

**City of Elk Grove
Actuarial Study of
Retiree Health Liabilities Under GASB 74/75
MEC Plan
Roll-forward Valuation
Valuation Date: July 1, 2016
Measurement Date: June 30, 2017**

*Prepared by:
Total Compensation Systems, Inc.*

Date: November 28, 2017

Table of Contents

PART I: EXECUTIVE SUMMARY	3
<u>A. INTRODUCTION</u>	3
<u>B. GENERAL FINDINGS</u>	4
<u>C. DESCRIPTION OF RETIREE BENEFITS</u>	5
<u>D. RECOMMENDATIONS.....</u>	5
PART II: BACKGROUND.....	7
<u>A. SUMMARY 7</u>	
<u>B. ACTUARIAL ACCRUAL</u>	7
PART III: LIABILITIES AND COSTS FOR RETIREE BENEFITS.....	9
<u>A. INTRODUCTION</u>	9
<u>B. LIABILITY FOR RETIREE BENEFITS.....</u>	9
<u>C. COST TO PREFUND RETIREE BENEFITS</u>	9
<u>1. Service Cost.....</u>	9
<u>2. Total OPEB Liability (TOL) and Net OPEB Liability (NOL).....</u>	10
PART V: RECOMMENDATIONS FOR FUTURE VALUATIONS.....	13
PART VI: APPENDICES	14
<u>APPENDIX A: MATERIALS USED FOR THIS STUDY</u>	14
<u>APPENDIX B: EFFECT OF ASSUMPTIONS USED IN CALCULATIONS</u>	15
<u>APPENDIX C: ACTUARIAL ASSUMPTIONS AND METHODS</u>	16
<u>APPENDIX D: DISTRIBUTION OF ELIGIBLE PARTICIPANTS BY AGE.....</u>	21
<u>APPENDIX E: GASB 74/75 ACCOUNTING ENTRIES AND DISCLOSURES</u>	22
<u>APPENDIX F: DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES</u>	27
<u>APPENDIX G: GLOSSARY OF RETIREE HEALTH VALUATION TERMS</u>	28

**City of Elk Grove
Actuarial Study of Retiree Health Liabilities**

PART I: EXECUTIVE SUMMARY

A. Introduction

City of Elk Grove engaged Total Compensation Systems, Inc. (TCS) to analyze liabilities associated with its current retiree health program as of June 30, 2017 (the measurement date). This valuation report is based on an earlier GASB 45 valuation as of July 1, 2016. We used standard actuarial “roll-forward” methodology to estimate the Total OPEB Liability (TOL) as of the measurement date. The Fiduciary Net Position (FNP) is based on the actual FNP at June 30, 2017. The numbers in this report are based on the assumption that they will first be used to determine accounting entries for the fiscal year ending June 30, 2017. If the report will first be used for a different fiscal year, the numbers may need to be adjusted accordingly.

This report does not reflect any cash benefits paid unless the retiree is required to provide proof that the cash benefits are used to reimburse the retiree’s cost of health benefits. Costs and liabilities attributable to cash benefits paid to retirees are reportable under applicable Governmental Accounting Standards Board (GASB) Standards.

This actuarial study is intended to serve the following purposes:

- To provide information to enable Elk Grove to manage the costs and liabilities associated with its retiree health benefits.
- To provide information to enable Elk Grove to communicate the financial implications of retiree health benefits to internal financial staff, the Council, employee groups and other affected parties.
- To provide information needed to comply with Governmental Accounting Standards Board Accounting Standards 74 and 75 related to "other postemployment benefits" (OPEB's).

Because this report was prepared in compliance with GASB 74 and 75, Elk Grove should not use this report for any other purpose without discussion with TCS. This means that any discussions with employee groups, governing Boards, etc. should be restricted to the implications of GASB 74 and 75 compliance.

We calculated the following estimates separately for active employees and retirees. As requested, we also separated results by the following employee classifications: General Employees, Management, Police Officers and Non-sworn Police. We estimated the following:

- the total liability created. (The actuarial present value of total projected benefit payments or APVPBP)
- ten years of projected benefit payments.
- the "total OPEB liability (TOL)." (The TOL is the portion of the APVPBP attributable to employees’ service prior to the measurement date.)
- the “net OPEB liability” (NOL). For plans funded through a trust, this represents the unfunded portion of the liability.
- the service cost (SC). This is the value of OPEB benefits earned for one year of service.

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- deferred inflows and outflows of resources attributable to the OPEB plan.
- “OPEB expense.” This is the amount recognized in accrual basis financial statements as the current period expense. The OPEB expense includes service cost, interest and certain changes in the OPEB liability, adjusted to reflect deferred inflows and outflows. This amount may need to be adjusted to reflect any contributions received after the Measurement Date.
- Amounts to support financial statement Note Disclosures and Required Supplementary Information (RSI) schedules.

We summarized the data used to perform this study in Appendix A. No effort was made to verify this information beyond brief tests for reasonableness and consistency.

All cost and liability figures contained in this study are estimates of future results. Future results can vary dramatically and the accuracy of estimates contained in this report depends on the actuarial assumptions used. Service costs and liabilities could easily vary by 10 - 20% or more from estimates contained in this report.

B. General Findings

We estimate the "pay-as-you-go" cost of providing retiree health benefits in the year beginning July 1, 2016 to be \$34,150 (see Section IV.A.). The “pay-as-you-go” cost is the cost of benefits for current retirees.

For current employees, the value of benefits "accrued" in the year beginning July 1, 2017 (the service cost) is \$172,842. This service cost would increase each year based on covered payroll. Had Elk Grove begun accruing retiree health benefits when each current employee and retiree was hired, a substantial liability would have accumulated. We estimate the amount that would have accumulated at June 30, 2017 to be \$2,777,214. This amount is called the "Total OPEB Liability" (TOL). Elk Grove has set aside funds to cover retiree health liabilities in a GASB 75 qualifying trust. The Fiduciary Net Position of this trust at June 30, 2017 was \$2,647,198. This leaves a Net OPEB Liability (NOL) Of \$130,016.

Based on the information we were provided, the OPEB Expense for the fiscal year ending June 30, 2017 is \$179,209. As noted in this report adjustments may be needed – particularly if the reporting date is not the same as the measurement date.

We based all of the above estimates on employees as of March, 2016. Over time, liabilities and cash flow will vary based on the number and demographic characteristics of employees and retirees.

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C. Description of Retiree Benefits

Following is a description of the current retiree benefit plan:

	<u>General</u>	<u>Management</u>	<u>Police</u>	<u>Non Sworn Police</u>
Benefit types provided	Medical only	Medical only	Medical only	Medical only
Duration of Benefits	Lifetime	Lifetime	Lifetime	Lifetime
Required Service	5 years	5 years	5 years	5 years
Minimum Age	50	50	50	50
Dependent Coverage	Yes	Yes	Yes	Yes
City Contribution %	100%	100%	100%	100%
City Cap	\$128 per month	\$128 per month	\$128 per month	\$128 per month

D. Recommendations

It is outside the scope of this report to make specific recommendations of actions Elk Grove should take to manage the liability created by the current retiree health program. Total Compensation Systems, Inc. can assist in identifying and evaluating options once this report has been studied. The following recommendations are intended only to allow the City to get more information from this and future studies. Because we have not conducted a comprehensive administrative audit of Elk Grove's practices, it is possible that Elk Grove is already complying with some or all of our recommendations.

- We recommend that Elk Grove maintain an inventory of all benefits and services provided to retirees – whether contractually or not and whether retiree-paid or not. For each, Elk Grove should determine whether the benefit is material and subject to GASB 74 and/or 75.
- We recommend that Elk Grove conduct a study whenever events or contemplated actions significantly affect present or future liabilities, but no less frequently than every two years, as required under GASB 74/75.
- Under GASB 75, it is important to isolate the cost of retiree health benefits. Elk Grove should have all premiums, claims and expenses for retirees separated from active employee premiums, claims, expenses, etc. To the extent any retiree benefits are made available to retirees over the age of 65 – ***even on a retiree-pay-all basis*** – all premiums, claims and expenses for post-65 retiree coverage should be segregated from those for pre-65 coverage. Furthermore, Elk Grove should arrange for the rates or prices of all retiree benefits to be set on what is expected to be a self-sustaining basis.
- Elk Grove should establish a way of designating employees as eligible or ineligible for future OPEB benefits. Ineligible employees can include those in ineligible job classes; those hired after a designated date restricting eligibility; those who, due to their age at hire cannot qualify for City-paid OPEB benefits; employees who exceed the termination age for OPEB benefits, etc.
- Several assumptions were made in estimating costs and liabilities under Elk Grove's retiree health program. Further studies may be desired to validate any assumptions where there is any doubt that the assumption is appropriate. (See Appendices B and C for a list of assumptions and concerns.) For example, Elk Grove should maintain a retiree database that

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includes – in addition to date of birth, gender and employee classification – retirement date and (if applicable) dependent date of birth, relationship and gender. It will also be helpful for Elk Grove to maintain employment termination information – namely, the number of OPEB-eligible employees in each employee class that terminate employment each year for reasons other than death, disability or retirement.

Respectfully submitted,



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PART II: BACKGROUND

A. Summary

Accounting principles provide that the cost of retiree benefits should be “accrued” over employees' working lifetime. For this reason, the Governmental Accounting Standards Board (GASB) issued in June of 2015 Accounting Standards 74 and 75 for retiree health benefits. These standards apply to all public employers that pay any part of the cost of retiree health benefits for current or future retirees (including early retirees), whether they pay directly or indirectly (via an “implicit rate subsidy”),

B. Actuarial Accrual

To actuarially accrue retiree health benefits requires determining the amount to expense each year so that the liability accumulated at retirement is, on average, sufficient (with interest) to cover all retiree health expenditures without the need for additional expenses. There are many different ways to determine the annual accrual amount. The calculation method used is called an “actuarial cost method.”

The actuarial cost method mandated by GASB 75 is the “entry age actuarial cost method”. Under this method, there are two components of actuarial cost – a “service cost” (SC) and the “Total OPEB Liability” (TOL). GASB 75 allows certain changes in the TOL to be deferred (i.e. deferred inflows and outflows of resources).

The service cost can be thought of as the value of the benefit earned each year if benefits are accrued during the working lifetime of employees. Under the entry age actuarial cost method, the actuary determines the annual amount needing to be expensed from hire until retirement to fully accrue the cost of retiree health benefits. This amount is the service cost. Under GASB 75, the service cost is calculated to be a level percentage of each employee's projected pay.

The service cost is determined using several key assumptions:

- The current *cost of retiree health benefits* (often varying by age, Medicare status and/or dependent coverage). The higher the current cost of retiree benefits, the higher the service cost.
- The “*trend*” rate at which retiree health benefits are expected to increase over time. A higher trend rate increases the service cost. A “cap” on City contributions can reduce trend to zero once the cap is reached thereby dramatically reducing service costs.
- *Mortality rates* varying by age and sex. (Unisex mortality rates are not often used as individual OPEB benefits do not depend on the mortality table used.) If employees die prior to retirement, past contributions are available to fund benefits for employees who live to retirement. After retirement, death results in benefit termination or reduction. Although higher mortality rates reduce service costs, the mortality assumption is not likely to vary from employer to employer.
- *Employment termination rates* have the same effect as mortality inasmuch as higher termination rates reduce service costs. Employment termination can vary considerably between public agencies.
- The *service requirement* reflects years of service required to earn full or partial retiree benefits. While a longer service requirement reduces costs, cost reductions are not usually substantial unless the service period exceeds 20 years of service.

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- **Retirement rates** determine what proportion of employees retire at each age (assuming employees reach the requisite length of service). Retirement rates often vary by employee classification and implicitly reflect the minimum retirement age required for eligibility. Retirement rates also depend on the amount of pension benefits available. Higher retirement rates increase service costs but, except for differences in minimum retirement age, retirement rates tend to be consistent between public agencies for each employee type.
- **Participation rates** indicate what proportion of retirees are expected to elect retiree health benefits if a significant retiree contribution is required. Higher participation rates increase costs.
- The **discount rate** estimates investment earnings for assets earmarked to cover retiree health benefit liabilities. The discount rate depends on the nature of underlying assets for funded plans. The rate used for a funded plan is the real rate of return expected for plan assets plus long term inflation assumption. For an unfunded plan, the discount rate is based on an index of 20 year General Obligation municipal bonds. For partially funded plans, the discount rate is a blend of the funded and unfunded rates.

The assumptions listed above are not exhaustive, but are the most common assumptions used in actuarial cost calculations. If all actuarial assumptions are exactly met and an employer expensed the service cost every year for all past and current employees and retirees, a sizeable liability would have accumulated (after adding interest and subtracting retiree benefit costs). The liability that would have accumulated is called the Total OPEB Liability (TOL). The excess of TOL over the value of plan assets is called the Net OPEB Liability (NOL). Under GASB 74 and 75, in order for assets to count toward offsetting the TOL, the assets have to be held in an irrevocable trust that is safe from creditors and can only be used to provide OPEB benefits to eligible participants.

The total OPEB liability (TOL) can arise in several ways - e.g., as a result of plan changes or changes in actuarial assumptions. TOL can also arise from actuarial gains and losses. Actuarial gains and losses result from differences between actuarial assumptions and actual plan experience.

Under GASB 74 and 75, a portion of actuarial gains and losses can be deferred as follows:

- Investment gains and losses can be deferred five years
- Experience gains and losses can be deferred over the expected average remaining service lives (EARSL) of plan participants. In calculating the EARSL, terminated employees (primarily retirees) are considered to have a working lifetime of zero. This often makes the EARSL quite short.
- Liability changes resulting from changes in economic and demographic assumptions are also deferred based on the average working lifetime
- Liability changes resulting from plan changes, for example, cannot be deferred.

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PART III: LIABILITIES AND COSTS FOR RETIREE BENEFITS

A. Introduction.

The liability for OPEB benefits was calculated in the valuation as of July 1, 2016 and the methodology used was described in our GASB 45 valuation report dated July 27, 2016. In Part III, we show the tables included in our July 27, 2016 valuation report and provide details of our roll-forward valuation.

We summarized actuarial assumptions used for this study in Appendix C.

B. Liability for Retiree Benefits.

Below is the actuarial present value of projected benefit payments (APVPBP) table presented in our July 27, 2016 valuation report.

Actuarial Present Value of Projected Benefit Payments at July 1, 2016

	<i>Total</i>	<i>General Employees</i>	<i>Management</i>	<i>Police Officers</i>	<i>Non-sworn Police</i>
Active: Pre-65	\$1,037,660	\$292,851	\$23,037	\$557,908	\$163,864
Post-65	\$2,424,012	\$835,202	\$73,910	\$1,069,817	\$445,083
Subtotal	\$3,461,672	\$1,128,053	\$96,947	\$1,627,725	\$608,947
Retiree: Pre-65	\$215,112	\$12,917	\$15,679	\$156,922	\$29,594
Post-65	\$461,102	\$147,677	\$45,726	\$197,472	\$70,227
Subtotal	\$676,214	\$160,594	\$61,405	\$354,394	\$99,821
Grand Total	\$4,137,886	\$1,288,647	\$158,352	\$1,982,119	\$708,768
Subtotal Pre-65	\$1,252,772	\$305,768	\$38,716	\$714,830	\$193,458
Subtotal Post-65	\$2,885,114	\$982,879	\$119,636	\$1,267,289	\$515,310

C. Cost to Prefund Retiree Benefits

1. Service Cost

Below is the service cost table included in our July 27, 2016 valuation report. This service cost is used in calculating the pension expense.

Service Cost Year Beginning July 1, 2016

	<i>Total</i>	<i>General Employees</i>	<i>Management</i>	<i>Police Officers</i>	<i>Non-sworn Police</i>
# of Employees	299	108	8	129	54
Per Capita Service Cost					
Pre-65 Benefit	N/A	\$113	\$151	\$226	\$103
Post-65 Benefit	N/A	\$394	\$548	\$456	\$351
First Year Service Cost					
Pre-65 Benefit	\$48,128	\$12,204	\$1,208	\$29,154	\$5,562
Post-65 Benefit	\$124,714	\$42,552	\$4,384	\$58,824	\$18,954
Total	\$172,842	\$54,756	\$5,592	\$87,978	\$24,516

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2. Total OPEB Liability (TOL) and Net OPEB Liability (NOL)

The table below shows the TOL included in the July 27, 2016 valuation report. This TOL is used as the beginning of year TOL to roll forward the TOL to June 30, 2017.

Total OPEB Liability (TOL) and Net OPEB Liability (NOL) as of July 1, 2016

	<i>Total</i>	<i>General Employees</i>	<i>Management</i>	<i>Police Officers</i>	<i>Non-sworn Police</i>
Active: Pre-65	\$567,122	\$176,936	\$13,405	\$266,302	\$110,479
Active: Post-65	\$1,214,597	\$431,039	\$38,954	\$481,444	\$263,160
Subtotal	\$1,781,719	\$607,975	\$52,359	\$747,746	\$373,639
Retiree: Pre-65	\$215,112	\$12,917	\$15,679	\$156,922	\$29,594
Retiree: Post-65	\$461,102	\$147,677	\$45,726	\$197,472	\$70,227
Subtotal	\$676,214	\$160,594	\$61,405	\$354,394	\$99,821
Subtotal: Pre-65	\$782,234	\$189,853	\$29,084	\$423,224	\$140,073
Subtotal: Post-65	\$1,675,699	\$578,716	\$84,680	\$678,916	\$333,387
Total OPEB Liability (TOL)	\$2,457,933	\$768,569	\$113,764	\$1,102,140	\$473,460
Fiduciary Net Position as of July 1, 2016	\$2,253,378				
Net OPEB Liability (NOL)	\$204,555				

In order to determine the June 30, 2017 NOL, we used a “roll-forward” technique for the TOL. The FNP is based on the actual June 30, 2017 FNP. The following table shows the results of the roll-forward. Elk Grove should restate its June 30, 2016 NOL accordingly.

Changes in Net OPEB Liability as of June 30, 2017

	<i>TOL</i>	<i>FNP</i>	<i>NOL</i>
Balance at July 1, 2016	\$2,457,933	\$2,253,378	\$204,555
Service Cost	\$172,842	\$0	\$172,842
Interest on TOL	\$152,480	\$0	\$152,480
Employer Contributions	\$0	\$200,000	(\$200,000)
Employee Contributions	\$0	\$0	\$0
Expected Investment Income	\$0	\$140,778	(\$140,778)
Investment Gains/Losses	\$0	\$67,185	(\$67,185)
Administrative Expense	\$0	(\$8,102)	\$8,102
Benefit Payments	(\$6,041)	(\$6,041)	\$0
Other	\$0	\$0	\$0
Net Change during 2016-17	\$319,281	\$393,820	(\$74,539)
Balance at June 30, 2017 *	\$2,777,214	\$2,647,198	\$130,016

* May include a slight rounding error.

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3. OPEB Expense

Under GASB 74 and 75, OPEB expense includes service cost, interest cost, change in TOL due to plan changes; all adjusted for deferred inflows and outflows. Following is the pension expense for the fiscal year ending June 30, 2017. The OPEB expense shown below is considered to be preliminary because there can be employer specific deferred items (e.g., contributions made after the measurement date, and active employee contributions toward the OPEB plan).

OPEB Expense Fiscal Year Ending June 30, 2017

	<i>Total</i>
Service Cost	\$172,842
Interest on Total OPEB Liability (TOL)	\$152,480
Employee Contributions	\$0
Recognized Actuarial Gains/Losses	\$0
Recognized Assumption Changes	\$0
Expected Investment Income	(\$140,778)
Recognized Investment Gains/Losses	(\$13,437)
Contributions After Measurement Date*	\$0
Liability Change Due to Benefit Changes	\$0
Administrative Expense	\$8,102
OPEB Expense**	<u>\$179,209</u>

* Should be added by Elk Grove if reporting date is after the measurement date.

** May include a slight rounding error.

The above OPEB expense does not include an estimated \$200,000 in employer contributions.

4. Deferred Inflows and Outflows

Certain types of TOL changes are subject to deferral, as are investment gains/losses. Appendix F provides details of any deferred inflows and/or outflows included in the pension expense.

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PART IV: "PAY AS YOU GO" FUNDING OF RETIREE BENEFITS

We used the actuarial assumptions shown in Appendix C to project the City's ten year retiree benefit outlay, including any implicit rate subsidy. Because these cost estimates reflect average assumptions applied to a relatively small number of employees, estimates for individual years are **certain** to be *in*accurate. However, these estimates show the size of cash outflow.

The following table shows a projection of annual amounts needed to pay the City's share of retiree health costs, including any implicit rate subsidy, that was included in the July 27, 2016 valuation report.

<i>Year Beginning July 1</i>	<i>Total</i>	<i>General Employees</i>	<i>Management</i>	<i>Police Officers</i>	<i>Non-sworn Police</i>
2016	\$34,150	\$9,914	\$3,171	\$15,954	\$5,111
2017	\$37,488	\$11,003	\$3,405	\$17,253	\$5,827
2018	\$43,647	\$13,565	\$3,766	\$19,255	\$7,061
2019	\$50,343	\$16,353	\$4,182	\$21,236	\$8,572
2020	\$57,907	\$19,354	\$4,570	\$23,607	\$10,376
2021	\$66,137	\$22,854	\$4,925	\$25,902	\$12,456
2022	\$74,708	\$26,575	\$5,390	\$28,192	\$14,551
2023	\$84,323	\$30,775	\$5,812	\$30,873	\$16,863
2024	\$97,129	\$35,358	\$6,341	\$35,903	\$19,527
2025	\$113,839	\$40,291	\$6,914	\$44,204	\$22,430

PART V: RECOMMENDATIONS FOR FUTURE VALUATIONS

To effectively manage benefit costs, an employer must periodically examine the existing liability for retiree benefits as well as future annual expected premium costs. GASB 74/75 require biennial valuations. In addition, a valuation should be conducted whenever plan changes, changes in actuarial assumptions or other employer actions are likely to cause a material change in accrual costs and/or liabilities.

Following are examples of actions that could trigger a new valuation.

- An employer should perform a valuation whenever the employer considers or puts in place an early retirement incentive program.
- An employer should perform a valuation whenever the employer adopts a retiree benefit plan for some or all employees.
- An employer should perform a valuation whenever the employer considers or implements changes to retiree benefit provisions or eligibility requirements.
- An employer should perform a valuation whenever the employer introduces or changes retiree contributions.
- An employer should perform a valuation whenever the employer forms a qualifying trust or changes its investment policy.
- An employer should perform a valuation whenever the employer adds or terminates a group of participants that constitutes a significant part of the covered group.

We recommend Elk Grove take the following actions to ease future valuations.

- We have used our training, experience and information available to us to establish the actuarial assumptions used in this valuation. We have no information to indicate that any of the assumptions do not reasonably reflect future plan experience. However, the City should review the actuarial assumptions in Appendix C carefully. If the City has any reason to believe that any of these assumptions do not reasonably represent the expected future experience of the retiree health plan, the City should engage in discussions or perform analyses to determine the best estimate of the assumption in question.

PART VI: APPENDICES

APPENDIX A: MATERIALS USED FOR THIS STUDY

We relied on the following materials to complete this study.

- We used paper reports and digital files containing employee demographic data from the City personnel records.
- We used relevant sections of collective bargaining agreements provided by the City.

APPENDIX B: EFFECT OF ASSUMPTIONS USED IN CALCULATIONS

While we believe the estimates in this study are reasonable overall, it was necessary for us to use assumptions which inevitably introduce errors. We believe that the errors caused by our assumptions will not materially affect study results. If the City wants more refined estimates for decision-making, we recommend additional investigation.

APPENDIX C: ACTUARIAL ASSUMPTIONS AND METHODS

Following is a summary of actuarial assumptions and methods used in this study. The City should carefully review these assumptions and methods to make sure they reflect the City's assessment of its underlying experience. It is important for Elk Grove to understand that the appropriateness of all selected actuarial assumptions and methods are Elk Grove's responsibility. Unless otherwise disclosed in this report, TCS believes that all methods and assumptions are within a reasonable range based on the provisions of GASB 74 and 75, applicable actuarial standards of practice, Elk Grove's actual historical experience, and TCS's judgment based on experience and training.

ACTUARIAL METHODS AND ASSUMPTIONS:

ACTUARIAL COST METHOD: GASB 74/75 require use of the entry age actuarial cost method.

Entry age is based on the age at hire for eligible employees. The attribution period is determined as the difference between the expected retirement age and the age at hire. The APVPBP and present value of future service costs are determined on an employee by employee basis and then aggregated.

To the extent that different benefit formulas apply to different employees of the same class, the service cost is based on the benefit plan applicable to the most recently hired employees (including future hires if a new benefit formula has been agreed to and communicated to employees). This greatly simplifies administration and accounting; as well as resulting in the correct service cost for new hires.

SUBSTANTIVE PLAN: As required under GASB 74 and 75, we based the valuation on the substantive plan. The formulation of the substantive plan was based on a review of written plan documents as well as historical information provided by Elk Grove regarding practices with respect to employer and employee contributions and other relevant factors.

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ECONOMIC ASSUMPTIONS:

Economic assumptions are set under the guidance of Actuarial Standard of Practice 27 (ASOP 27). Among other things, ASOP 27 provides that economic assumptions should reflect a consistent underlying rate of general inflation. For that reason, we show our assumed long-term inflation rate below.

INFLATION: We assumed 2.75% per year used for pension purposes. Actuarial standards require using the same rate for OPEB that is used for pension.

INVESTMENT RETURN / DISCOUNT RATE: We assumed 6% per year net of expenses. This is based on assumed long-term return on plan assets assuming 100% funding through PARS. We used the “Building Block Method”. (See Appendix E, Paragraph 53 for more information).

TREND: We assumed 4% per year. Our long-term trend assumption is based on the conclusion that, while medical trend will continue to be cyclical, the average increase over time cannot continue to outstrip general inflation by a wide margin. Trend increases in excess of general inflation result in dramatic increases in unemployment, the number of uninsured and the number of underinsured. These effects are nearing a tipping point which will inevitably result in fundamental changes in health care finance and/or delivery which will bring increases in health care costs more closely in line with general inflation. We do not believe it is reasonable to project historical trend vs. inflation differences several decades into the future.

PAYROLL INCREASE: We assumed 2.75% per year. Since benefits do not depend on salary (as they do for pensions), using an aggregate payroll assumption for the purpose of calculating the service cost results in a negligible error.

FIDUCIARY NET POSITION (FNP): The following table shows the beginning and ending FNP numbers that were provided by Elk Grove.

Fiduciary Net Position as of June 30, 2017

	<u>06/30/2016</u>	<u>06/30/2017</u>
Cash and Equivalents	\$0	\$0
Contributions Receivable	\$0	\$0
Total Investments	\$2,253,378	\$2,647,198
Capital Assets	\$0	\$0
Total Assets	<u>\$2,253,378</u>	<u>\$2,647,198</u>
Benefits Payable	<u>\$0</u>	<u>\$0</u>
Fiduciary Net Position	<u>\$2,253,378</u>	<u>\$2,647,198</u>

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NON-ECONOMIC ASSUMPTIONS:

Economic assumptions are set under the guidance of Actuarial Standard of Practice 35 (ASOP 35). See Appendix E, Paragraph 52 for more information.

MORTALITY

<i>Employee Type</i>	<i>Mortality Tables</i>
Police	2014 CalPERS Mortality for Active Safety Employees
Miscellaneous	2014 CalPERS Active Mortality for Miscellaneous Employees

RETIREMENT RATES

<i>Employee Type</i>	<i>Retirement Rate Tables</i>
Sworn Police	Hired before 2013: 2009 CalPERS 3% @50 Rates for Sworn Police Hired after 2012: 2009 CalPERS 3% @50 Rates for Sworn Police
Miscellaneous	Hired before 2013: 2009 CalPERS 2.7% @55 Rates for Miscellaneous Employees Hired after 2012: 2009 CalPERS 2.7% @55 Rates for Miscellaneous Employees

SERVICE REQUIREMENT

<i>Employee Type</i>	<i>Service Requirement Tables</i>
Police	100% at 5 Years of Service
Miscellaneous	100% at 5 Years of Service

COSTS FOR RETIREE COVERAGE

The costs below are those used in the July 27, 2016 valuation for this roll-forward, we used increased costs shown below by the applicable trend rate.

Actuarial Standard of Practice 6 (ASOP 6) provides that, as a general rule, retiree costs should be based on actual claim costs or age-adjusted premiums. This is true even for many medical plans that are commonly considered to be “community-rated.” However, ASOP 6 contains a provision – specifically section 3.7.7(c) – that allows use of unadjusted premiums in certain circumstances.

Because the section 3.7.7(c) exception is new, there is not a consensus among practicing actuaries regarding the specific circumstances under which a section 3.7.7(c) exception may be invoked. It is my opinion that the section 3.7.7(c)(4) exception allows use of unadjusted premium for PEMHCA agencies if certain conditions are met. Other actuaries have taken the position that ASOP 6 does not explicitly allow use of unadjusted premium for any agencies participating in the CalPERS medical plan.

Prior to the most recent ASOP 6 revision, there was general agreement that ASOP 6 allowed use of unadjusted premium as a retiree cost basis for PEMHCA agencies (under section 3.4.5 of the prior version of ASOP 6). Since there have been no changes to the CalPERS medical plan, use of unadjusted premium must still be viewed as appropriate actuarial practice to the extent that it was under the prior version of ASOP 6. That means that if the current ASOP 6 section 3.7.7(c)(4) exception is not deemed to explicitly allow use of unadjusted premium as a retiree cost basis for Elk Grove, then it would be allowable as a “deviation.”

While I am confident that ASOP 6 section 3.7.7(c)(4) will ultimately be found to explicitly allow use of unadjusted premium as a retiree cost basis for most PEMHCA agencies, I cannot be certain that this will be the case if and when this issue is fully reviewed. Therefore, I am including disclosure information required for a “deviation” so that the valuation will not need to be revised in the event section 3.7.7(c)(4) should be found not to explicitly allow use of unadjusted premium. Following is the disclosure information that is required should a deviation be necessary.

Use of *age-adjusted* premium for the CalPERS medical plan results in an overstatement of Elk Grove’s OPEB

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Expense and Total OPEB Liability (TOL) to the extent that Elk Grove continues to participate in the CalPERS medical plan AND that the rate structure of the CalPERS medical plan continues in its current form (i.e. with no rate distinction between active employees and retirees). In addition to the overstatement of OPEB costs and liabilities, Elk Grove's policy of funding OPEB obligations could lead to an inability of Elk Grove to recover overfunded assets. It is important to note that, should Elk Grove leave the CalPERS medical plan, the subsequent plan may not qualify to use unadjusted premium rates. In this event, leaving the CalPERS medical plan would be comparable to a significant change in plan terms and would likely require a new valuation.

Following are the criteria we applied to Elk Grove to determine that it is reasonable to assume that Elk Grove's future participation in PEMHCA is likely and that the CalPERS medical program as well as its premium structure are sustainable. (We also have an extensive white paper on this subject that provides a basis for our rationale entirely within the context of ASOP 6. We will make this white paper available upon request.)

The City participates in the CalPERS medical program. We have performed the required evaluation of the CalPERS medical program and we have determined that there is sufficient evidence to apply the 3.7.7(c)(4) exception. Following are details regarding the evaluation based on the criteria we have set:

- **Plan qualifies as a “pooled health plan.”** ASOP 6 defines a “pooled health plan” as one in which premiums are based at least in part on the claims experience of groups other than the one being valued.” Since CalPERS rates are the same for all employers in each region, rates are clearly based on the experience of many groups.
- **Rates not based to any extent on the agency’s claim experience.** As mentioned above, rates are the same for all participating employers regardless of claim experience or size.
- **Rates not based to any extent on the agency’s demographics.** As mentioned above, rates are the same for all participating employers regardless of demographics.
- **No refunds or charges based on the agency’s claim experience or demographics.** The terms of operation of the CalPERS program are set by statute and there is no provision for any refunds and charges that vary from employer to employer for any reason. The only charges are uniform administrative charges.
- **Plan in existence 20 or more years.** Enabling legislation to allow “contracting agencies” to participate in the CalPERS program was passed in 1967. The CalPERS medical plan has been successfully operating for almost 50 years. As far back as we can obtain records, the rating structure has been consistent, with the only difference having been a move to regional rating which is unrelated to age-adjusted rating.
- **No recent large increases or decreases in the number of participating plans or enrollment.** The CalPERS medical plan has shown remarkably stable enrollment. In the past 10 years, there has been small growth in the number of employers in most years – with the maximum being a little over 2% and a very small decrease in one year. Average year over year growth in the number of employers over the last 10 years has been about 0.75% per year. Groups have been consistently leaving the CalPERS medical plan while other groups have been joining with no disruption to its stability.
- **Agency is not expecting to leave plan in foreseeable future.** The City does not plan to leave CalPERS at present.

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- **No indication the plan will be discontinued.** We are unaware of anything that would cause the CalPERS medical plan to cease or to significantly change its operation in a way that would affect this determination.
- **The agency does not represent a large part of the pool.** The City is in the CalPERS Sacramento Area region. Based on the information we have, the City constitutes no more than 1.5% of the Sacramento Area pool. In our opinion, this is not enough for the City to have a measurable effect on the rates or viability of the Sacramento Area pool.

Retiree liabilities are based on actual retiree costs. Liabilities for active participants are based on the first year costs shown below. Subsequent years' costs are based on first year costs adjusted for trend and limited by any City contribution caps.

<i>Employee Type</i>	<i>Future Retirees Pre-65</i>	<i>Future Retirees Post-65</i>
General Employees	\$1,566	\$1,566
Management	\$1,566	\$1,566
Non-sworn Police	\$1,566	\$1,566
Police Officers	\$1,566	\$1,566

PARTICIPATION RATES

<i>Employee Type</i>	<i><65 Non-Medicare Participation %</i>	<i>65+ Medicare Participation %</i>
Police	70%	70%
Miscellaneous	70%	70%

TURNOVER

<i>Employee Type</i>	<i>Turnover Rate Tables</i>
Police	2009 CalPERS Rates for Sworn Police
Miscellaneous	2009 CalPERS Turnover for Miscellaneous Employees

SPOUSE PREVALENCE

To the extent not provided and when needed to calculate benefit liabilities, 80% of retirees assumed to be married at retirement. After retirement, the percentage married is adjusted to reflect mortality.

SPOUSE AGES

To the extent spouse dates of birth are not provided and when needed to calculate benefit liabilities, female spouse assumed to be three years younger than male.

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APPENDIX D: DISTRIBUTION OF ELIGIBLE PARTICIPANTS BY AGE

ELIGIBLE ACTIVE EMPLOYEES

<i>Age</i>	<i>Total</i>	<i>General Employees</i>	<i>Management</i>	<i>Police Officers</i>	<i>Non-sworn Police</i>
Under 25	13	3	0	7	3
25-29	22	5	0	12	5
30-34	42	18	0	18	6
35-39	47	22	0	16	9
40-44	65	18	4	35	8
45-49	59	20	1	26	12
50-54	35	14	1	14	6
55-59	9	5	1	0	3
60-64	5	1	1	1	2
65 and older	2	2	0	0	0
Total	299	108	8	129	54

ELIGIBLE RETIREES

<i>Age</i>	<i>Total</i>	<i>General Employees</i>	<i>Management</i>	<i>Police Officers</i>	<i>Non-sworn Police</i>
Under 50	2	0	0	2	0
50-54	5	0	0	5	0
55-59	8	1	1	3	3
60-64	2	1	1	0	0
65-69	2	2	0	0	0
70-74	2	2	0	0	0
75-79	0	0	0	0	0
80-84	0	0	0	0	0
85-89	0	0	0	0	0
90 and older	0	0	0	0	0
Total	21	6	2	10	3

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APPENDIX E: GASB 74/75 ACCOUNTING ENTRIES AND DISCLOSURES

This report does not necessarily include the entire accounting values. As mentioned earlier, there are certain deferred items that are employer-specific. The City should consult with its auditor if there are any questions about what, if any, adjustments may be appropriate.

GASB 74/75 include a large number of items that should be included in the Note Disclosures and Required Supplementary Information (RSI) Schedules. Many of these items are outside the scope of the actuarial valuation. However, following is information to assist the City in complying with GASB 74/75 disclosure requirements:

Paragraph 50: **Information about the OPEB Plan**

Most of the information about the OPEB plan should be supplied by Elk Grove. Following is information to help fulfill Paragraph 50 reporting requirements.

50.c: Following is a table of plan participants

	Number of Participants
Inactive Employees Receiving Benefits	21
Inactive Employees Entitled to But Not Receiving Benefits*	0
Participating Active Employees	299
Total Number of participants	320

*We were not provided with information about any terminated, vested employees

Paragraph 51: **Significant Assumptions and Other Inputs**

shown in Appendix C.

Paragraph 52: **Information Related to Assumptions and Other Inputs**

The following information is intended to assist Elk Grove in complying with the requirements of Paragraph 52.

52.b: Mortality Assumptions Following are the tables the mortality assumptions are based upon. Inasmuch as these tables are based on appropriate populations, and that these tables are used for pension purposes, we believe these tables to be the most appropriate for the valuation.

Mortality Table Disclosure	2014 CalPERS Active Mortality for Miscellaneous Employees The mortality assumptions are based on the 2014 CalPERS Active Mortality for Miscellaneous Employees table created by CalPERS. CalPERS periodically studies mortality for participating agencies and establishes mortality tables that are modified versions of commonly used tables. This table incorporates mortality projection as deemed appropriate based on CalPERS analysis.
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Mortality Table	2014 CalPERS Mortality for Retired safety Employees
Disclosure	The mortality assumptions are based on the 2014 CalPERS Mortality for Retired safety Employees table created by CalPERS. CalPERS periodically studies mortality for participating agencies and establishes mortality tables that are modified versions of commonly used tables. This table incorporates mortality projection as deemed appropriate based on CalPERS analysis.
Mortality Table	2014 CalPERS Mortality for Active Safety Employees
Disclosure	The mortality assumptions are based on the 2014 CalPERS Mortality for Active Safety Employees table created by CalPERS. CalPERS periodically studies mortality for participating agencies and establishes mortality tables that are modified versions of commonly used tables. This table incorporates mortality projection as deemed appropriate based on CalPERS analysis.
Mortality Table	2014 CalPERS Retiree Mortality for Miscellaneous Employees
Disclosure	The mortality assumptions are based on the 2014 CalPERS Retiree Mortality for Miscellaneous Employees table created by CalPERS. CalPERS periodically studies mortality for participating agencies and establishes mortality tables that are modified versions of commonly used tables. This table incorporates mortality projection as deemed appropriate based on CalPERS analysis.

52.c: Experience Studies Following are the tables the retirement and turnover assumptions are based upon. Inasmuch as these tables are based on appropriate populations, and that these tables are used for pension purposes, we believe these tables to be the most appropriate for the valuation.

Retirement Tables

Retirement Table	2009 CalPERS 2.0% @60 Rates for Miscellaneous Employees
Disclosure	The retirement assumptions are based on the 2009 CalPERS 2.0% @60 Rates for Miscellaneous Employees table created by CalPERS. CalPERS periodically studies the experience for participating agencies and establishes tables that are appropriate for each pool.
Retirement Table	2009 CalPERS 2.7% @55 Rates for Miscellaneous Employees
Disclosure	The retirement assumptions are based on the 2009 CalPERS 2.7% @55 Rates for Miscellaneous Employees table created by CalPERS. CalPERS periodically studies the experience for participating agencies and establishes tables that are appropriate for each pool.

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Retirement Table	2009 CalPERS 3% @55 Rates for Sworn Police
Disclosure	The retirement assumptions are based on the 2009 CalPERS 3% @55 Rates for Sworn Police table created by CalPERS. CalPERS periodically studies the experience for participating agencies and establishes tables that are appropriate for each pool.

Retirement Table	2009 CalPERS 3% @50 Rates for Sworn Police
Disclosure	The retirement assumptions are based on the 2009 CalPERS 3% @50 Rates for Sworn Police table created by CalPERS. CalPERS periodically studies the experience for participating agencies and establishes tables that are appropriate for each pool.

Turnover Tables

Turnover Table	2009 CalPERS Turnover for Miscellaneous Employees
Disclosure	The turnover assumptions are based on the 2009 CalPERS Turnover for Miscellaneous Employees table created by CalPERS. CalPERS periodically studies the experience for participating agencies and establishes tables that are appropriate for each pool.

Turnover Table	2009 CalPERS Rates for Sworn Police
Disclosure	The turnover assumptions are based on the 2009 CalPERS Rates for Sworn Police table created by CalPERS. CalPERS periodically studies the experience for participating agencies and establishes tables that are appropriate for each pool.

For other assumptions, we use actual plan provisions and plan data.

52.d: The alternative measurement method was not used in this valuation.

52.e: NOL Using alternative trend assumptions The following table shows the Net OPEB Liability with a health care cost trend rate 1% higher and 1% lower than assumed in the valuation.

	Trend 1% Lower	Valuation Trend	Trend 1% Higher
Net OPEB Liability	(\$321,600)	\$130,016	\$693,139

Paragraph 53:

Discount Rate

The following information is intended to assist Elk Grove to comply with Paragraph 53 requirements.

53.a: A discount rate of 6% was used in the valuation.

53.b: We assumed that contributions would be sufficient to fully fund the obligation over a period not to exceed 30 years.

53.c: We used historic 30 year real rates of return for each asset class along with our

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fully fund the obligation over a period not to exceed 30 years.
57.d: We are not aware that there are any statutorily or contractually established contribution requirements.

Paragraph 58:

Actuarially Determined Contributions

We have not been asked to calculate an actuarially determined contribution amount. We assume the City contributes on an ad hoc basis, but in an amount sufficient to fully fund the obligation over a period not to exceed 30 years.

Paragraph 244:

Transition Option

Prior periods were not restated due to the fact that prior valuations were not rerun in accordance with GASB 75. It was determined that the time and expense necessary to rerun prior valuations and to restate prior financial statements was not justified.

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APPENDIX F: DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES

INVESTMENT GAINS AND LOSSES

**Increase (Decrease) in OPEB Expense Arising from the Recognition of Effects of
Investment Gains and Losses on OPEB Plan Investments
(Measurement Periods)**

Measurement Period	Investment Gain/Loss	Original Recognition Period (Years)	Amounts Recognized in OPEB Expense through 2016	2017	Amounts to be Recognized in OPEB Expense after 2017	2018	2019	2020	2021	Thereafter
2016-17	\$67,185	5	\$0	\$13,437	\$53,748	\$13,437	\$13,437	\$13,437	\$13,437	\$13,437
Net Increase (Decrease) in OPEB Expense			\$0	\$13,437	\$53,748	\$13,437	\$13,437	\$13,437	\$13,437	\$0

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APPENDIX G: GLOSSARY OF RETIREE HEALTH VALUATION TERMS

Note: The following definitions are intended to help a *non*-actuary understand concepts related to retiree health valuations. Therefore, the definitions may not be actuarially accurate.

<u>Actuarial Cost Method:</u>	A mathematical model for allocating OPEB costs by year of service. The only actuarial cost method allowed under GASB 74/75 is the entry age actuarial cost method.
<u>Actuarial Present Value of Projected Benefit Payments:</u>	The projected amount of all OPEB benefits to be paid to current and future retirees discounted back to the valuation or measurement date.
<u>Deferred Inflows/Outflows of Resources:</u>	A portion of certain items that can be deferred to future periods or that weren't reflected in the valuation. The former includes investment gains/losses, actuarial gains/losses, and gains/losses due to changes in actuarial assumptions or methods. The latter includes contributions made to a trust subsequent to the measurement date but before the statement date.
<u>Discount Rate:</u>	Assumed investment return net of all investment expenses. Generally, a higher assumed interest rate leads to lower service costs and total OPEB liability.
<u>Fiduciary Net Position:</u>	Net assets (liability) of a qualifying OPEB "plan" (i.e. qualifying irrevocable trust or equivalent arrangement).
<u>Implicit Rate Subsidy:</u>	The estimated amount by which retiree rates are understated in situations where, for rating purposes, retirees are combined with active employees and the employer is expected, in the long run, to pay the underlying cost of retiree benefits.
<u>Measurement Date:</u>	The date at which assets and liabilities are determined in order to estimate TOL and NOL.
<u>Mortality Rate:</u>	Assumed proportion of people who die each year. Mortality rates always vary by age and often by sex. A mortality table should always be selected that is based on a similar "population" to the one being studied.
<u>Net OPEB Liability (NOL):</u>	The Total OPEB Liability minus the Fiduciary Net Position.
<u>OPEB Benefits:</u>	Other Post Employment Benefits. Generally medical, dental, prescription drug, life, long-term care or other postemployment benefits that are not pension benefits.
<u>OPEB Expense:</u>	This is the amount employers must recognize as an expense each year. The annual OPEB expense is equal to the Service Cost plus interest on the Total OPEB Liability (TOL) plus change in TOL due to plan changes minus projected investment income; all adjusted to reflect deferred inflows and outflows of resources.
<u>Participation Rate:</u>	The proportion of retirees who elect to receive retiree benefits. A lower

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participation rate results in lower service cost and a TOL. The participation rate often is related to retiree contributions.

Retirement Rate:

The proportion of active employees who retire each year. Retirement rates are usually based on age and/or length of service. (Retirement rates can be used in conjunction with the service requirement to reflect both age and length of service). The more likely employees are to retire early, the higher service costs and actuarial accrued liability will be.

Service Cost:

The annual dollar value of the “earned” portion of retiree health benefits if retiree health benefits are to be fully accrued at retirement.

Service Requirement:

The proportion of retiree benefits payable under the OPEB plan, based on length of service and, sometimes, age. A shorter service requirement increases service costs and TOL.

Total OPEB Liability (TOL):

The amount of the actuarial present value of projected benefit payments attributable to employees’ past service based on the actuarial cost method used.

Trend Rate:

The rate at which the employer’s share of the cost of retiree benefits is expected to increase over time. The trend rate usually varies by type of benefit (e.g. medical, dental, vision, etc.) and may vary over time. A higher trend rate results in higher service costs and TOL.

Turnover Rate:

The rate at which employees cease employment due to reasons other than death, disability or retirement. Turnover rates usually vary based on length of service and may vary by other factors. Higher turnover rates reduce service costs and TOL.

Valuation Date:

The date as of which the OPEB obligation is determined by means of an actuarial valuation. Under GASB 74 and 75, the valuation date does not have to coincide with the statement date, but can’t be more than 30 months prior.