



Michigan Public School Employees

Retiree Health Actuarial Valuation Results
as of September 30, 2007

GRS

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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



MPSERS – GASB Compliant Valuation

- ◆ Annual Expenditures for Retiree Health Care Benefits:

- ▶ FY 2007: \$654 million

- ◆ 2007 Potential Unfunded Accrued Liability and ARC:

	<u>Unfunded Liability</u>	<u>ARC - FY2008</u>
Full Actuarial Funding	\$15.8 billion	\$1,617 million

Potential Unfunded Liability and ARC from September 2007 actuarial valuation.

Annual Expenditures from the State's 2007 Comprehensive Annual Financial Report.

Medicare Advantage payments will likely reduce the potential unfunded liability and ARC.



MPERS – GASB Compliant Valuation Full Actuarial Funding

◆ 2007 Potential Unfunded Accrued Liability and ARC:

	<u>Unfunded Liability</u>	<u>ARC - FY2008</u>
Full Actuarial Funding	\$15.8 billion	\$1,617 million
Less Actual FY2007 Employer Contribution		<u>\$ (672 million)</u>
Additional Employer Contribution to Fully Fund the ARC		\$ 945 million

- ◆ Lump sum of \$15.8 billion would fully fund the 2007 unfunded liability
- ◆ Once fully funded, the annual employer contribution requirement decreases to the normal cost
- ◆ Employer normal cost is \$653 million in FY2008

Potential Unfunded Liability and ARC from September 2007 actuarial valuation.

Actual FY2007 Employer Contribution from State's 2007 Comprehensive Annual Financial Report.

Medicare Advantage payments will likely reduce the potential unfunded liability and ARC.



MPERS – GASB Compliant Valuation Full Actuarial Funding vs. Cash Funding

- ◆ 2007 Potential Unfunded Accrued Liability and ARC:

	<u>Unfunded Liability</u>	<u>ARC - FY2008</u>
Full Actuarial Funding	\$15.8 billion	\$1,617 million
Cash Funding	\$25.0 billion	\$2,426 million

- ◆ Lump sum of \$15.8 billion would fully fund the 2007 unfunded liability (annual normal cost thereafter).
- ◆ The \$25.0 billion 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.
- ◆ \$9.2 billion (\$25.0 less \$15.8) represents some of the lost investment income from not pre-funding.

Potential Unfunded Liability and ARC from September 2007 GASB valuation.

Medicare Advantage payments will likely reduce the potential unfunded liability and ARC.



Recent MPERS Reform

PA 110 of 2007

- ◆ School employees hired after June 30, 2008 will be eligible for a graded retiree health premium subsidy based on *credited* service:
 - ▶ Under 10 years: No subsidy
 - ▶ 10 years: 30% subsidy
 - ▶ Over 10 years: 4% per additional year
 - ▶ 25+ years: 90% subsidy
- ◆ If the member retires before age 60 with fewer than 25 years of *actual* service, the subsidy does not start until age 60



MPSERS

Costs after PA 110 of 2007

- ◆ The current cash funding employer contribution rate for retiree health benefits is 6.55%
- ◆ Before PA 110, the cash funding contribution rate was projected to increase over the next 50 years to around 20% of payroll
- ◆ After PA 110, the cash funding contribution rate is projected to increase much less: to about 10% - 11% of payroll by 2017, stabilizing at that level in later years
- ◆ Of course, the actual future rates will depend entirely on future per capita health cost increases (health inflation) *

* *Per capita costs are projected to increase 9.5% the first year, graded down to 3.5% in the eleventh and later years. For comparison, per capita costs increased 6.6% annually (compounded) from 2000 to 2006.*



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

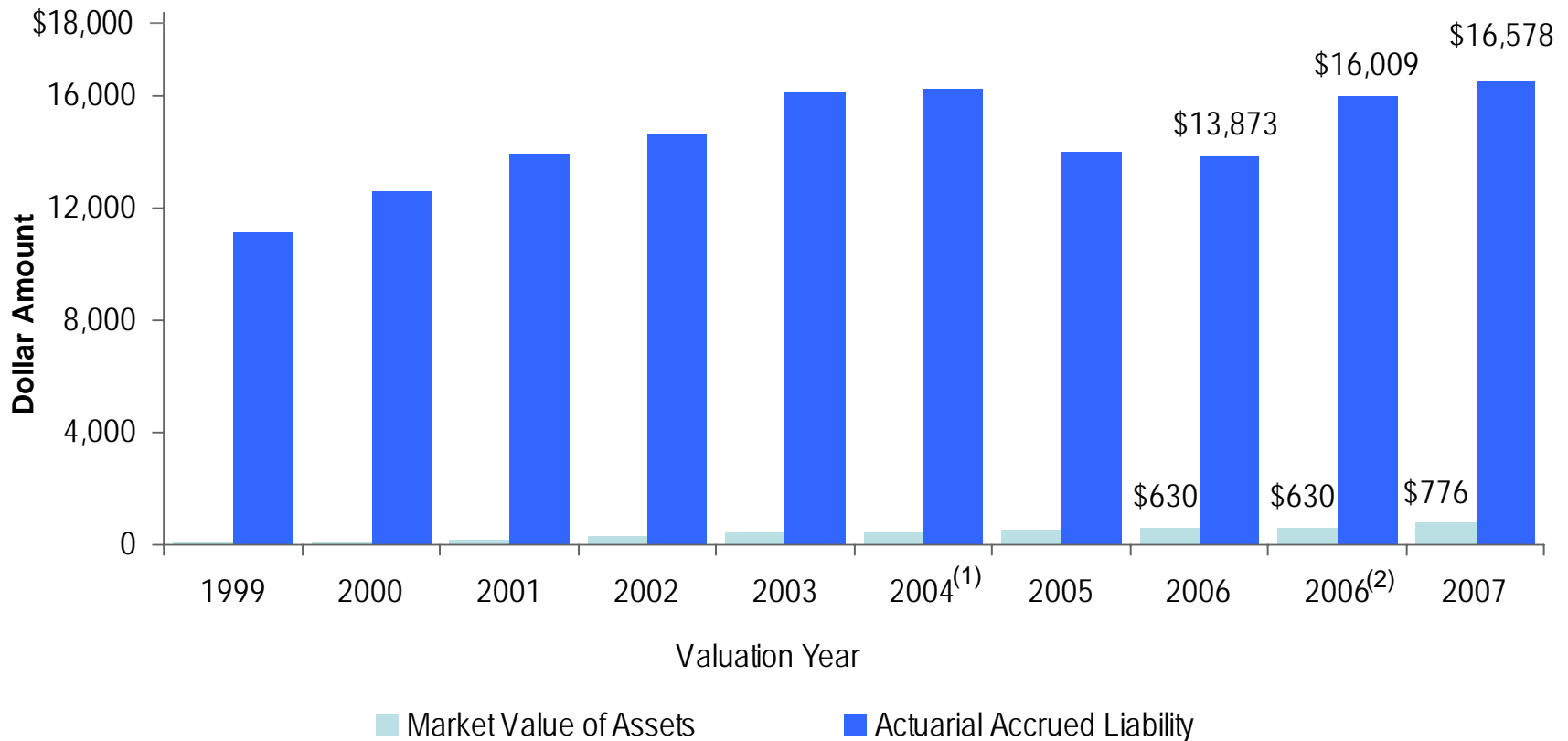


Solutions and Observations

- ◆ Strategic planning – an important tool to contain costs while delivering valuable benefits
- ◆ Plan for increases in employer health care contribution rates during the next 10 years
- ◆ PA 110 mitigates a significant portion of the long term projected contribution rate increases
- ◆ 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)

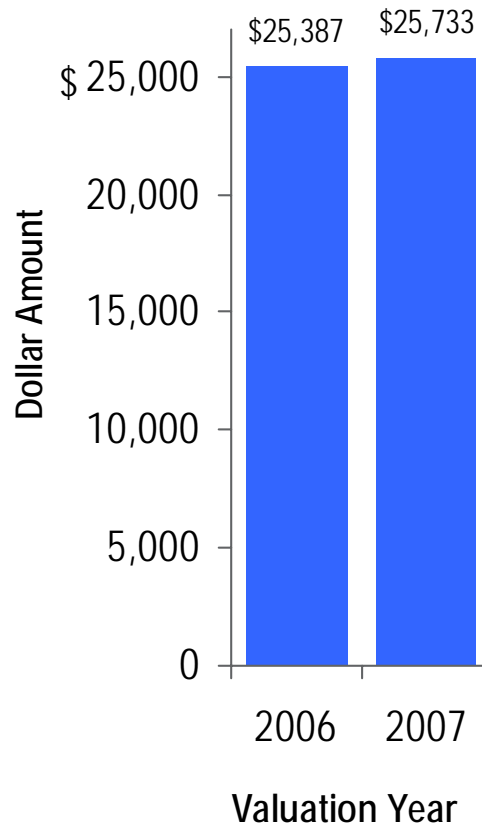


(1) Reflects assumption changes

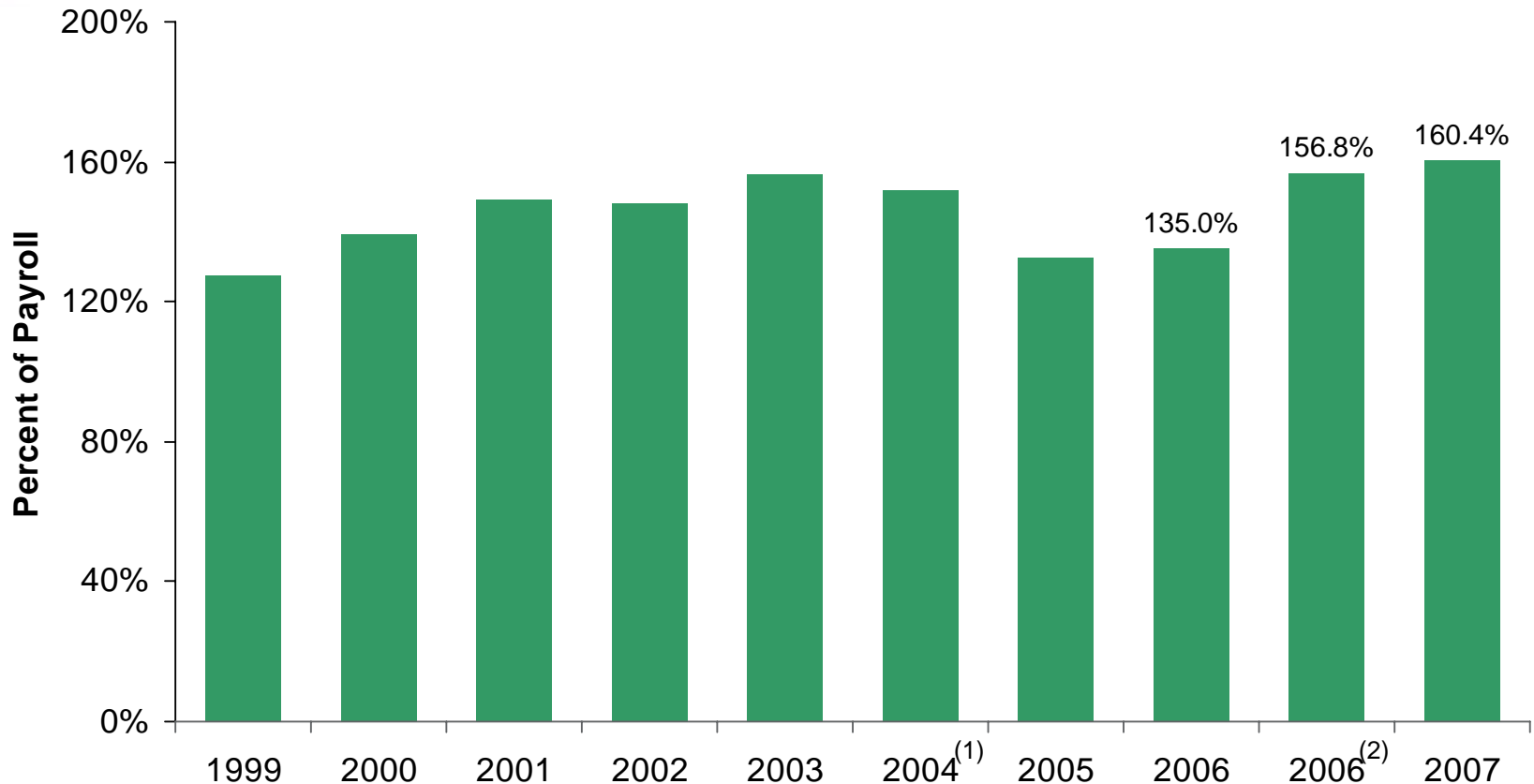
(2) Reflects assumption changes and compliance with GASB Statements No. 43 and No. 45



Health Accrued Liabilities Cash Funding (Paygo) (Amounts in Millions)



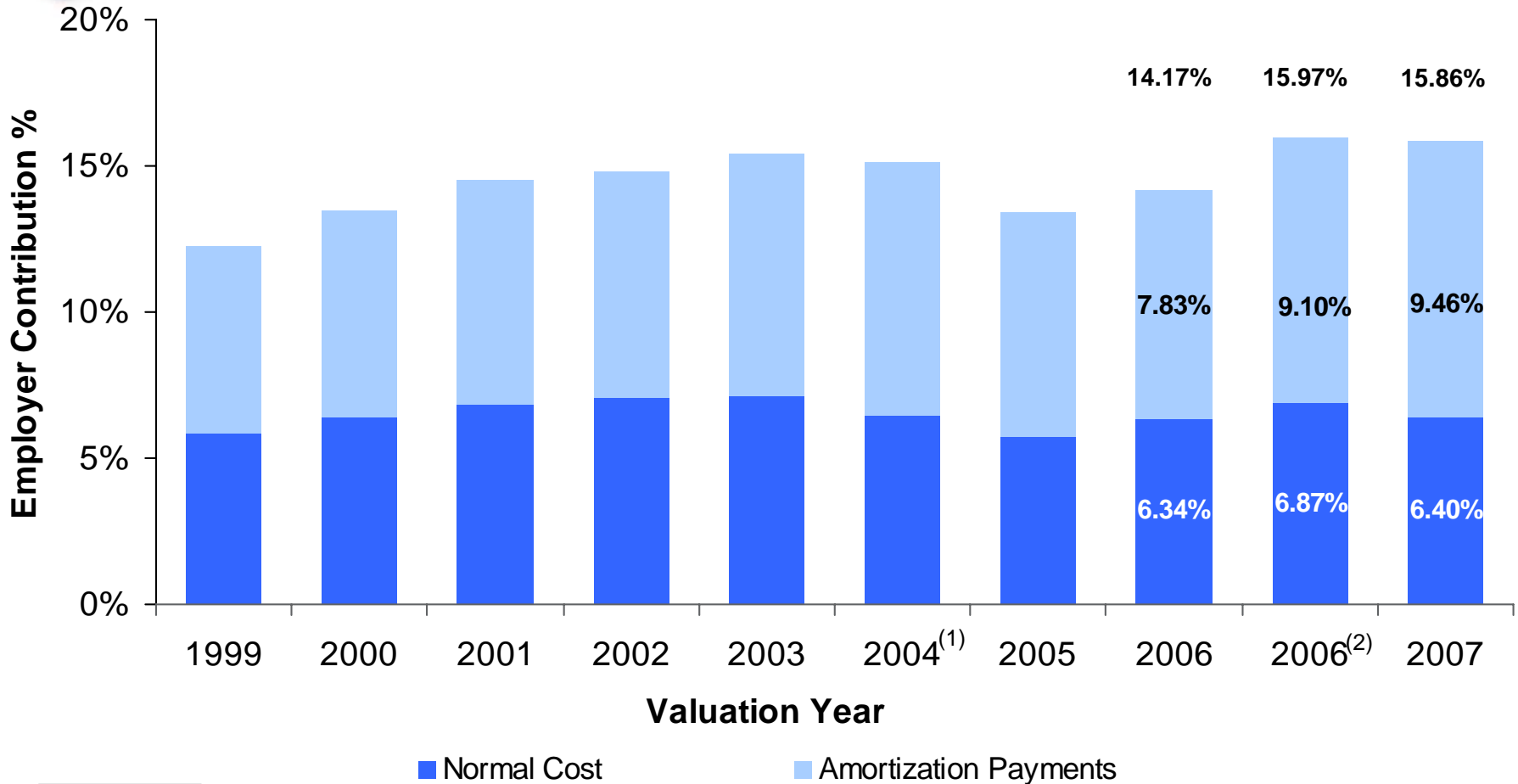
Unfunded Accrued Liabilities as %'s of Payroll – Full Actuarial Funding



(1) Reflects assumption changes

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

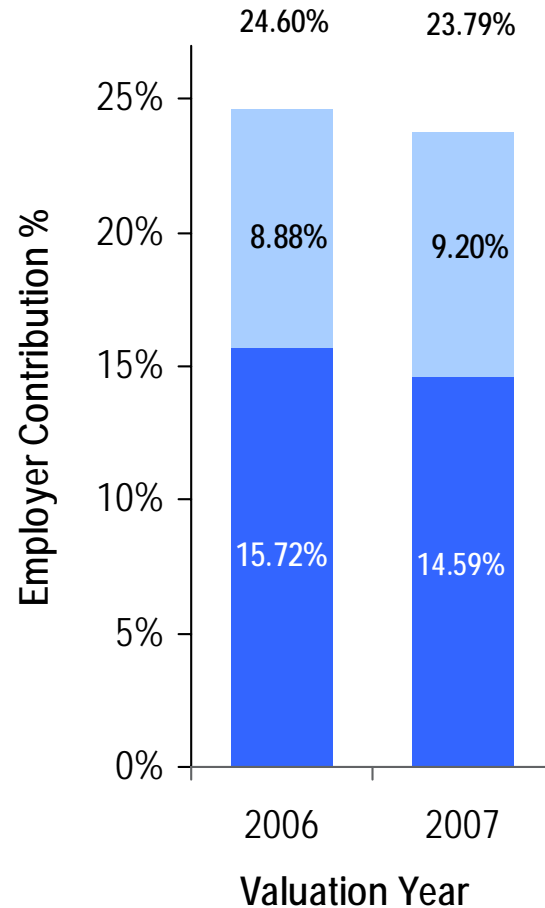
Annual Required Contributions (ARC) as Percents of Payroll (Full Actuarial Funding)



(1) Reflects assumption changes

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

Annual Required Contributions (ARC) as Percents of Payroll (Cash Funding - Paygo)



■ Normal Cost ■ Amortization Payments



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