COLLEGE OF
MARIN

Board of Trustees

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July 17, 2013

The Honorable Judge James Ritchie
Marin County Superior Court
P.O. Box 4988
San Rafael, CA 94913-4988

Mr. Rich Treadgold, Foreperson
Marin County Grand Jury
3501 Civic Center Drive, Room #275
San Rafael, CA 94904

Dear Judge Ritchie and Foreperson Treadgold:

The Grand Jury Report: ***Marin's Retirement Health Care Benefits: The Money Isn't There*** speaks broadly to the issue of unfunded liabilities associated with retiree health benefits for all public agencies in Marin County. Marin Community College District (MCCD) has taken significant steps to address this issue. In 2005, MCCD Board of Trustees developed an action plan with unanimous support to address the unfunded retiree benefits liability. In June 2013, $2.1 million was invested in an irrevocable trust and we project our liability to be fully funded within five years.

MCCD's responses to the Findings and Recommendations to the Grand Jury findings and recommendations are provided in ***italicized blue print.***

MCCD agrees with the findings numbered: F6 and F9.

F6. Marin entities using "Pay Go" funding are paying only the current year health care benefits of those already retired. This ignores the reasonably known rising costs to cover future retirees who are already heading for retirement. Some actuarial valuation reports the Grand Jury studied provide those future "Pay Go" estimates year-by-year, so they should be readily available from the actuary's valuations. Estimates of those annual costs for each of the next 10 years should be provided to the public so that those who will incur the costs can know those costs.

MCCD has posted its actuarial studies on its website (http://www.marin.edu/fiscal/fiscal-reports.html) which is available to the public and includes the "Pay Go" estimates annually for the next 10 years.

F9. There is a wide range of retiree health care benefits offered among the entities studied in this investigation. No clear explanation for the range from minimal to extremely generous is readily available. Those entities that are promising relatively generous benefits should provide clear justifications to their citizens and customers.

MCCD has capped the employees eligible for retiree health benefits. Employees hired since 1988 are not eligible for retiree health benefits. The retiree health benefits available to those employees hired prior to 1988 are limited to age 70 and there is also a cap of $1,784.79 per month on the District contribution. (Exhibit 1)

MCCD disagrees wholly or partially with the findings numbered: F1, F2, F3, F4, F5, F7, F8 and F10.

F1. We find that many of Marin's local governments and special districts are failing to pre-fund future costs for retired employees by making investments to cover promised benefits for active employees. This jeopardizes the certainty that retiree health care benefits promised to current employees will be paid.

MCCD has taken active steps to prefund future costs for health benefits for retired employees since 2005. The District's governing Board of Trustees elected early application of the GASB pronouncement and in the fall of 2004 commissioned Total Compensation System, Inc. to perform the OPEB actuarial study which was completed in the spring of 2005. (Exhibit 2) *The Board further directed funding the obligation in advance rather than on the prior "pay as you go" basis, and in Fiscal Year 2005-06, $1 million of pre-funding for the obligation was designated to be set aside and was transferred out of the General Fund into the Retiree Unfunded Medical Benefits Liability Fund.* (Exhibit 3)

In Fiscal Year 2007-08, an additional $500 thousand was transferred from the General Fund into the Retiree Unfunded Medical Benefits Liability Fund. And, in 2009-10, an additional $500 thousand was transferred from the General Fund into the Retiree Unfunded Medical Benefits Liability Fund. (Exhibit 4)

At the June 18, 2013 MCCD Board of Trustees meeting, the Board passed a resolution to transfer $2.1 million that had been set aside plus interest into an irrevocable trust. These funds were transferred on June 26, 2013. (Exhibit 5)

F2. The failure of the majority of entities studied in this investigation to begin an investment program to provide a portion of the needed funds to pay for retiree health care benefits leads to generation shifting of the payment responsibility. Thus it appears to be, at the least unethical, and even a breach of fiduciary responsibility.

See Response to F-1.

F3. The extreme 30-year amortization period used by most entities minimizes the annual cost of funding the liability gap and further defers to future generations the compensation owed to present employees who provide services to present taxpayers and customers. Shorter amortization periods should be required for reasons of equity and to ensure that the promised benefits will be provided.

MCCD has historically used a 14-year amortization period. To date, MCCD has set-aside and transferred $2.1 million to an irrevocable trust. MCCD's actuarial analysis indicates that its unfunded liability will be fully-funded in five years. (Exhibit 6)

F4. By capping retiree health care benefits, the City of San Rafael has reasonable certainty as to what those costs are. Other entities studied here that promise to pay for future retiree health care with uncertain and likely rapidly increasing costs are accepting an unknown and potentially very costly risk.

MCCD does not have an unknown risk. MCCD has capped retiree health benefits and has imposed limitation as follows:

- *The employee eligibility for retiree health benefits – only employees hired prior to 1988.*
- *The age to which they will receive the benefits – up to age 70.*
- *The maximum monthly District contribution toward those benefits - $1,784.79 per month.*

F5. Because a few Marin County cities and other entities studied provide very limited benefits yet still appear able to meet community service needs, and because providing such benefits is increasingly rare in the private sector, such benefits appear to be unnecessary for attracting and

retaining employees. Accordingly, for active and newly hired employees, the benefits should be trimmed and costs should be shared between the employees and their employer.

MCCD does not offer retiree health benefits to newly hired employees. All active employees contribute to health benefits to the extent the cost exceeds the monthly cap of $1,784.79.

F7. Employers studied for this report should include an age-60, or even later, date for retiree health care benefits to commence in future negotiations with employees and their representatives.

MCCD's retiree health benefits commence and are consistent with the State Retirement Program. This is governed by the Legislature as set forth in the government code, which provides laws pertaining to the State Teachers Retirement System and the Public Employees Retirement System. The recommended action is not within the purpose of the District's governing board.

F8. The results of retiree health care actuarial cost analyses are summarized if at all only in obscure notes to annual financial statements. The public is entitled to more readily accessible explanation of these costs because the public will bear those costs.

MCCD has posted its actuarial studies on its website (http://www.marin.edu/fiscal/fiscal-reports.html) which is available to the public.

F10. Most of the entities the Grand Jury investigated are using fairly reasonable discount rates of 4%-5% per year to bring back to today in actuarial valuations the future annual costs of retiree health care benefits. However, some are using higher and highly questionable rate assumptions that are not justified by the investments (if any) that they have made to grow and fund the future benefits. The result is to understate the total funding needed today and in future years, to pay for those future benefits.

MCCD has historically used a 5% discount rate in its actuarial studies. The most recent actuarial study increased the discount rate to 7% based on anticipated investment earnings from the irrevocable trust investment strategies.

Recommendations numbered R1, R2, R3 and R6 have been implemented.

R1. Begin setting aside in separate investment accounts, if it is not already doing so, each year's funds for amortizing its retiree health care benefits UAAL, in addition to its "Pay Go" funding of those benefits for present retirees.

The District's Board of Trustees elected early application of the GASB pronouncement and in the fall of 2004 commissioned Total Compensation System, Inc. to perform the OPEB actuarial study which was completed in the spring of 2005. (Exhibit 2) *The Board further directed funding the obligation in advance rather than on the prior "pay as you go" basis, and in Fiscal Year 2005-06, $1 million of pre-funding the obligation was set aside and transferred out of the General Fund into the Retiree Unfunded Medical Benefits Liability Fund.* (Exhibit 3)

In 2007-08, an additional $500 thousand was transferred from the General Fund into the Retiree Unfunded Medical Benefits Liability Fund. And, in 2009-10, an additional $500 thousand was transferred from the General Fund into the Retiree Unfunded Medical Benefits Liability Fund. (Exhibit 4)

At the June 18, 2013 Board of Trustees meeting, the Board passed a resolution to transfer $2.1 million that had been set aside into an irrevocable trust, and the funds were transferred on June 26, 2013. (Exhibit 5)

R2. Begin a program to lower the amortization period for funding its retiree health care benefits from as much as 30 years presently, to approach (within 10 years), the commonly used 17-year amortization period for retiree pension funding.

MCCD has historically used a 14-year amortization period. MCCD has set-aside and transferred $2.1 million to an irrevocable trust. MCCD's actuarial analysis indicates that its unfunded liability will be fully-funded in five years. (Exhibit 6)

R3. Negotiate caps on the amounts it commits to pay existing and new employees for retiree health care benefits.

MCCD has a cap of $1,784.79 per month for retiree health benefit for existing eligible employees. No employees hired after 1988 are eligible for retiree medical benefits. (Exhibit 1)

R6. Place a link on its website to provide the latest actuarial valuation of its AAL, its UAAL, its consequent percent funded, its discount rate (annual percentage) used to determine these values, and a projection of outlays ("Pay Go") for retiree health care benefits for each of the current and subsequent 10 years.

MCCD has posted all of its actuarial studies on its website (http://www.marin.edu/fiscal/fiscal-reports). The actuarial studies contain the information requested.

Recommendations numbered R4 and R5 will not be implemented.

R4. Negotiate a higher retirement age than the currently applicable age for the commencement of retiree health care benefits.

MCCD's retiree health benefits commence and are consistent with the State retirement programs, e.g., STRS and PERS.

R5. Require active employees to make a contribution towards the cost of their retiree health care benefits.

Active employees contribute toward the cost of their health benefits to the extent the cost exceeds the monthly cap of $1,784.79. Requiring an additional contribution toward their retiree health care benefits would have to be negotiated with all bargaining units. MCCD anticipates its unfunded liability to be fully funded in five years.

Thank you for the opportunity to respond to the Grand Jury Report pertaining to retirement health care benefits. The MCCD Board of Trustees reviewed this report on July 16, 2013 and is in full agreement with its content. Should further clarification be desired, please contact Dr. David Wain Coon, Superintendent/President of the Marin Community College District.

Sincerely,

James Namnath, Ph.D., President
Marin Community College Board of Trustees
College of Marin
Kentfield, CA 94904

COLLEGE OF
MARIN

Rates Effective February 1, 2013

	Monthly Premium	Member Contribution
Kaiser ($20 Office; Prescription $5 Generic/$10 Brand)		(Cap $1,784.79)
Member Only	$ 706.73	$0.00
Member + 1	$ 1,413.45	$ 0.00
Family	$ 1,879.89	$95.10
Health Net (HMO) ($20 Office; $5/10/35 Prescription; 5/40Chiropractic)		(Cap $1,784.79)
Member Only	$ 1,254.74	0.00
Member + 1	$2,509.48	$724.69
Family	$3,337.60	$1,552.81
Health Net Select ($20/30/Tiered Office; $10/15/35 Prescription; $5/40 Chiropractic)		(Cap $1,784.79)
Member Only	$ 1,803.58	$18.79
Member + 1	$3,607.15	$1,822.36
Family	$4,797.53	$3,012.74

NOTE: The monthly premium for Delta Dental is $128.50 per month. The monthly premium for Vision Service Plan is $15.50 per month. These monthly premiums remained unchanged from last year.

College of Marin
Actuarial Study of
Retiree Health Liabilities

Prepared by:
Total Compensation Systems, Inc.

Date: May 18, 2005

Table of Contents

PART I: EXECUTIVE SUMMARY 3

A. INTRODUCTION 3
B. GENERAL FINDINGS 4
C. DESCRIPTION OF RETIREE BENEFITS 5
D. RECOMMENDATIONS 5

PART II: BACKGROUND 7

A. SUMMARY 7
B. ACTUARIAL PRE-FUNDING 7

PART III: LIABILITIES AND COSTS FOR RETIREE BENEFITS 10

A. INTRODUCTION 10
B. MEDICARE 10
C. LIABILITY FOR RETIREE BENEFITS 10
D. COST TO PREFUND RETIREE BENEFITS 11
1. Normal Cost 11
2. Amortization of Past Service Liability 12
3. Other Components of Cost 12
4. Total First Year Prefunding Cost 13

PART IV: "PAY AS YOU GO" FUNDING OF RETIREE BENEFITS 14

PART V: FUNDING ALTERNATIVES 15

PART VI: RECOMMENDATIONS FOR FUTURE VALUATIONS 18

PART VII: BENEFIT DESIGN ISSUES 19

PART VIII: APPENDICES 20

APPENDIX A: MATERIALS USED FOR THIS STUDY 20
APPENDIX B: EFFECT OF ASSUMPTIONS USED TO CALCULATE 21
APPENDIX C: ACTUARIAL ASSUMPTIONS 22
APPENDIX D: DISTRIBUTION OF ELIGIBLE PARTICIPANTS BY AGE 24
APPENDIX E: GASB 12 COMPLIANCE INFORMATION 25
APPENDIX F: RETIREE HEALTH EXPENSES CHARGEABLE TO CATEGORICAL PROGRAMS 26
APPENDIX G: GLOSSARY OF RETIREE HEALTH VALUATION TERMS 27

COLLEGE OF MARIN

Actuarial Study of Retiree Health Liabilities

PART I: EXECUTIVE SUMMARY

A. Introduction

College of Marin asked Total Compensation Systems, Inc. (TCS) to analyze liabilities associated with its current retiree health program as of May 1, 2005.

This actuarial study is intended to serve the following purposes:

- To provide information to enable College of Marin to manage the costs and liabilities associated with its retiree health benefits.
- To provide information to enable College of Marin to communicate the financial implications of retiree health benefits to internal financial staff, the Board, employee groups and other affected parties.
- To provide information needed to comply with Governmental Accounting Standards Board Accounting Standard 12 (GASB 12) and with the forthcoming GASB accounting standard related to "other postemployment benefits" (OPEB's). (See Appendix E)

This actuarial report includes several estimates for College of Marin's retiree health program. We calculated the following estimates separately for active employees and retirees. As requested, we also separated results by the following employee classifications: Faculty, Classified and Management. We estimated the following:

- the total liability created.
- the ten year "pay-as-you-go" cost to provide these benefits.
- the "past service liability." (The past service liability is the amount that would currently be in funds earmarked for retiree benefits if the College had begun prefunding each employee's benefit cost when that employee was hired.)
- the amount necessary to amortize the initial "past service liability" over a period of 18 years.
- the annual contribution required to fund retiree benefits over the working lifetime of eligible employees (the "annual accrual cost").

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 depend on the actuarial assumptions used.

Actual costs and liabilities could easily vary by 10 - 20% or more from estimates contained in this report. The best way to respond to this uncertainty of future results is to have an actuarial study performed regularly - no less frequently than every three years.

B. General Findings

We estimate the "pay-as-you-go" cost of providing retiree health benefits in the year beginning May 1, 2005 to be $613,411 (see Section IV.A.). However, this cost would increase over the next ten years at an annual rate of 0.9%.

There are several reasons why it is important for community college districts to evaluate retiree health costs and liabilities. The Governmental Accounting Standards Board (GASB) will soon require accounting for the costs and liabilities associated with retiree health benefits on an accrual basis -- i.e. over the working lifetime of eligible employees. (The effective date of the GASB accounting standard will range from 2007 to 2009, depending on the annual revenue of the College during the 1998-99 fiscal year. Auditors may require an actuarial study for an unqualified audit based on AICPA Statement of Position 92-06.

Community College Districts may have additional reasons to obtain a retiree health valuation. Accreditation teams have been instructed to look for an actuarial valuation when district-paid retiree health benefits are provided. Also, charging any part of retiree benefit costs to categorical programs requires an actuarial valuation and funding on an actuarial basis.

To comply with accounting and regulatory requirements will effectively require that retiree health benefit costs be prefunded. "Prefunding" retiree health benefits refers to the practice of setting aside funds that are earmarked for retiree health benefits while employees are still actively employed - i.e. before the funds are actually expended to pay for retiree health benefits. By prefunding retiree benefits, there will be enough funds available at retirement (on average) that, with interest, will be sufficient to pay all promised retiree health benefits without the need for any post-retirement College contributions.

For current employees, the value of benefits "accrued" in the year beginning May 1, 2005 is $208,316. This accrual cost would increase each year based on covered payroll. Had College of Marin begun pre-funding retiree health benefits when each current employee and retiree was hired, a substantial fund would have accumulated. We estimate the amount that would have accumulated to be $7,878,291. This amount is often called the "past service liability."

We calculated the annual cost to amortize the unfunded past service liability using a 5% interest discount rate. We used a 18 year amortization period. The current year cost to amortize the unfunded "past service liability" is $522,810. This amortization payment would increase each year based on covered payroll. Payments would continue for 18 years, after which time amortization payments would end.

Combining the accrual and amortization costs in the first year produces total first year pre-funding costs of $731,126. This amount would be in lieu of (rather than in addition to) the "pay-as-you-go" cost. The additional cost of prefunding is therefore $117,715.

Funding retiree benefits over employees' working lifetime would add to total compensation an average of $1,929 per year per employee from each employee's hire date until the employee reaches retirement. This accrual cost would increase each year based on covered payroll.

We based all of the above estimates on employees as of April, 2005. Over time, liabilities and cash flow

will vary based on the number and demographic characteristics of employees and retirees. It will be important to periodically revalue costs and liabilities.

C. Description of Retiree Benefits

Following is a description of the current retiree benefit plan:

	Faculty	Classified	Management
Benefit types provided	Medical and dental	Medical and dental	Medical and dental
Duration of Benefits	To age 70	To age 70	To age 70
Required Service	15 years	10 years	10 years
Minimum Age	55	50	50/55*
Dependent Coverage	Yes	Yes**	Yes
College Contribution %	100%	100%	100%
College Cap	Kaiser Rates	None***	None

*Depending on retirement system
**SEIU employees are not eligible for District-paid dependent benefits
***SEIU benefits capped at Kaiser or HealthNet reates

D. Recommendations

It is outside the scope of this report to make specific recommendations of actions College of Marin should take to manage the substantial liability created by the current retiree health program. Total Compensation Systems, Inc. can assist in identifying options once this report has been studied. The following recommendations are intended only to allow the College to get more information from this and future studies.

- Until GASB 45 is effective, we recommend that College of Marin conduct a study whenever events or contemplated actions significantly affect present or future liabilities, but no less frequently than every three years. (See Part VI for a list of events that can affect retiree health liabilities.)

- We recommend that the College communicate the magnitude of these costs to employees and include employees in discussions of options to control the costs.

- Because of the significant liabilities created by the current retiree health program, the College should maintain a program of earmarking funds to pay future benefits. It should be noted that the upcoming GASB accounting standard will require assets sufficient to offset retiree health liabilities. (See Part V for a review of funding alternatives.)

- Under GASB 45, it is important to isolate the cost of retiree health benefits. We strongly urge College of Marin to 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.

- Several assumptions were made in estimating costs and liabilities under College of Marin'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.)

- Segregating plan assets will allow taking advantage of California Government Code Sections 53620 through 53622 to achieve greater investment income on plan assets. This study assumes an investment return net of all investment and plan expenses of 5%. We recommend College of Marin take actions to achieve a long term rate of return that reflects the long term nature of the liabilities.

Respectfully submitted,

Geoffrey L. Kischuk, FSA, MAAA, FCA
Consultant
Total Compensation Systems, Inc.
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PART II: BACKGROUND

A. Summary

Accounting principles have long held that the cost of retiree benefits should be "accrued" over employees' working lifetime. For this reason, the Governmental Accounting Standards Board (GASB) issued in 2004 Accounting Standards 43 and 45 for retiree health benefits. These standards will apply to all public employers that pay any part of the cost of retiree health benefits for current or future retirees (including early retirees).

The GASB standards will become effective on a phased basis based on revenue during the 1998-99 fiscal year. For employers, the first phase will be $100 million or more in revenue. The effective date will be the first fiscal year on or after December 15, 2006. Successive annual phases will sweep in "$10 to $100 million" and "less than $10 million" employers. The effective date for "plans" will be one year earlier than the dates for employers. A "plan" is a trust or other arrangement that is exclusively for retiree health benefits and the assets of which are protected from creditors.

Until the new GASB standards take effect, the Governmental Accounting Standards Board (GASB) currently requires public employers to disclose the existence and/or cost of retiree health benefits. GASB requirements are contained in GASB 12.

Prudent fiscal management of retiree health costs and liabilities requires establishment of a long-term plan. For most public employers, the magnitude of the accrued liability makes it difficult to immediately begin to fully pre-fund retiree health benefits on an actuarial basis. Fortunately, the current absence of stringent accounting or regulatory funding requirements allows public employers flexibility to transition into full actuarial pre-funding over the next few years. Transitioning into full actuarial pre-funding provides public employers with the time to establish fiscal management plans that

- protect retiree benefit security to the greatest possible extent;
- involve employee groups in discussions of benefit design and funding options; and
- minimize disruptions to core services that could result from rapidly increasing retiree benefit costs.

Waiting to address retiree health benefit funding until the GASB accounting standards become effective will dramatically reduce employers' fiscal options. By then, unfunded accrued liabilities will be bigger, thereby increasing the payments needed to amortize the unfunded liability. Higher future amortization payments would squeeze financial resources for vital services. Waiting to pre-fund until required by GASB will result in less time to evaluate options and take action to protect benefits for future retirees and/or reduce benefit costs. To the extent retiree benefits are subject to collective bargaining, the timing and extent of benefit and funding changes may be constrained.

B. Actuarial Pre-funding

To actuarially pre-fund retiree health benefits requires determining the amount to be set aside each year so that funds available at retirement are, on average, sufficient (with interest) to pay all retiree health expenditures without the need for additional employer contributions. There are many different ways to determine the annual pre-funding cost. The calculation method used is called an "actuarial cost method."