Michigan Judges' Retirement System

Retiree Health Actuarial Valuation Results as of September 30, 2015

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Retiree Health Benefits

Participants Eligible for Employer Subsidized Benefits

- Plan 1 and Plan 2 members, both defined benefit (Tier 1) and defined contribution (Tier 2)
- Covered participants pay 2% of compensation while actively employed
- Covered participants receive employer subsidized health benefits after retirement
- Other retired judges may enroll in the health plan, but pay the full cost of their coverage

Retiree Health Benefits
The Funding Issue

- Unlike pensions, health benefits have not been pre-funded (most plan sponsors 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

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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 the financial statements
- The reported annual expense is based on 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

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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

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

- 2015 Potential Unfunded Accrued Liability and ARC:

	Unfunded Liability	ARC - FY2016
Full Actuarial Funding	$6.1 million	$495 thousand
Cash Funding	$9.1 million	$712 thousand

- Lump sum of $6.1 million would fully fund the 2015 unfunded liability (annual employer normal cost payments thereafter –$50 thousand in FY 2016).
- The $9.1 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.
- $3.0 million ($9.1 less $6.1) represents some of the lost investment income from not pre-funding.

The potential Unfunded Liability and ARC are from the September 2015 GASB valuation.

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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% the first year, graded down to 3.5% in the tenth and later years.*

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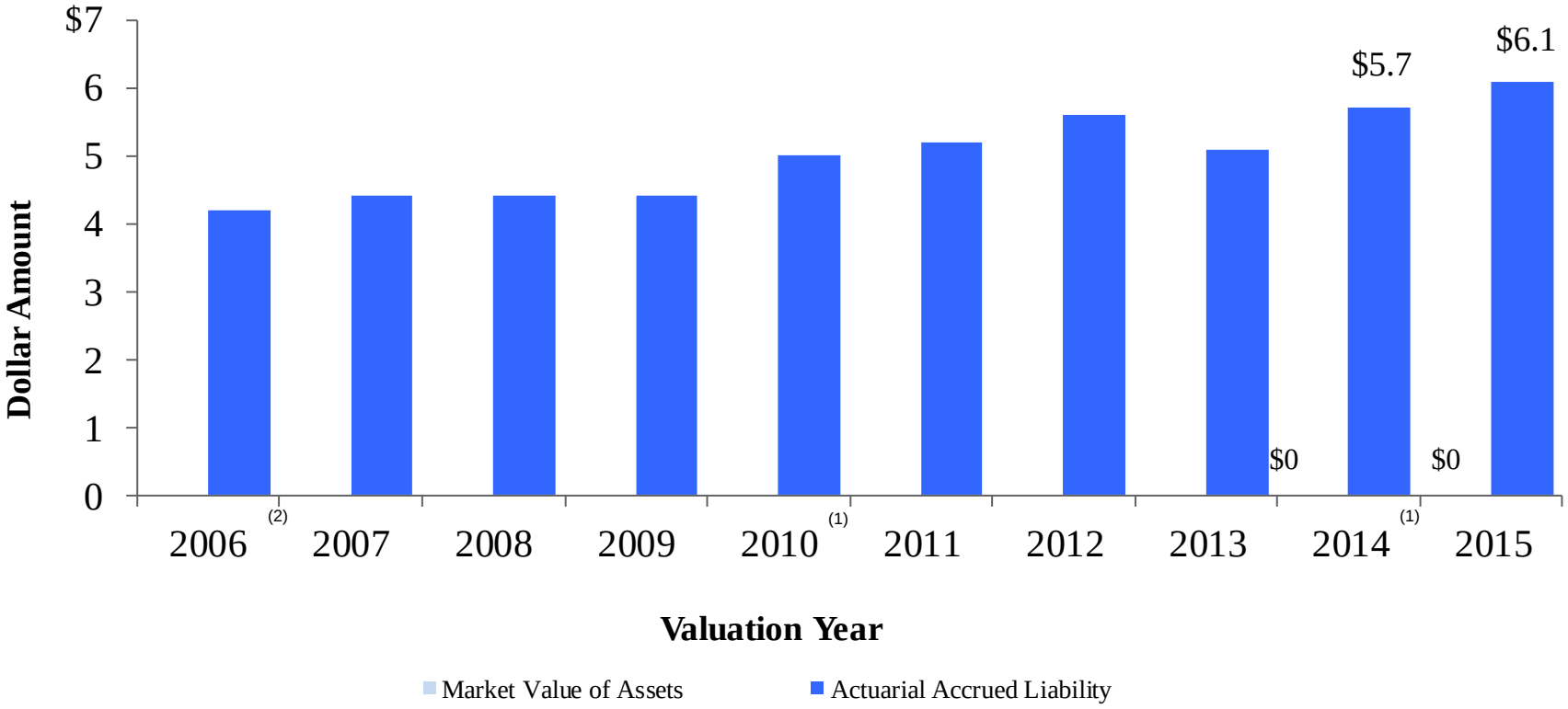
Solutions and Observations

- 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*

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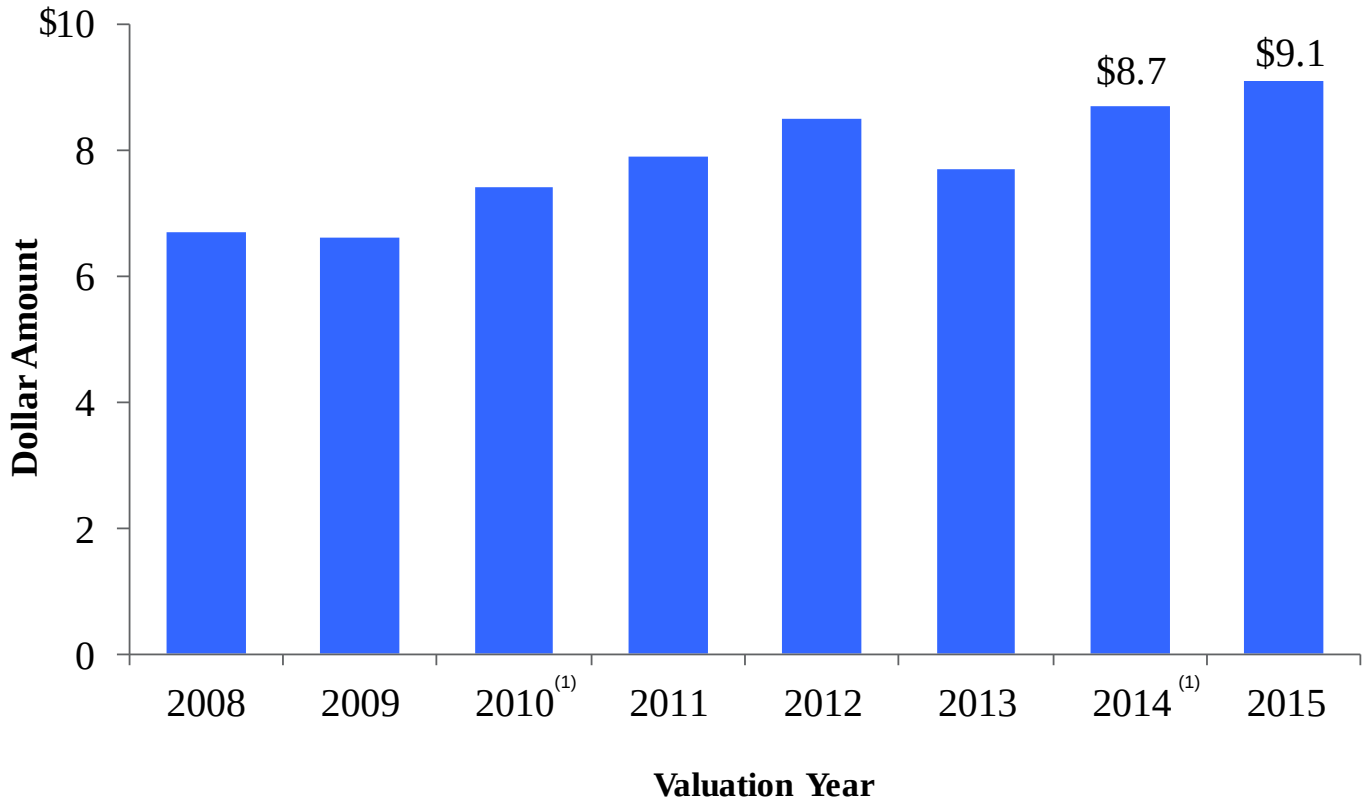
Health Accrued Liabilities
Cash Funding (Paygo) (Amounts in Millions)



(1) *Reflects assumption changes*

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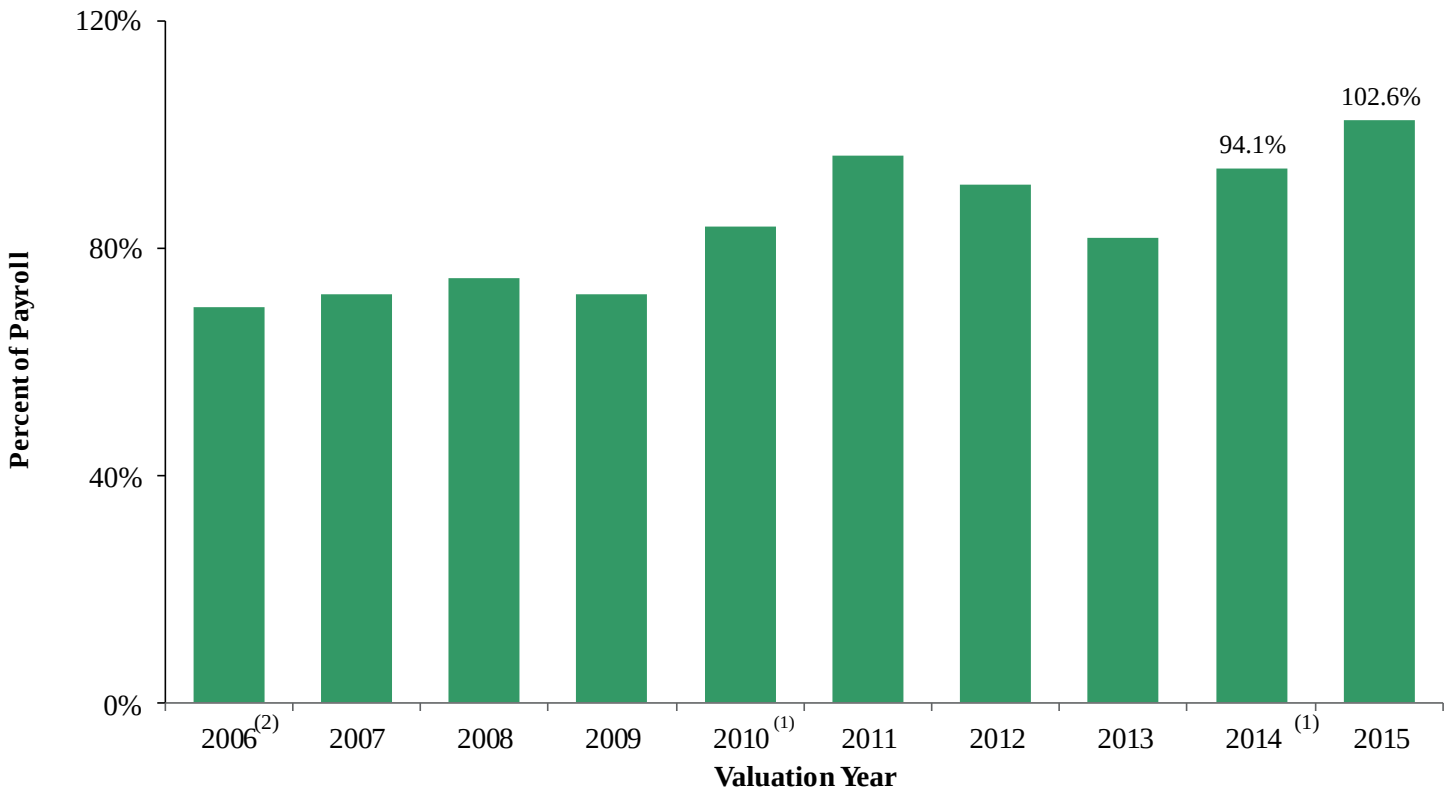
Unfunded Accrued Liabilities as %'s of Payroll – Full Actuarial Funding



(1) *Reflects assumption changes*

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

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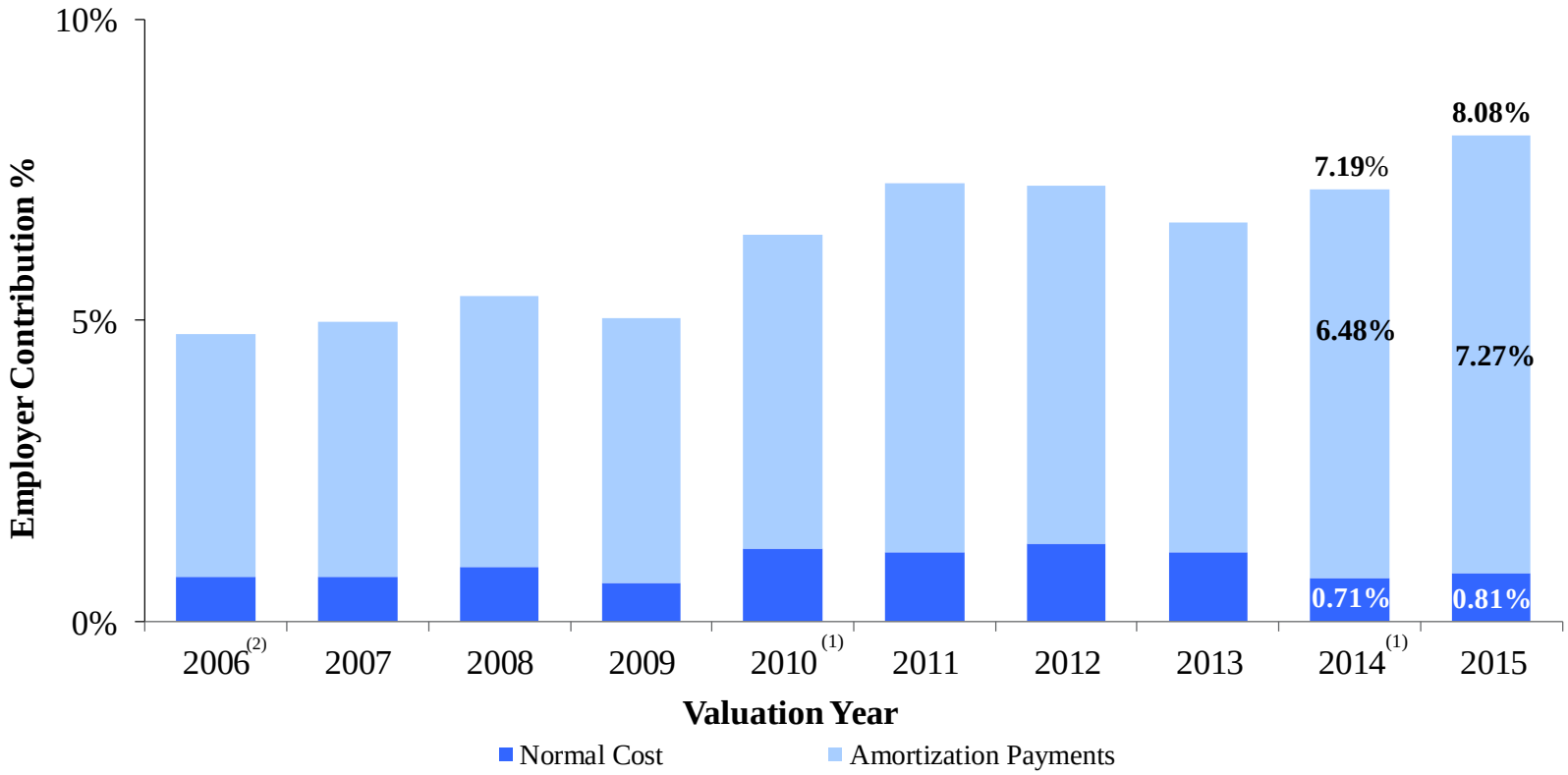
Annual Required Contributions (ARC) as Percents of Pay[3] (Full Actuarial Funding)



(1) *Reflects assumption changes*

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

(3) *Projected pay*

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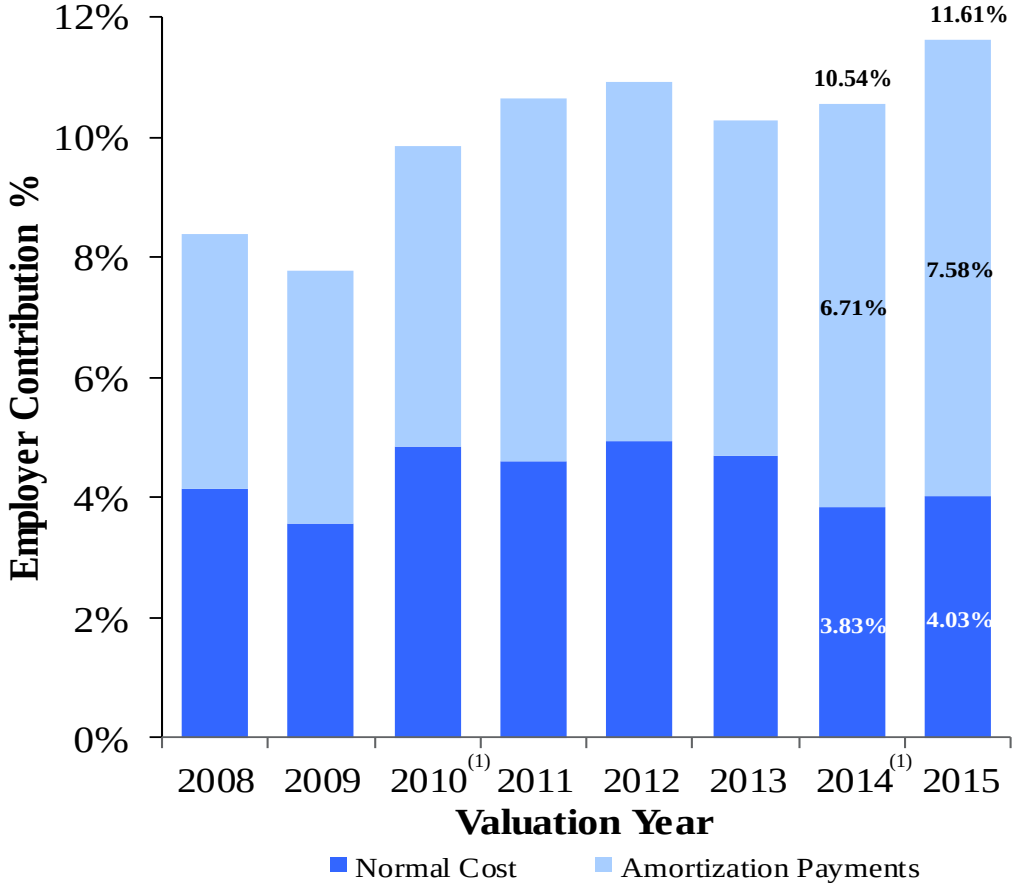
Annual Required Contributions (ARC) as Percents of Pay[2] (Cash Funding - Paygo)



[1] *Reflects assumption changes*

[2] *Projected pay*

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