

**SUBMITTAL TO THE BOARD OF SUPERVISORS  
COUNTY OF RIVERSIDE, STATE OF CALIFORNIA**



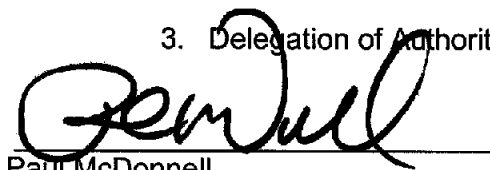
**FROM:** Paul McDonnell, Treasurer-Tax Collector  
Chairman, Pension Advisory Review Committee (PARC)

**SUBMITTAL DATE:**  
September 27, 2007

**SUBJECT:** Approval of Trust Agreement and Election to Pre-fund Other Post Employment Benefits (OPEB) with the California Public Employees Retirement System (CalPERS)

**RECOMMENDED MOTION:** That the Board of Supervisors:

- (1) Receive and file Aon's Actuarial Valuation Study on Post Retirement benefits dated August, 20, 2007 (Attachment A)
- (2) Authorize the Chair to execute the following agreements and certifications with CalPERS in order to establish a trust and election to pre-fund OPEB:
  1. California Employer's Retiree Benefit Trust Program Agreement and Election to Pre-fund OPEB Through CalPERS (Attachment B)
  2. Certification of Funding Policy (Attachment C)
  3. Delegation of Authority to Request Disbursements (Attachment D)

  
Paul McDonnell  
Treasurer-Tax Collector, Chairman

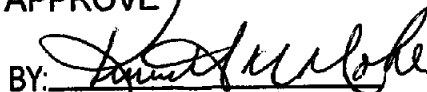
  
Ronald W. Komers  
Asst. CEO/Human Resources Dir., Member

  
Bill Luna  
County Finance Director, Member

<b>FINANCIAL DATA</b>	Current F.Y. Total Cost:	\$ 10 million	In Current Year Budget:	No
	Current F.Y. Net County Cost:	\$ 5 million	Budget Adjustment:	Yes
	Annual Net County Cost:	\$ TBD	For Fiscal Year:	07/08

<b>SOURCE OF FUNDS:</b> General fund designation (50%) and Fund 46120 (50%)	<b>Positions To Be Deleted Per A-30</b>	<input type="checkbox"/>
	<b>Requires 4/5 Vote</b>	<input checked="" type="checkbox"/>

**C.E.O. RECOMMENDATION:** APPROVE

BY:   
Kenneth M. Mohr

**County Executive Office Signature**

Policy  
 Consent

Policy  
 Consent

Dep't Recomm.:  
 Per Exec. Ofc.:

**Prev. Agn. Ref.:**

**District:**

**Agenda Number:**

FISCAL PROCEDURES APPROVED  
 ROBERT E. BYRD, AUDITOR-CONTROLLER  
 10/17/07  
 BY:   
 SUSANA GARCIA-BOCANEGRA

FORM APPROVED COUNTY COUNSEL  
 10-11-07  
 DATE  
 Departmental Concurrence  
 BY: DOROTHY L. HONN

**BOARD OF SUPERVISORS**

**Form 11: Approval of Trust Agreement with CalPERS**

**September 27, 2007**

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- (3) Direct the Executive Office and Human Resources Department to each make a \$5 million deposit (for a total deposit of \$10 million, plus earned interest of approximately \$400,000) to the trust on or before November 30, 2007.
- (4) Direct the Auditor-Controller to make the adjustments to designations and appropriations (Attachment E).
- (5) Direct staff to develop a rate structure for OPEB costs as a percentage of payroll, based on the entry age normal cost method, using a 30-year amortization period and the repayment of the \$10 million advance from the General Fund.

**BACKGROUND:** In June 2004 the Government Accounting Standards Board (GASB) issued GASB Statement 45 (GASB 25) effective for fiscal years beginning after December 15, 2006. GASB 45 addresses accounting and financial reporting for post-employment benefits other than pensions, referred to as OPEB. GASB 45 requires the County to report OPEB costs on an actuarial basis to account for the future costs of promised benefits. The County incurs OPEB cost because it provides retiree medical benefits for eligible retirees enrolled in County-sponsored plans. The benefit is provided in the form of: monthly County contributions towards retiree premiums, \$25 per month contribution to the RSA Trust for RSA law enforcement retirees, and the "implicit subsidy" incurred by allowing pre-Medicare retirees to receive health care coverage at the same premium rates as active employees.

On September 12, 2006, the Board directed the PARC to explore the options for establishing a trust to pre-fund OPEB liabilities and directed the Executive Office to designate \$10 million for an initial deposit to the trust. Also on September 12, 2006, the Board of Supervisors adopted a policy position that effective January 1, 2011 the County will establish a separate medical rate for all pre-Medicare retirees, thereby ending the "implicit subsidy." Employees whose retirement pre-dates January 1, 2009 will receive the subsidy until January 1, 2011. Employees retiring after January 1, 2009 will receive no subsidy.

The County's independent actuary Bradley J. Au (Aon) has prepared the Post Retirement Benefits Actuarial Valuation Study dated August 20, 2007 (Attachment A). The report was prepared using generally accepted actuarial practices and methods. Actuarial computations such as the Present Value of Benefits (PVB) and the Annual Required Contribution (ARC) have been made for GASB 45 purposes to fulfill the County's accounting requirements. The PVB represents the actuarial present value of all benefits ever to be paid to current employees and retirees for OPEB. The ARC represents the total current OPEB costs to the County for the fiscal year ending June 30, 2008.

The independent actuary's report indicates that as a result of the Board policy position taken on September 12, 2006 to eliminate the "implicit subsidy", the actuarial Present Value of all Benefits (PVB) declined from \$236.7 million to \$93.1 million. The Annual Required Contribution (ARC) declined from \$15.9 million to \$4.3 million since the last valuation report using the 30-year Entry Age Normal Cost Method. The impact of these decisions on medical plan rates was described and illustrated by Human Resources in the Form 11 establishing retiree medical plan rates for 2008, approved by the Board on the October 16, 2007 agenda.

Although GASB 45 does not require pre-funding, the portion of the ARC that is not funded each year accumulates as liability on the County's financial statements. If the County adopts a policy of pre-funding contributions into a trust, such as the CalPERS trust that invests in a mix of assets, it may use a higher discount rate in calculating the magnitude of GASB liabilities. The utilization of a higher discount rate significantly lowers the County's OPEB liability.

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The independent actuary's report compares the PVB results in a scenario where the County does not pre-fund the ARC versus where the County fully pre-funds the ARC, other than the portion attributable to the "implicit subsidy" that will be phased out by 2011. The report shows a reduction of the PVB from \$93.1 million to \$58.7, using 4.50% and 7.24% discount rates, respectively.

In order to take advantage of a higher discount rate and a significantly reduced PVB, the PARC recommends that the County adopt a policy to fully pre-fund the ARC, other than the portion attributable to the "implicit subsidy." The PARC will continue to monitor funding options. It is anticipated that an actuarial valuation will be commissioned annually.

As a first step to funding the OPEB obligation to a trust, a Post Employment Benefits designation in the amount of \$10 million was established in October 2006. The Executive Office and the Human Resources department together identified \$5 million of flexible credit funds accumulated in prior years for individuals that waived healthcare coverage that can be used in place of an equivalent amount of designation. The \$5 million remaining in the OPEB designation can be reallocated later this year to the capital projects designation.

The PARC, having reviewed various trust and funding arrangements, recommends entering into an agreement with the California Employers Retirement Benefits Trust Program (CalPERS Trust). The CalPERS Trust offers several advantages over other trust arrangements including but not limited to CalPERS' experience in operating similar trusts and CalPERS' cost competitiveness.

In order to facilitate pre-funding the ARC and repay the \$10 million General Fund advance, the PARC recommends that the County develop a rate structure for OPEB costs as a percentage of payroll, based on the Entry age Normal Cost Method under a 30 year amortization period used in the valuation report. This new rate structure should be developed in time to be implemented for the 2008/09 fiscal year.



**COUNTY OF RIVERSIDE  
POSTRETIREMENT BENEFITS**

**Actuarial Valuation Study**

**Valuation Date: January 1, 2007**  
**Date of Report: August 20, 2007**

# Executive Summary

## Background

The County of Riverside provides retiree medical benefits for eligible retirees enrolled in County sponsored plans. The benefits are provided in the form of:

- Monthly County contributions toward the retiree's premium, and
- \$25 per month to the RSA Trust for RSA law enforcement retirees, and
- Allowing pre-65 retirees to receive coverage at the active premium rates instead of normally higher retiree rates. Only participants who retire prior to January 1, 2009 are eligible for this benefit and the benefit will cease effective January 1, 2011, at which time all retirees will be required to pay "retiree only" (i.e. unblended) premium rates.

## County Contributions

The County of Riverside makes contributions to eligible retirees for their medical plan premiums when the retiree enrolls in a County sponsored health plan. The current monthly amount paid by the County ranges from \$25 – \$256, depending on the retiree's bargaining unit at retirement. The County provided amounts are detailed in Exhibit VIII and summarized as follows:

- **CalPERS Health Benefits program retirees** (Law Enforcement Management, Prosecution (Deputy DAs), and RSA Public Safety members) are eligible for the greater of the stated Public Employees' Medical and Hospital Care Act (PEMHCA) amounts and the bargaining unit's negotiated amount. The PEMHCA monthly amount of \$80.80 in 2007 grows to \$97.00 in 2008 and increases annually thereafter by Medical CPI. These are the only groups that have inflation-indexed benefits.
- **All other retirees** are eligible for the bargaining unit negotiated amount (i.e. \$25 – \$256). These amounts do not increase in future years to account for inflation.

Note: The County contributes \$25.00 per month to the RSA Benefit Trust for RSA Law Enforcement retirees. Although the Trust is responsible for providing a benefit with a much larger premium, the County is responsible for the \$25.00 monthly contribution and this benefit is included in Plan liabilities.

As described above, the majority of participants are eligible to receive benefits that are fixed at current levels. Only those receiving the PEMHCA benefits are eligible for inflation-indexed benefits. The long term benefit under PEMHCA could be 10 times greater than certain fixed benefit amounts in 25 years, as illustrated in Appendix A.

## Executive Summary (cont.)

### *Implicit Subsidy*

The County allows retirees to receive coverage prior to age 65 by paying premiums that are developed by blending active and retiree costs. Since retirees are older and generally cost more than actives, the premium paid by the retiree is less than the "true cost" of coverage for retirees. For example, under the Blue Shield HMO, the estimated "true cost" for retirees is \$610 per month, while the required premium is only \$374 per month in 2007. This implicit subsidy is considered an employer obligation under the new GASB requirements.

The implicit subsidy does not apply to post 65 benefits because premiums are based exclusively on retiree costs. It also does not apply to the CalPERS provided benefits as these premiums are considered "community rated" and, unlike the County's other plan premiums, do not vary due to claims experience or demographic differences of the employer.

The accounting rules do not require recognition of such implicit subsidization in the case of a "community-rated" plan. In this case, as just one of many employers in CalPERS plans, it is assumed that County premiums do not fluctuate on the basis of the number of covered County retirees. Rather, rates are dependent on the proportion of retirees from *all employers* in the plan, and the implied subsidy is not allocated to individual employers at all under the current accounting rules.

In the same respect, the dental and vision benefits offered to the County retirees are not considered to vary by age or demographics. Therefore, because a retiree must pay the entire premium amount to receive dental and vision benefits, there is no liability to the County for providing these benefits.

*Only participants who retire prior to January 1, 2009 and are not in the CalPERS plan are eligible for the implicit subsidy benefit. The implicit subsidy benefit will cease effective January 1, 2011, at which time all retirees will be required to pay "retiree only" (i.e. unblended) premium rates.*

### **GASB 45**

In June 2004, the Governmental Accounting Standards Board (GASB) issued GASB Statement 45, which addresses accounting and financial reporting for Postemployment Benefits Other Than Pensions (OPEB). This statement replaces and significantly modifies prior guidance. GASB 45 is effective for Phase I governments, including the County of Riverside, for fiscal years beginning after December 15, 2006.

## Executive Summary (cont.)

There are several reasons an agency should review its OPEB obligations sooner rather than later, such as:

- Pre-funding alternatives – although funding is not required, an unfunded plan results in higher balance sheet liabilities and costs
- Bargaining issues – recognizing how the obligation will impact the collective bargaining process in the near and long term
- Bond rating – potential impact to the cost of debt due to unfunded liabilities

The liabilities and annual costs for the County's contribution promises to retirees are calculated in this actuarial valuation in accordance with GASB 45. Similar to most government entities, the County has not previously pre-funded or recognized OPEB liability as benefits were accrued. This report assumes the County intends to fully pre-fund the County Contribution, but will not pre-fund the implicit subsidy. As this report shows, any required accrual determined on a GASB basis will be considerably higher than the amount on a pay-as-you-go basis.

It is important to note that only current active and retired participants are valued in this actuarial study. Future new entrants or any projected growth in the County's employee population are not considered.

### *ARC Development*

GASB requires an Annual Required Contribution (ARC) to be developed each year based on the Plan's assets and liabilities. Although GASB does not actually require prefunding, the portion of the ARC that is not funded each year accumulates as a liability on the County's financial statements.

The ARC can be developed under a variety of funding methods. This report shows results under two of the methods permitted – Aggregate and Entry Age Normal. We also show the ARC calculated using different amortization periods as a level percent of pay.

### **Summary of Results**

#### *Liabilities*

There are a few terms to understand related to the Plan's liabilities. The Present Value of Benefits (PVB) represents the actuarial present value of all future benefits expected to be paid to current employees and retirees. The Actuarial Accrued Liability (AAL) is the portion of the PVB attributable to past service. The Normal Cost is the portion of the PVB that is allocated to the current plan year for active employees.

## Executive Summary (cont.)

The table below summarizes the liability results:

Present Value of Benefits (PVB)	\$58,757,000
Actuarial Accrued Liability (AAL)	\$48,582,000
Normal Cost	\$1,626,000

The level of liabilities is very dependent on the discount rate used in the calculations, as shown in this summary. The following section discusses discount rate selection.

### *Discount Rate Selection*

The discount rate can have a considerable impact on the magnitude of the liabilities, with lower discount rates resulting in higher liabilities. As guidance in selecting an appropriate discount rate, GASB states that the discount rate should be based on the long-term yield of investments used to finance the benefits.

For an unfunded plan or in the case where contributions are simply allocated to separate accounts, but still reside in general assets, it is appropriate to consider the return on the general County asset pool. However, if the County fully pre-funds contributions into a trust with a mix of asset classes (e.g., CalPERS' retiree health trust fund), a higher rate is more appropriate. This valuation assumes 4.50% and 7.75% rates for the unfunded and pre-funded portion of liability, which represent assumptions for the County asset pool and CalPERS trust fund, respectively. A blended rate is used when partial pre-funding is anticipated.

The County has requested this report based on the assumption that the County contribution is fully pre-funded, but the implicit subsidy is not pre-funded. Since the implicit subsidy will be discontinued after 2011, this results in the use of a blended rate of 7.24% before 2011 and the fully pre-funded rate of 7.75% thereafter.

### *Annual Required Contributions (ARC)*

As discussed above, the ARC can be developed using various methodologies. Selecting an appropriate method and amortization period for funding the liabilities is a balance between the County's ability to pay costs immediately and the long-term cost of borrowing.

## Executive Summary (cont.)

The following table summarizes the ARC under the methodologies provided in this report based on the blended discount rates:

Aggregate Method	\$5,620,000
Entry Age Normal Method	
30 year amortization	\$4,390,000
20 year amortization	\$5,158,000
10 year amortization	\$7,575,000

The difference in the cost methods is the period over which past service liabilities are spread. The aggregate method spreads past service liabilities over the future working lifetimes of active participants while the entry age normal method spreads past service liabilities over the specified amortization period. It should be noted that the Entry Age Normal method – level percent of pay is used to determine the ARC for CalPERS retirement plans.

### *Projected ARC*

As discussed in the previous section, the ARC amounts are determined based on a level percent of payroll. Thus, the ARC is expected to increase as payroll increases. The following table illustrates this based on the Entry Age Normal Method with 30 year amortization of the unfunded actuarial accrued liability and further assuming actual contributions are equal to the full ARC each year:

ARC	2007-2008	2008-2009	2009-2010
	\$4,390,000	\$4,533,000	\$4,680,000

### *Comparison to Prior Valuation Results*

The following table compares results to the prior valuation results, where the implicit subsidy was assumed to be ongoing:

	January 1, 2007	January 1, 2006
<b>Liabilities</b>		
Present Value of Benefits (PVB)	\$58,757,000	\$236,728,000
Actuarial Accrued Liability (AAL)	\$48,582,000	\$141,920,000
Normal Cost	\$1,626,000	\$10,264,000
<b>Plan Assets</b>	\$0	\$0
<b>ARC</b>		
Aggregate Method	\$5,620,000	\$19,186,000
Entry Age Normal Method		
30 year amortization	\$4,390,000	\$15,991,000
20 year amortization	\$5,158,000	\$18,377,000
10 year amortization	\$7,575,000	\$25,570,000

## Executive Summary (cont.)

The liability and ARC decreased considerably from the prior year, primarily due to the phase out of the implicit subsidy and the expectation of eventually pre-funding the County contribution. Other factors impacting results included:

- Overall healthcare costs increased less than assumed, resulting in liability gains.
- The total number of participants (active and retired) in the groups valued increased, increasing liabilities and annual costs.
- The liabilities, by their nature, grow each year as all participants get closer to receiving benefits and active participants accrue additional benefits.

It should be noted that employee groups from Special Districts (Waste, Parks, and Flood) were not included in the valuation results presented in this report, but will be provided in separate reports. These groups are included in the January 1, 2006 results shown above, although the costs are relatively small.

### *Implicit Subsidy Effect on Results*

The liabilities associated with the implicit subsidy are a notable portion of the total plan liabilities, although they have been reduced considerably due to the phase out of this benefit that will be complete by 2011. The following table shows the breakdown of liabilities by the two main sources:

	County Contributions	Implicit Subsidy	Total
<b>Liabilities</b>			
PVB	\$45,037,000	\$13,720,000	\$58,757,000
AAL	\$34,892,000	\$13,690,000	\$48,582,000
Normal Cost	\$1,595,000	\$31,000	\$1,626,000
<b>Plan Assets</b>	\$0	\$0	\$0
<b>ARC Range *</b>	\$3,580,000	\$810,000	\$4,390,000
	- \$5,868,000	- \$1,707,000	- \$7,575,000

\* The ARC range encompasses the variation in results due to the different funding methods and amortization periods.

### *Effect of Pre-Funding and the Discount Rate Impact*

As discussed previously, the discount rate has a considerable impact on the magnitude of liabilities. Although the County is currently anticipating fully pre-funding the liabilities once the implicit subsidy is phased out in 2011, the funding options and funding policy should be continually monitored to assure consistency with the County's overall financial policies.

## Executive Summary (cont.)

The following table compares the valuation results to the scenario where the County chooses not to pre-fund (4.50%):

	Valuation Results – 7.24% (until 2010) and 7.75% thereafter	No Pre-Funding (Pay-as-you-go) 4.50%
<b>Liabilities</b>		
Present Value of Benefits (PVB)	\$58,757,000	\$93,188,000
Actuarial Accrued Liability (AAL)	\$48,582,000	\$67,915,000
Normal Cost	\$1,626,000	\$3,074,000
<b>Plan Assets</b>	<b>\$0</b>	<b>\$0</b>
<b>ARC</b>		
Aggregate Method	\$5,620,000	\$7,448,000
Entry Age Normal Method		
30 year amortization	\$4,390,000	\$5,787,000
20 year amortization	\$5,158,000	\$6,918,000
10 year amortization	\$7,575,000	\$10,326,000

The remainder of the report provides details of results based on the blended discount rate scenario 7.24% discount rate until 2010 and 7.75% thereafter.

We understand the County intends to contribute the County Contribution pay-as-you-go amount plus an additional \$10 million in the first year. This is reflected in the GASB Reporting and Disclosure Information section.

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