

Public Agenda Item #19

Review, Discussion and Consideration of the
Texas Employees Group Benefits Program:
Actuarial Valuation of Retiree Health Insurance Benefits
as of August 31, 2016

December 2, 2016

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Employees Retirement System of Texas

Texas Employees Group Benefits Program

**Actuarial Valuation of GBP
Retiree Insurance Benefits (OPEB)
for Fiscal Year 2016**

**Board of Trustees
December 2, 2016**

**Philip S. Dial
Mitchell L. Bilbe**



Rudd and Wisdom, Inc.
CONSULTING ACTUARIES

FY 2016 GBP OPEB Valuation

General Information

- ❑ The valuation is conducted in order to provide the information required under Governmental Accounting Standards Board Statement No. 43 (GASB 43).
- ❑ This is the tenth valuation of GBP OPEB.
- ❑ The GBP provides OPEB to the retirees of state agencies, certain higher education institutions and “other” employers.
- ❑ OPEB provided through the GBP are:
 - Health
 - Basic Life
- ❑ OPEB does not include retirement benefits
- ❑ Retirees have access to other optional benefits, but those benefits are fully funded by member contributions and, therefore, do not generate employer obligations under GASB 43.

FY 2016 GBP OPEB Valuation

Application of GASB Reporting Standards

- ❑ The information required under GASB 43 is reported by ERS in the notes and supplementary information contained in the CAFR.
- ❑ ERS provides the information to the Texas Comptroller of Public Accounts (Comptroller).
- ❑ The Comptroller obtains similar information from TRS.
- ❑ The Comptroller does not report GASB expense and liability information for ERS and TRS in the financial statements in the State's CAFR. Instead, certain information regarding both plans is disclosed in the notes to the financial statements.
- ❑ GASB 43 requires disclosure of the Annual Required Contribution (ARC), but the employer is not actually required to contribute the ARC each year.

FY 2016 GBP OPEB Valuation

Impact of SB 1459

- ❑ SB 1459 adopted by the 83rd Texas Legislature amended Article 1551 of the Insurance Code.
- ❑ SB 1459 requires insurance contribution rates for retirees to vary based on length of service (LOS) at retirement.
- ❑ Amendment applies only to:
 - Employees with less than five years of service on September 1, 2014,
 - Who retire on or after September 1, 2014.

LOS (Years)	State Contribution		Retiree Contribution	
	Retiree	Dependents	Retiree	Dependents
20 or more	100%	50%	0%	50%
15-19	75%	37.5%	25%	62.5%
10-14	50%	25%	50%	75%

FY 2016 GBP OPEB Valuation

Impact of SB 1459

- ❑ This is the fourth valuation to reflect the impact of SB 1459.
- ❑ SB 1459 has only a small impact on the FY 2016 OPEB liabilities and costs, since it applies to only a small segment of the membership, most of whom will not be eligible to retire for many years.
- ❑ But the impact of the bill will gradually grow for many years:
 - As employees to whom the requirements do not apply are replaced by those to whom they do, and
 - As employees to whom the requirements apply get closer to and eventually retire.
- ❑ The requirements of SB 1459 will:
 - Reduce the state's liability and cost for applicable employees who retire with less than 20 years of service.
 - Discourage some applicable employees and vested terminated members with less than 20 years of service from enrolling for insurance upon retirement.

FY 2016 GBP OPEB Valuation

Actuarial Cost Method and Assumptions

- Actuarial cost method
 - Entry age normal (EAN)
 - Same method used since inception of the GASB reporting requirements.
 - Same method used for ERS retirement plan valuation.
 - Normal cost and 30 year amortization amounts are determined as level percentages of pay.

- Actuarial assumptions
 - Demographic and pay-related assumptions are the same as those used in valuing the retirement plans.
 - Investment return assumption for a plan funded on a PAYGO basis is based on the rate of return on the employer's assets.
 - Health plan benefit cost trend has been established consistent with other economic assumptions as required by GASB.

FY 2016 GBP OPEB Valuation

Demographic Assumptions

- Demographic assumptions include:
 - Mortality
 - Disability
 - Termination
 - Withdrawal
 - Retirement

- State agency employees and retirees:
 - Same demographic assumptions as those utilized by ERS for its retirement plan valuation for FY 2016

- Higher education employees and retirees:
 - Same demographic assumptions as those utilized by TRS for its retirement plan valuation for FY 2016

FY 2016 GBP OPEB Valuation

Economic Assumptions

- Economic assumptions include:
 - Inflation
 - Payroll growth and inflationary salary increases
 - Salary increases for merit, promotion and longevity

- State agency employees and retirees:
 - Same economic assumptions as those utilized by ERS for its retirement plan valuation for FY 2016

- Higher education employees and retirees:
 - Same economic assumptions as those utilized by TRS for its retirement plan valuation for FY 2016, with an adjustment to the inflation assumption to be consistent with the GASB 43 inflation assumption.

FY 2016 GBP OPEB Valuation

Economic Assumptions - Investment Return Assumption

- ❑ Since the OPEB benefits provided under the GBP are funded on a PAYGO basis, GASB 43 requires that the investment return assumption be based on the expected yield of the “*assets of the employer*”.
- ❑ For the State of Texas, the “*assets of the employer*” are the assets held in the Treasury Pool and managed by the Comptroller.
- ❑ The average annual real rate of return (return in excess of inflation) for the Treasury Pool has been approximately 2.0% over the last 30 years.
- ❑ Based on this analysis and the inflation assumption adopted by the Board for purposes of the retirement plan valuation (3.5%) we have selected an investment return assumption of 5.5% in the OPEB valuation.
- ❑ This is the same investment return assumption as was used for the FY 2008 - FY 2015 valuations.

FY 2016 GBP OPEB Valuation

Economic Assumptions – FY 2017 Per Capita Health Benefit Costs

- The OPEB valuation is based on projected Per Capita Health Benefit Costs for FY 2017
 - By gender
 - By age
- Prior to the FY 2011 valuation, the Per Capita Health Benefit Costs represented the projected cost of HealthSelect coverage since the great majority of retirees participate in HealthSelect.
- With the addition of the Medicare Advantage PPO option (HealthSelect Medicare Advantage) effective January 1, 2012, it became necessary to have two sets of Per Capita Health Benefit Costs:
 - HealthSelect (for participants for whom Medicare is not primary and for Medicare-primary participants who elect to remain in HealthSelect).
 - HealthSelect Medicare Advantage (for Medicare-primary participants who elect HealthSelect Medicare Advantage).

FY 2016 GBP OPEB Valuation

Economic Assumptions – FY 2017 Per Capita Health Benefit Costs

- HealthSelect (medical and prescription drug)
 - The retiree population is such that a great deal of credible data exists.
 - Extensive historical data allows us to examine both current cost as well as evolving cost trends.
 - HealthSelect experience data through FY 2016 is used to establish current gender/age-specific costs for HealthSelect.

- HealthSelect Medicare Advantage
 - Per capita medical costs are based on the HealthSelect Medicare Advantage premiums applicable to the fully insured medical benefits and the associated Health Insurance Provider Fee as required under the Affordable Care Act (ACA).
 - Per capita prescription drug costs are the same as those applicable to HealthSelect participants since HealthSelect Medicare Advantage participants have the same prescription drug coverage as HealthSelect participants.

FY 2016 GBP OPEB Valuation

Economic Assumptions – Health Plan Benefit Cost Trend

- ❑ A select and ultimate trend assumption is used which begins at the levels we are using for the next biennium.
- ❑ The trends have been revised to reflect updated projections for FY 2018 – FY 2023.
- ❑ The trend is expected to be 8.5% through FY 2019 and then decline over the next five years to a “sustainable” ultimate level.
- ❑ The ultimate level is two percent in excess of the assumed rate of inflation (5.5% = 3.5% + 2.0%).
- ❑ The ultimate level is the same as that used in previous OPEB valuations.

FY 2016 GBP OPEB Valuation

Economic Assumptions – Health Plan Benefit Cost Trend

Fiscal Year	FY 2015 Valuation	FY 2016 Valuation
2018	8.0%	8.5%
2019	7.5%	8.5%
2020	7.0%	7.5%
2021	6.5%	7.0%
2022	6.0%	6.5%
2023	5.5%	6.0%
2024 and beyond	5.5%	5.5%

FY 2016 GBP OPEB Valuation

GBP Membership

Category	Members	Covered Spouses	Covered Dependent Children	Total
Actives	235,108 ¹	41,564 ²	126,597	403,269
Deferred Vested	11,329	0 ²	0 ²	11,329²
Retirees and Nominees	113,430 ³	29,153	9,757	152,340
Total - August 31, 2016	359,867	70,717	136,354	566,938
Total - August 31, 2015	350,777	70,108	134,794	555,679
Change	9,090	609	1,560	11,259

¹ Includes (a) return-to-work retirees and (b) employees who have not yet satisfied the waiting period.

² Rather than use current spouse/dependent child coverage information, actuarial assumptions are used to estimate the future number of spouses and dependent children that will be covered at retirement.

³ Includes 3,968 retirees who receive the Opt-Out Credit in lieu of health benefits.

FY 2016 GBP OPEB Valuation

Results (See page II-3 of the Actuarial Valuation Report.)

Member Class	UAAL	NC	Amortization	ARC
Actives	\$15,008M	\$1,123M	\$652M	\$1,775M
Vested Non-Contributing	1,363M	NA	59M	59M
Retirees	10,720M	NA	465M	465M
Total	\$27,091M	\$1,123M	\$1,176M	\$2,299M

- Actual Employer Contributions for FY 2016 (including Federal Retiree Drug Subsidy revenue) = \$666M which is 29.0% of ARC.
- Terminology
 - UAAL = Unfunded Actuarial Accrued Liability = APVTPB – PVFNC – Net Assets
 - NC = Normal Cost
 - Amortization = UAAL amortized over 30 years as a level % of payroll
 - ARC = Annual Required Contribution = NC + Amortization
 - APVTPB = Actuarial Present Value of Total Projected Benefits
 - PVFNC = Present Value of Future Normal Costs

FY 2016 GBP OPEB Valuation

Reconciliation with FY 2015 (See page II-5 of the Actuarial Valuation Report.)

OPEB Measure	Actual FY 2015	Expected FY 2016 Based on FY 2015 Assumptions	Change Attributable to			Actual FY 2016
			Differences in Actual vs Expected	Assumption Changes	Plan Change	
UAAL	\$25,741M	\$27,432M	(\$311M)	(\$30M)	0	\$27,091M
NC	\$1,044M	\$1,080M	\$31M	\$12M	0	\$1,123M

- a) Year-to-year increases will occur if actual and expected experience are the same:
 - UAAL: Since OPEB is funded on a PAYGO basis, the excess of NC plus interest over the PAYGO amount increases the UAAL.
 - NC: NC is determined as a level percentage of payroll; therefore the dollar amount increases due to growth in active employment and/or inflationary increases in salaries.
- b) Gains/losses from differences in actual vs expected will occur to the extent that the assumptions are too pessimistic/optimistic; e.g., fewer retirements than were expected would create a gain.
- c) Gains resulting from changes in Per Capita Health Benefit Costs have been partially offset by losses resulting from changes in the demographic assumptions and the Health Benefit Cost Trend.
- d) SB1459 has resulted in liabilities and costs that are lower than they would have otherwise been. The impact of SB 1459 will grow over time.

FY 2016 GBP OPEB Valuation

Comparison of FY 2015 and FY 2016 Results

OPEB Measure	FY 2015	FY 2016
Normal Cost - % Payroll	9.3%	9.5%
Amortization - % of Payroll	10.0%	10.0%
ARC - % Payroll	19.3%	19.5%

FY 2016 GBP OPEB Valuation

GASB 74

- ❑ GASB 74 replaces GASB 43 effective for FY 2017.

- ❑ GASB 74 will require significant changes in the OPEB valuation.
 - For unfunded plans like the GBP OPEB, the investment return assumption will be based on yields of 20-year, tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher. If GASB follows the mark-to-market approach required for retirement plans under GASB 67/68, the expected investment return assumption for FY 2017 could be lower than the current investment return assumption depending on the yields of these tax-exempt bonds at that time.

 - The Net OPEB Liability will be equal to the difference between the Actuarial Accrued Liability (determined using the new investment return assumption) and the fair value of plan assets, which are currently \$0 since the plan uses a PAYGO approach.

 - There will also be increased note disclosures and supplementary information including a sensitivity analysis of the Net OPEB Liability to $\pm 1\%$ changes in the investment return assumption and changes in the healthcare trend rate.

FY 2016 GBP OPEB Valuation

GASB 74

- ❑ GASB 74 may require significant changes in presentation of the OPEB expense and liability information.
 - Under GASB 43 OPEB expense and liability information is reported by ERS in the notes and supplementary information contained in the CAFR. GASB 74 may require this information to be reported in the Statements of Fiduciary Position and Changes in Fiduciary Position.
 - Under GASB 45 the Comptroller reports OPEB expense and liability information for ERS and TRS in the notes to the financial statements in the State's CAFR. GASB 75 may require this information to be presented in the financial statements.
 - GASB 74/75 may require increased reporting by GBP participating employers.

- ❑ ERS will conduct discussions with the Comptroller during 2017.

Appendix

GBP OPEB Valuation - Key OPEB Measures

See Section IX of the Actuarial Valuation Report for the definitions of certain terms used in this presentation.

Questions?