2010</u>
Full Actuarial Funding	\$527 million	\$42 million

Potential Unfunded Liability and ARC from September 2009 actuarial valuation
Annual Expenditures from the SPRS 2009 Comprehensive Annual Financial Report



SPRS – GASB Compliant Valuation Full Actuarial Funding

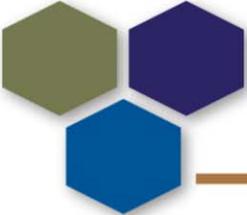
◆ 2009 Potential Unfunded Accrued Liability and ARC:

	<u>Unfunded Liability</u>	<u>ARC - FY2010</u>
Full Actuarial Funding	\$527 million	\$ 42 million
Less Actual FY2009 Employer Contribution		<u>\$(30 million)</u>
Additional Employer Contribution to Fully Fund the ARC		\$ 12 million

- ◆ Lump sum of \$527 million would fully fund the 2009 unfunded liability
- ◆ Once fully funded, the annual employer contribution requirement decreases to the normal cost
- ◆ Employer normal cost is \$9.0 million in FY2010

Potential Unfunded Liability and ARC from September 2009 actuarial valuation

Actual FY2009 Employer Contribution from the SPRS 2009 Comprehensive Annual Financial Report



SPRS – GASB Compliant Valuation

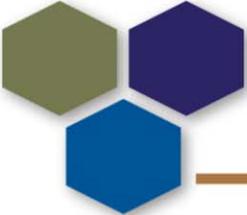
Full Actuarial Funding vs. Cash Funding

- ◆ 2009 Potential Unfunded Accrued Liability and ARC:

	<u>Unfunded Liability</u>	<u>ARC - FY2010</u>
Full Actuarial Funding	\$527 million	\$42 million
Cash Funding	\$882 million	\$60 million

- ◆ Lump sum of \$527 million would fully fund the 2009 unfunded liability (annual normal cost thereafter)
- ◆ The \$882 million amount is for reporting and disclosure purposes (if cash funding is continued), and is not an amount that needs to be funded in a lump sum
- ◆ \$355 million (\$882 less \$527) represents some of the lost investment income from not pre-funding

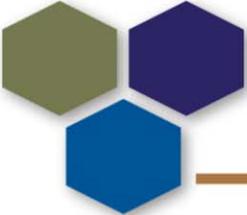
Potential Unfunded Liability and ARC from September 2009 GASB valuation



SPRS – GASB Compliant Valuation

Impact of Cash Funding Policy (Pay-go)

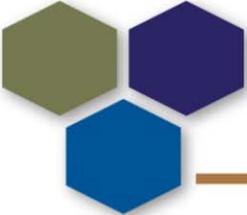
- ◆ No investment income to help pay the costs
 - Higher liability reported, compared to full actuarial funding
- ◆ Reported liability on State's balance sheet
 - Page 75 of State of Michigan 2009 CAFR
 - Only 47.2% of ARC
 - \$63.4 million Net OPEB Obligation
 - This balance sheet liability will grow



Circumstances That Would Increase Projected Costs

- ◆ Medicare funding reductions or cost shifting
- ◆ Unexpected new entrants into the retiree health plan (from health benefit cutbacks of other employers)
- ◆ Medical inflation worse than assumed; the actual future contributions will depend on future per capita health cost increases (health inflation) *
- ◆ Active member population decline (contribution rates as a percentage of payroll would increase)
- ◆ This is not a complete list

* *Per capita costs are projected to increase 9.0% the first year, graded down to 3.5% in the twelfth and later years*

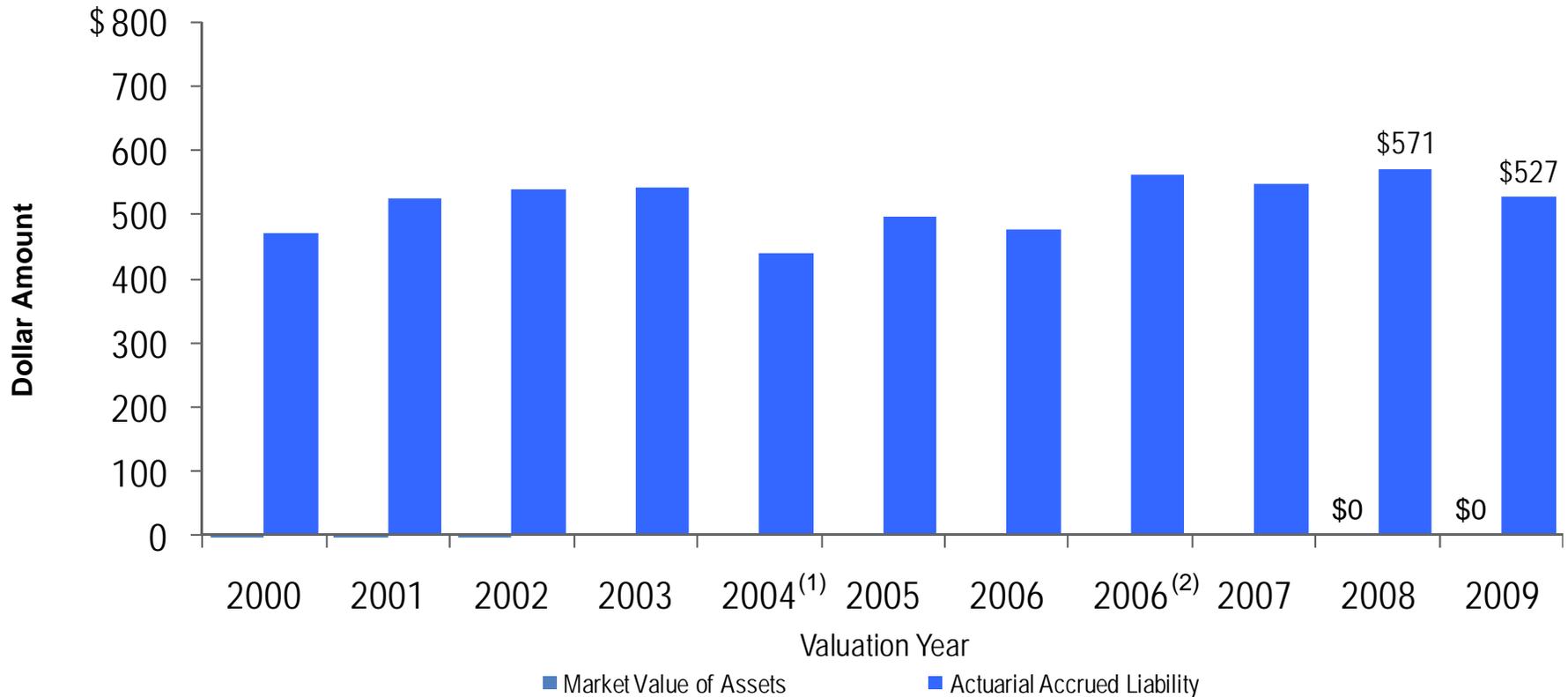


Solutions and Observations

- ◆ Strategic planning – an important tool to contain costs while delivering valuable benefits
- ◆ Plan for increases in employer health care contributions
- ◆ Partial pre-funding (more than cash funding, but less than GASB ARC) may protect against higher costs if experience is worse than projected

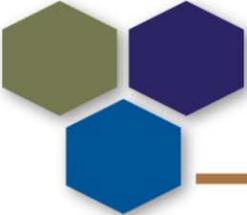
Health Assets & Accrued Liabilities

Full Actuarial Funding (Amounts in Millions)

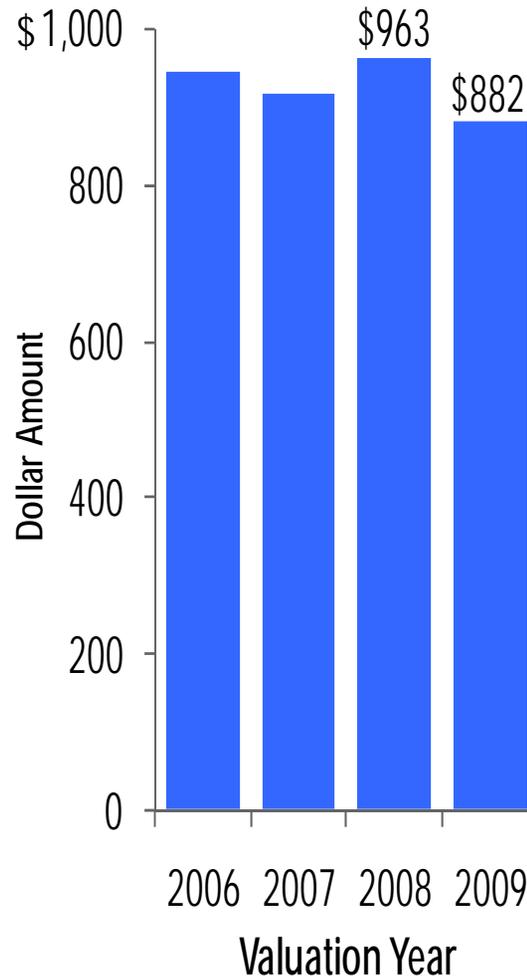


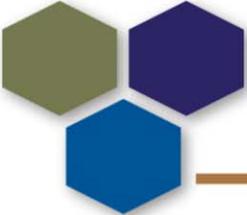
(1) Reflects assumption changes

(2) Reflects assumption changes and compliance with GASB Statements No. 43 and No. 45

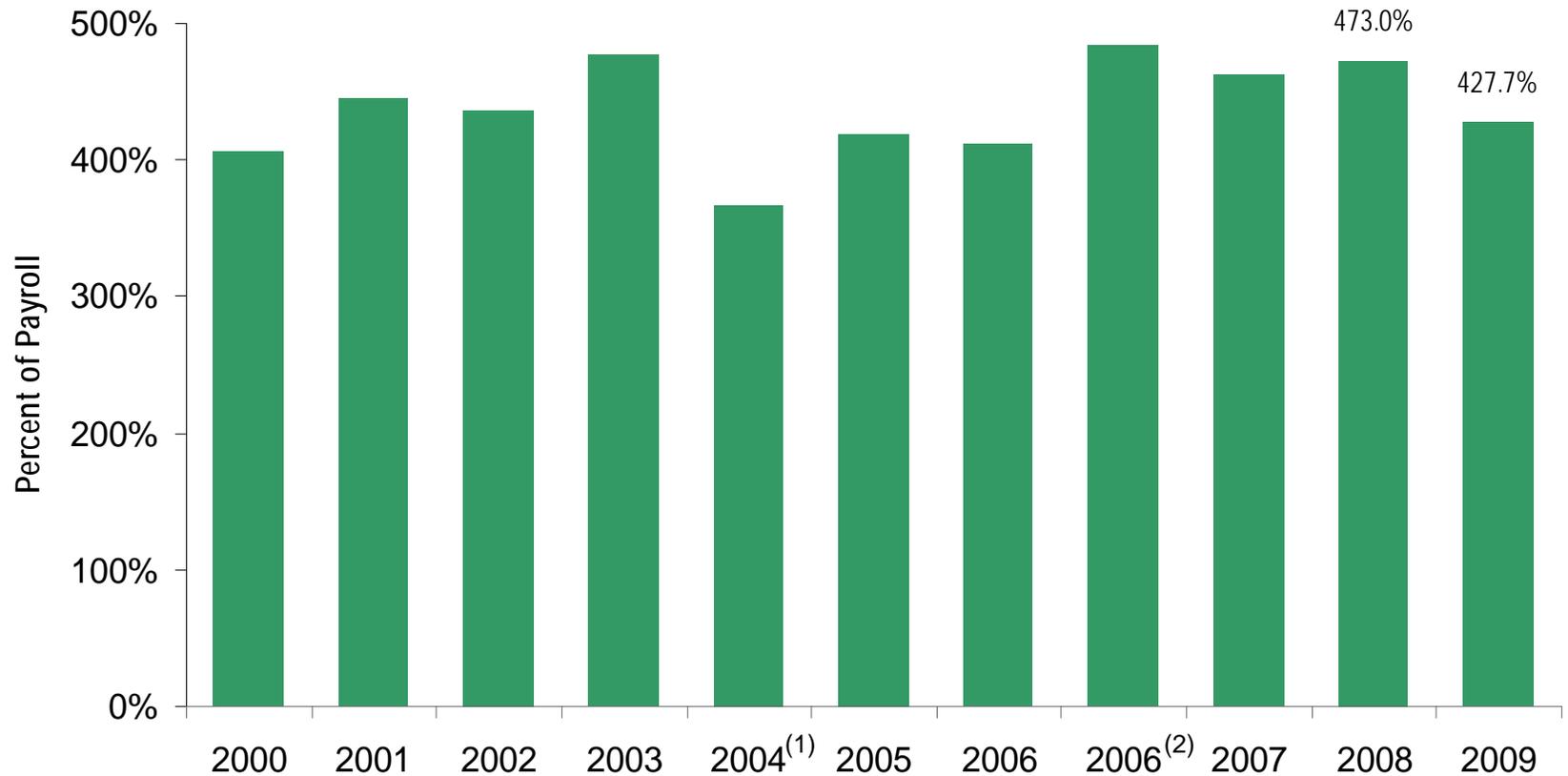


Health Accrued Liabilities - Cash Funding (Pay-go) (Amounts in Millions)





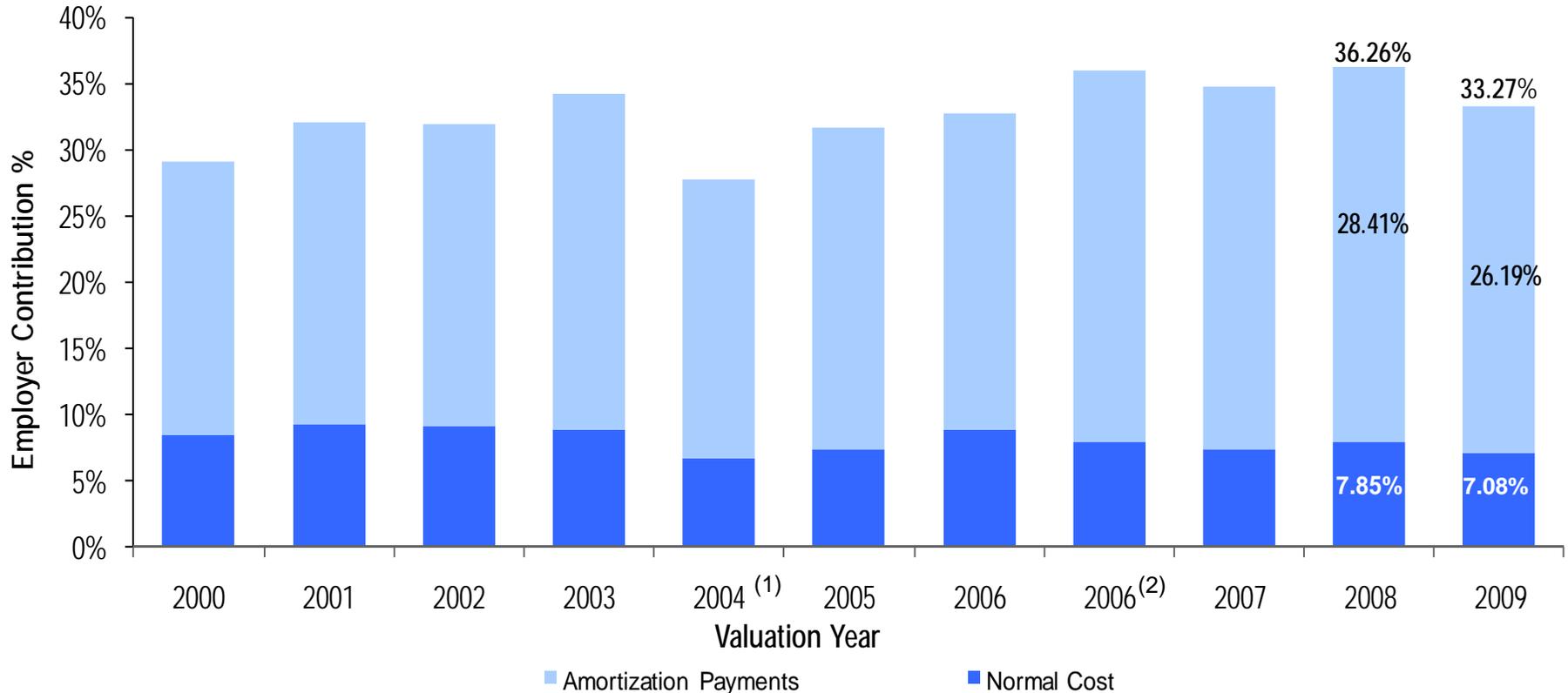
Unfunded Accrued Liabilities as %'s of Payroll – Full Actuarial Funding



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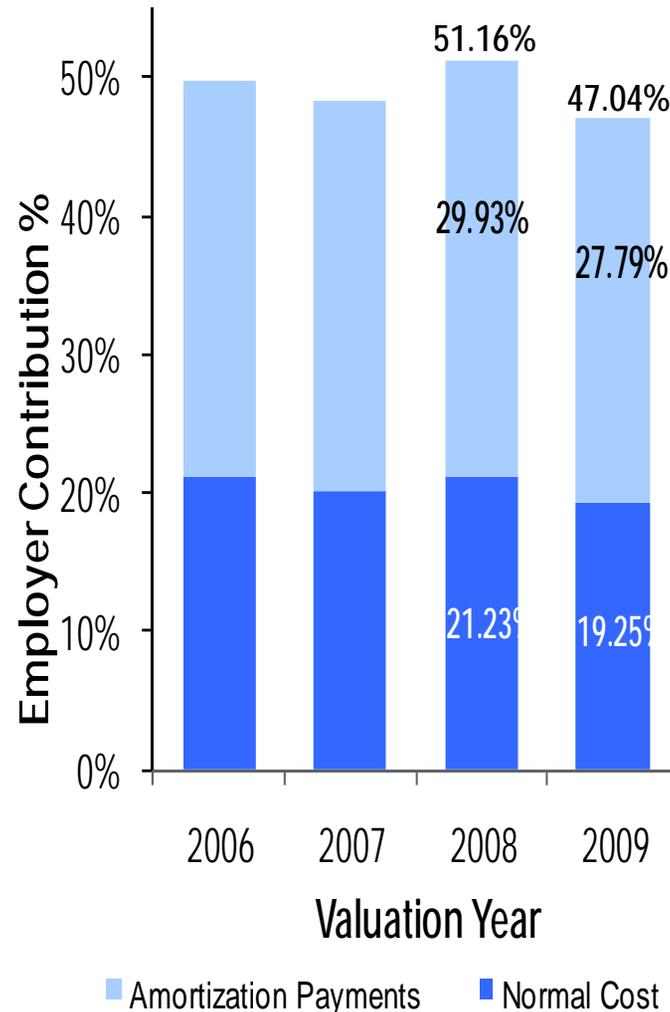
Annual Required Contributions (ARC) as Percents of Payroll (Full Actuarial Funding)

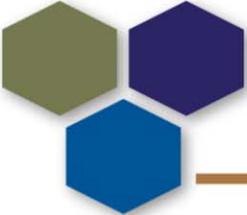


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Annual Required Contributions (ARC) as Percents of Payroll (Cash Funding – Pay-go)





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