Town of Yountville

"The Heart of the Napa Valley"

Agenda Date: February 5, 2008
Agenda Item: 10 B
Reviewed by Town Manager:

Yountville Town Council
Staff Report

TO: Mayor and Town Council

FROM: Richard Stranzl, Finance Director

SUBJECT: GASB 45 Actuarial Study Report

BACKGROUND

This item is for presentation of the GASB 45 actuarial study of the Town of Yountville's Other Post Employment Benefits (OPEB) as performed by the firm Bartel Associates LLC of San Mateo.

The purpose of this report is to provide the Council with the actuarial study results required by the Governmental Accounting Standards Board's (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Post Employment Benefits Other Than Pensions.* It addresses how public entities should account for and report their costs and obligations related to post employment health care and other non-pension benefits.

The Town of Yountville is required by GASB 45 to begin reporting its OPEB liability in its Consolidated Annual Financial Report (CAFR) for the 2009-10 fiscal year (December 2010). In commissioning this study for an actuarial analysis of its OPEB liability the Town is taking the first steps toward early-implementation of the GASB 45 reporting requirements.

At this meeting the Council is asked to consider in general terms, the results and implications of the study, and the options and strategies available to the Town in addressing the OPEB liability going forward. No Council action is required at this time. Staff plans to return at a future meeting with specific options and plans for Council consideration.

DISCUSSION

GASB Statement 45

In 2004, the Government Accounting Standards Board (GASB) issued rules relating to the accounting and reporting of Other Post-Employment Benefits (OPEB). These include all benefits – other than retirement benefits – that are earned by employees as a result of active service, but are not paid-out as benefits until the beneficiaries have retired.

The main purpose of implementing the new reporting requirements is to ensure that public entities accurately represent the cost of providing benefits as these costs are incurred (as benefits are earned), and not at a later date when a benefits are paid-out. The approach being implemented by GASB for OPEB is similar to that long-required of retirement plans in that retirement costs are incurred and reported as active employees earn the benefits, ensuring that adequate funding in available when benefits are actually paid-out.

GASB 45 generally requires that public entities account for and report the annual cost of OPEB, and the outstanding obligations and commitments related to OPEB, in a manner analogous to pension reporting. Annual OPEB costs for most public entities will be based on actuarially determined amounts that, if paid on an ongoing basis, would provide sufficient resources to pay for benefits as they come due. The provisions of GASB 45 may be applied prospectively and do not require public entities to fund their OPEB plans. A public entity may establish its OPEB liability at zero as of the beginning of the initial year of implementation; however, the unfunded actuarial liability is required to be amortized over future periods. GASB 45 also establishes disclosure requirements for information about the plans in which an employer participates, the funding policy followed, the actuarial valuation process and assumptions, and the extent to which the plan has been funded over time.

There is nothing in the GASB guidelines that requires that the Town to address any liability, either in terms of methodology or funding level. Implementing the requirements of GASB 45 affects how the Town reports its funding obligation, and funding status, of its retiree medical benefit plan in its annual financial statements. Nonetheless, the actuarial analysis conducted by the Town to assess the funding status of current retiree medical benefits highlights the long-term financial implications of maintaining a “pay-as-you-go” funding approach, as compared to a “pre-funding” approach where funds are set-aside as benefits are earned and accrue interest until the time when funds are needed to pay the benefits.

GASB 45 replaces the pay-as-you-go method that many public entities, including Yountville, currently utilize, with accrual accounting (recognizing an expense when it is earned). In addition to paying for current retiree medical premium costs, public entities must now recognize in their financial statements the “earned” cost of current employees’ future retiree medical premiums. In reporting these “earned” costs a public agency is compelled to recognize an important future financial obligation and, through actuarially determined analyses, annually set-aside amounts that enable a public agency to manage its OPEB liability judiciously.

Implementing Provisions of GASB 45

The specific requirements of GASB 45 are for public agencies to report annually, the difference between the Annual Required Contribution (ARC) – as calculated by the actuarial analysis – and the actual annual contribution made by the agency. The financial statements will also contain supplemental information related to the over-all funding status of the retiree medical benefit plan.

Implementation dates required by GASB 45 vary according to the size (annual operating budget) of public agencies, as presented in the following table:

TABLE 1 – GASB 45 IMPLEMENTATION		
Annual Revenue (FY00/01)	Re: Financial Statements	Deadline
$100 million or more	FY 2007-08	December 2008
$10 million or more	FY 2008-09	December 2009
Less than $10 million	FY 2009-10	December 2010

These deadline dates were established by GASB for implementing GASB 45 financial reporting requirements. In conducting the study and addressing GASB 45 issues now the Town is ahead of its prescribed implementation date of December 2010.

The Actuarial Study

In accordance with the aforementioned GASB 45 requirements the Town contracted with Bartel Associates to perform an actuarial valuation to determine the Town’s unfunded retiree medical insurance liability and the estimated amount the Town should set-aside annually to fully fund the OPEB liability. In producing the Study the consultant relied on data provided by staff with respect to our current budgeting for OPEB, actual employee census and tenure information, and on data provided by CalPERS regarding demographic information for both the Town's retirees and for all participating agencies. The valuation was completed in January 2008.

The following is a summary of the final results of the actuarial valuation of the Town's retiree medical benefit plan:

1. Our Unfunded Actuarial Accrued Liability as of June 30, 2007 is estimated in the range of $1.4 million to $2.1 million, depending on actuarial interest rate assumptions.

2. Both liabilities and Annual Required Contribution Rates (ARC) are highly sensitive to the discount rate and amortization assumptions. While generally accepted actuarial methods would amortize unfunded liabilities over 20 years, GASB allows for up to 30-year amortization of any unfunded OPEB liabilities. In addition, the discount rate (investment earnings) applied to plan assets have a dramatic effect on annual contributions needed to meet future funding obligations.

3. The following table provides a comparison of using a 4.25% rate (assumed Town's investment return) and 7.75% rate (the assumed PERS long-term investment return) for both 20-year and 30-year amortization of unfunded liabilities:

TABLE 2 - STUDY SUMMARY DATA				
Amortization Period	20 Years		30 Years	
Discount Rate	4.25%	7.75%	4.25%	7.75%
Unfunded Actuarial Liability	$ 2,109,000	$ 1,378,000	$ 2,109,000	$ 1,378,000
Normal Cost	239,000	132,000	239,000	132,000
Unfunded Liability	135,000	122,000	94,000	97,000
Annual Required Contribution	374,000	254,000	333,000	229,000
% of Payroll	24.6%	16.7%	21.9%	15.0%

The Town currently budgets $53,000 (on a pay-as-you-go basis) for OPEB, this represents about 3.5% of current payroll, this compares with possible full-funding of the OPEB liability that requires 15% to 24% of payroll, or $229,000 to $374,000 annually, based upon different actuarial assumptions.

While GASB 45 does not require the Town to modify its current funding of OPEB benefits, implementation of GASB 45's reporting requirements highlights the true cost of these benefits, and long-term cost projections strongly suggest the need to move from a pay-as-you-go funding practice to a pre-funding approach.

Going Forward

There are several issues that will need to be explored in greater detail prior to returning to Town Council with formal recommendations. This study provides the impetus for Staff review of the funding options with respect to unfunded liabilities and costs related to OPEB plans, as well as a review of OPEB plans themselves. Some items include; a review of benefit levels, vesting requirements, and alternative funding plan structures

FISCAL IMPACT

Is there a Fiscal Impact? No.

Is it currently budgeted? Yes.

Where is it budgeted? Funds to conduct this study were appropriated in the adopted FY 2007-08 Finance Department budget.

Is it Mandatory or Discretionary? Mandatory.

Is there a Staff Resource Impact? No.

This is an informational report, with no current impact. There will be a small impact on Town resources as Staff researches alternative methods for addressing our OPEB structure and its associated future liability.

ALTERNATIVES

Not applicable.

RECOMMENDATION

Staff recommends that Town Council accept the study and presentation by Bartel Associates. Specific action related to addressing the OPEB liability, the establishment of a funding plan, and post-employment medical benefits will be addressed at future Council meetings.

ATTACHMENTS

1. GASB 45 Actuarial Study, Bartel Associates (February 2008).