Los Gatos Union School District

Valuation of Retiree Health Benefits

REPORT OF GASB 45 VALUATION
AS OF JULY 1, 2014

Prepared by: North Bay Pensions
December 19, 2014

North Bay Pensions

Contents of This Report

Actuarial Certification		**1**
Summary of Results		**2**
Detailed Exhibits		
Exhibit 1	Actuarial Values as of July 1, 2014	**5**
Exhibit 2	Annual OPEB Cost	**6**
Exhibit 3	Five-Year Projection of Costs	**7**
Exhibit 4	20-Year Forecast of Benefit Payments	**8**
Exhibit 5	Net OPEB Asset	**9**
Exhibit 6	Summary of Plan Provisions	**9**
Exhibit 7	Summary of Actuarial Assumptions	**11**

Actuarial Certification

This report presents the determination of benefit obligations under **Statement No. 45 of the Governmental Accounting Standards Board (GASB 45)** as of July 1, 2014 for the retiree health and welfare benefits provided by the Los Gatos Union School District. I was retained by the District to perform these calculations.

GASB Statement 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions", was issued to provide standards for governmental employers to record expense for **Other Postemployment Benefits (OPEB)**. OPEB includes postretirement health and welfare benefits hence GASB 45 is the appropriate Standard to follow when recording the District's OPEB obligations.

The information contained in this report was based on participant census information provided to me by the District. The actuarial assumptions and methods used in this valuation were selected by the District after consultation with me. I believe the assumptions and methods are reasonable and appropriate for purposes of actuarial computations under GASB 45.

Actuarial computations under GASB 45 are for purposes of fulfilling employer accounting requirements. The calculations reported herein have been made on a basis consistent with my understanding of GASB 45. Determinations for purposes other than meeting employer financial accounting requirements may be significantly different from the results reported herein.

To the best of my knowledge, this report is complete and accurate. This valuation has been conducted in accordance with generally accepted actuarial principles and practices. The undersigned is a Fellow of the Society of Actuaries, a Fellow of the Conference of Consulting Actuaries, and a Member of the American Academy of Actuaries, and meets their continuing education requirements and qualification standards for public statements of actuarial opinion relating to retirement plans. In my opinion, I am qualified to perform this valuation.

12-19-14

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Summary of Results

Background

The District maintains a program which pays part or all of monthly medical insurance premiums on behalf of retired former employees, provided that the employee has satisfied certain requirements. As of July 1, 2014, the District has funded $1,500,541 in an irrevocable trust (SISC) toward the cost of future benefits. This valuation was prepared under the assumption that the District will continue funding these benefits on a pay-as-you-go basis for at least the next five years.

In June 2004, the Governmental Accounting Standards Board (GASB) released Statement No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions". This statement, often referred to as GASB 45, requires governmental entities to (1) record annual expense for their OPEB and (2) disclose certain information in their year-end financial statements.

The District has requested this actuarial valuation to determine what its OPEB obligations under the program are, and what the fiscal impact of GASB 45 will be for the 2014-2015 and 2015-2016 fiscal years.

Present Value of Future Benefits

The Actuarial Present Value of Total Projected Benefits (APVTPB) for all current and former employees, as of July 1, 2014, is **$8,183,230**. This is the amount the District would theoretically need to have funded at this time to fully fund all those future benefits.

The APVTPB of $8,183,230 is the sum of these amounts:

Future benefits of current employees	
Certificated employees	$ 4,724,759
Classified employees	1,580,453
Management/confidential employees	399,016
Subtotal	$ 6,704,228
Future benefits of current retirees	
Certificated employees	$ 814,435
Classified employees	283,222
Management/confidential employees	381,345
Subtotal	$ 1,479,002
Total present value of all future benefits	$ 8,183,230

This APVTPB of $8,183,230 can be compared to the $8,766,943 amount that was disclosed in the July 1, 2012 valuation. We would have expected the APVTPB to be approximately $8,896,000 this year. The difference is mainly because medical premiums are lower than expected. The Kaiser (high) premium is about 10% less than we expected it to be, the Blue Cross (High) premium is about 5% less than expected.

These figures are computed by (1) estimating the OPEB benefits that will be paid to each current and former employee and their beneficiaries (if applicable), upon the employee's retirement from the District, (2) estimating the likelihood that each payment will be made, taking into consideration the likelihood of remaining employed until retirement age and the likelihood of survival after retirement, and (3) discounting each expected future payment to the present date at the assumed rate of investment return of 7%.

Subsidized Premiums

Another way to look at the APVTPB is like this:

Present value of District-paid premiums	$ 5,605,315
Present value of subsidized premiums	2,577,915
APVTPB	$ 8,183,230

The second line above, "Present value of subsidized premiums", calls for some explanation. It is well known that the cost of health care increases as people grow older. When your insurance carriers calculate a single monthly premium that applies to all your employees, they calculate an average premium rate which is based on the distribution of ages of your covered employees and their dependents. Generally speaking, this average premium rate is higher than the true cost of medical care for your younger employees and lower than the true cost for older employees and early retirees. Your retired employees under age 65 are actually paying a monthly premium which is less than the true cost of their coverage. This difference, called a "subsidy", is being paid by the District as part of the monthly premiums it pays for all employees. The GASB 45 accounting rules require us to include the value of the subsidy for current and future retirees, so that the entire value of employer-paid benefits has been accrued by the time employees retire.

One consequence of including the value of the subsidized premiums in your GASB 45 operating expense is that there is a potential for double-counting the amount of the subsidized premiums. In other words, unless you make an adjustment, you will be accruing the amount of those subsidized premiums *twice* in each fiscal year: once for your active employees, in the medical premiums you are paying, and again in the GASB 45 expense. Fortunately, GASB 45 permits you to make a simple adjustment to the medical premium costs you accrue for your employees. As shown in Exhibit 3, **for the 2014-15 year you may reduce your accrual of medical premiums for current employees by $189,508.** For the 2015-16 year, you may reduce your accrual of medical premiums by $194,075.

“Annual OPEB Cost” Under GASB 45

GASB 45 requires that the cost of the program be recognized in a systematic manner over the working careers of employees. There are six different budgeting methods (called “actuarial funding methods”) that may be used to determine what the annual operating expense (called the Annual OPEB Cost) will be. The District has elected to use the Entry Age Normal actuarial funding method with a closed 30-year level percentage of pay amortization of the unfunded actuarial accrued liability.

The actuarial funding method is used to compute the **Annual Required Contribution (ARC)**. The ARC is generally equal to the sum of (1) the value of benefits earned by employees in the current year, plus (2) an amortization of the value of benefits earned by employees in prior years. **Annual OPEB Cost** is equal to the sum of (a) the ARC, and (b) interest on any over/unfunded OPEB operating expense from prior years, less (c) an amount to reflect the amortization of unfunded OPEB already included in the ARC.

Please note that the ARC is not the amount that the District should record as an operating expense each year. The annual operating expense is the Annual OPEB Cost.

For the fiscal year beginning July 1, 2014, the District’s Annual OPEB Cost is **$558,684**. A detailed derivation of this amount is shown in Exhibit 2. For the 2015-2016 fiscal year, Annual OPEB Cost will be **$580,449**.

Exhibit 3 shows a 5-year projection of expected benefits, District contributions and GASB 45 operating expense. Exhibit 4 shows a 20-year forecast of the post-retirement benefits expected to be paid in future years to all current and former employees.

Actuarial Assumptions

The assumptions are described in detail in Exhibit 7 of this report. The calculated results are highly dependent on the assumptions selected.

Exhibit 1 - Actuarial Values as of July 1, 2014

The Actuarial Present Value of Total Projected Benefits as of July 1, 2014 of all future benefits from the program, for all current and former employees, is as follows:

	Certificated	Classified	Management *	Total
Current Employees	$ 4,724,759	$ 1,580,453	$ 399,016	$ 6,704,228
Retired Employees	814,435	283,222	381,345	1,479,002
	$ 5,539,194	$ 1,863,675	$ 780,361	$ 8,183,230

* The category "Management" also includes Confidential employees.

Number of persons included in this valuation:

Current Employees	123	46	11	180
Retired Employees	18	7	4	29

In addition to these 180 employees, there are 63 persons who are not eligible for this program because they were hired after June 30, 2010.

Statistical Averages

	July 1, 2014	July 1, 2012
Active Employees		
Number	180 employees	204 employees
Average Age	48.0 years	46.9 years
Average Service	11.9 years	10.3 years
Retired Former Employees and Surviving Spouses		
Number	29 persons	32 persons
Average Age	62.3 years	62.8 years

Source of Information

A census of all eligible District employees and retirees as of July 2014 was provided to me by the District.

Exhibit 2 - Annual OPEB Cost

In the Entry Age Normal method, the cost of each individual's OPEB benefits is amortized as a level percentage of salary over his/her working career. For each employee, a "normal cost" is computed in each year of employment, the amounts which, if accumulated during all years of employment, will at retirement are expected to be sufficient to fund the benefits for that individual. The sum of all the individual normal costs for all employees is called the Normal Cost. The accumulated value of all normal costs attributed to prior years, including the full value of benefits for all currently retired employees, is called the Actuarial Accrued Liability. The Unfunded Actuarial Accrued Liability is amortized over a period of future years. The ARC is the sum of the Normal Cost and the amortization of the Unfunded Actuarial Accrued Liability.

The Annual OPEB Cost for the 2014-2015 year is computed in this way:

1.	Normal Cost for the 2014-15 fiscal year	$ 272,445
2.	Actuarial Accrued Liability at July 1, 2014	6,085,752
3.	Value of Plan Assets	1,500,541
4.	Unfunded Actuarial Accrued Liability: 2. minus 3.	4,585,211
5.	Amortization of 4. over 25 years	289,910
6.	Annual Required Contribution (ARC): 1. plus 5.	$ 562,355
7.	Net OPEB Obligation/(Asset) at beginning of year From Exhibit 4	(541,993)
8.	One year's interest on 7.	(37,940)
9.	ARC Adjustment: amortization of 7. over 25 years	34,269
10.	**Annual OPEB Cost: 6. plus 8. plus 9.**	**$ 558,684**

Exhibit 3 - Five-Year Projection of Costs

Shown below are estimates of the way in which Annual OPEB Cost might be expected to increase over the next five years. In this illustration, it is assumed that the Normal Cost will increase 3% per year, that all actuarial assumptions will remain unchanged, and that the District will continue to fund the plan on a pay-as-you-go basis.

Fiscal Year:	2014-15	2015-16	2016-17	2017-18	2018-19
Accrued Liability	$ 6,085,752	$ 6,270,416	$ 6,445,366	$ 6,651,425	$ 6,906,248
Estimated Assets	1,500,541	1,605,579	1,717,970	1,838,228	1,966,904
Unfunded Accd Liab	$ 4,585,211	$ 4,664,837	$ 4,727,396	$ 4,813,197	$ 4,939,344
Normal cost	$ 272,445	$ 280,618	$ 289,037	$ 297,708	$ 306,639
Amortization	289,910	302,323	314,531	329,378	348,307
Total ARC	$ 562,355	$ 582,941	$ 603,568	$ 627,086	$ 654,946
Plus interest	(37,940)	(33,600)	(29,822)	(23,823)	(14,374)
Plus ARC adjustment	34,269	31,108	28,346	23,289	14,481
Annual OPEB Cost	**$ 558,684**	**$ 580,449**	**$ 602,092**	**$ 626,552**	**$ 655,053**
Funding by the District					
Premiums paid for retired employees	$ 307,185	$ 332,407	$ 342,865	$ 326,685	$ 285,458
Subsidized premiums	189,508	194,075	173,521	164,886	115,890
Additional funding	0	0	0	0	0
Total Funding	**$ 496,693**	**$ 526,482**	**$ 516,386**	**$ 491,571**	**$ 401,348**
Increase in net OPEB Obligation	61,991	53,967	85,706	134,981	253,705
Net OPEB (Asset) at beginning of year	$ (541,993)	$ (480,002)	$ (426,035)	$ (340,329)	$ (205,348)
Net OPEB (Asset) at end of year	**$ (480,002)**	**$ (426,035)**	**$ (340,329)**	**$ (205,348)**	**$ 48,357**

How to read this chart:

- Annual OPEB Cost: Each year's operating expense. Not the same as the ARC.
- Total Funding: Amount the District will contribute each year, equal to the amount paid to retired employees, plus subsidized premiums.
- Net OPEB (Asset) at end of year: Estimated amount on the District's balance sheet at the end of each year, as a prepaid asset.

Exhibit 4 - 20-Year Forecast of Benefit Payments

The total amounts of post-retirement benefits expected to be paid over the next twenty years, assuming that there are no significant changes to the benefits or workforce or assumptions, are:

	Premiums Paid	Subsidized Premiums	Total
2014-2015	$ 307,000	$ 190,000	$ 497,000
2015-2016	332,000	194,000	526,000
2016-2017	343,000	173,000	516,000
2017-2018	327,000	165,000	492,000
2018-2019	285,000	116,000	401,000
2019-2020	291,000	122,000	413,000
2020-2021	257,000	110,000	367,000
2021-2022	271,000	117,000	388,000
2022-2023	271,000	112,000	383,000
2023-2024	335,000	143,000	478,000
2024-2025	328,000	131,000	459,000
2025-2026	400,000	164,000	564,000
2026-2027	463,000	195,000	658,000
2027-2028	497,000	211,000	708,000
2028-2029	523,000	225,000	748,000
2029-2030	527,000	220,000	747,000
2030-2031	607,000	259,000	866,000
2031-2032	676,000	292,000	968,000
2032-2033	682,000	292,000	974,000
2033-2034	783,000	358,000	1,141,000

Exhibit 5 - Net OPEB Asset

In the vocabulary of GASB 45, the "Net OPEB Asset" is the balance sheet asset that the District should report at the end of each fiscal year. The Net OPEB Obligation or Asset is the cumulative sum of all operating expenses that have been accrued under GASB 45, minus the sum of all contributions made (and benefits paid) by the District since the adoption of GASB 45.

The Net OPEB Asset as of June 30, 2014 is developed in this way:

1.	Net OPEB Obligation as of June 30, 2012	$ (825,875)
2.	Annual OPEB Cost for the 2012-13 year	637,031
3.	Benefits paid and subsidized premiums during the 2012-13 year	547,855
4.	Net OPEB Obligation/(Asset) at June 30, 2013: 1. plus 2. minus 3.	$ (736,699)
5.	Annual OPEB Cost for the 2013-14 year	648,335
6.	Benefits paid and subsidized premiums during the 2013-14 year	453,629
7.	Net OPEB Obligation/(Asset) at June 30, 2014: 4. plus 5. minus 6.	$ (541,993)

Exhibit 6 - Summary of Plan Provisions

The District contributes toward post-retirement benefits for employees who retire after meeting certain age and service requirements.

Eligibility for benefits: Retirement from the District after attaining at least age 55, with at least 10 years of service. Also eligible if the employee had at least 30 years of service as of July 1, 2003. Employee must have been a regular permanent employee of the District for at least 10 of the last 14 years before retirement. Employees hired after June 30, 2010 are not eligible.

Benefits Paid: The District will pay 100% of the monthly premiums for medical, dental, vision and life insurance benefits. Benefits are only paid by the District until the retired employee attains age 65. Benefits are paid only for the retired employee, not for any dependents – unless the retired employee has at least 15 years of service at retirement, in which case benefits are paid for both the retiree and spouse. Benefits paid by the District are pro-rated if the retired employee was working less than full-time. The retired employee may continue coverage after age 65, and may also cover dependents that the District does not pay for, but the retiree must pay all premiums in excess of the amounts which are paid by the District.

Current Monthly Premiums. The premium amounts in effect for 2014 and 2015 are:

	Employee Only	**Employee + 1**	**Family**
2014 Rates			
Anthem Blue Cross HMO High	$ 785.77	$ 1,571.54	$ 2,223.73
Anthem Blue Cross HMO Mid	729.20	1,458.40	2,063.63
Anthem Blue Cross HMO Low	642.81	1,285.62	1,819.15
ABC HAS/PPO Plan	650.00	1,365.00	1,950.00
Kaiser (High Plan)	636.33	1,272.66	1,800.82
Kaiser (Mid Plan)	604.15	1,208.29	1,709.73
Kaiser (Low Plan)	500.38	1,000.76	1,416.08
Delta Dental PPO	87.82	161.82	248.16
Deltacare USA DHMO	33.38	55.06	81.44
Vision Service Plan	12.01	18.89	30.85
ING Life Insurance	10.00	10.58	
2015 Rates			
Anthem Blue Cross HMO High	$ 860.43	$ 1,720.86	$ 2,435.02
Anthem Blue Cross HMO Mid	798.16	1,596.33	2,258.80
Anthem Blue Cross HMO Low	703.08	1,406.17	1,989.72
ABC HAS/PPO Plan	711.75	1,494.68	2,135.25
Kaiser (High Plan)	668.60	1,337.20	1,892.14
Kaiser (Mid Plan)	634.60	1,269.20	1,795.92
Kaiser (Low Plan)	526.44	1,052.88	1,489.83
Delta Dental Premium	79.55	159.11	268.90
Deltacare USA DHMO	33.38	55.06	81.44
Vision Service Plan	12.01	18.89	30.85
ING Life Insurance	10.00	10.58	

Exhibit 7 - Summary of Actuarial Assumptions

Actuarial Assumptions: The following assumptions as of July 1, 2014 were selected by the District in accordance with the requirements of GASB 45. In my opinion, these assumptions are reasonable and appropriate for purposes of determining OPEB costs under GASB 45.

Discount rate: 7% per year. This represents what the District expects to earn on its investments over the long term (20 to 60 years) in the SISC (Self-Insured Schools of California) trust.

Mortality: Mortality rates are taken from the 2010 CalPERS OPEB Assumptions Model (for classified, management and confidential employees) and from the 2010 valuation of Cal STRS (for certificated employees). CalPERS mortality rates have been projected to future years using Scale BB to reflect anticipated improvements in life expectancy in future years. No such adjustment is needed for the STRS rates, which already include an adjustment for future longevity improvements.

Premium Increases: Dental, vision and life insurance premiums are assumed to increase 4% per year. Medical premiums are assumed to increase as follows:

2016	6.5 %
2017	6.0 %
2018	5.5 %
2019	5.0 %
2020	4.5 %
2021 and later	4.0 %

Coverage Elections: 100% of retiring employees who are eligible for benefits are assumed to elect coverage upon retirement, and to remain covered under District plans until at least age 65.

Actuarial Methods: The Normal Cost and Actuarial Accrued Liability are determined using the Entry Age Normal method, with the normal cost for each employee computed as a level percentage of salary. The Actuarial Value of Assets is the fair value of assets. The Unfunded Actuarial Accrued Liability is being amortized as a level percentage of salaries over the 30-year period beginning July 1, 2009.

Family Status: 60% of future retirees are assumed to cover a spouse, who is the same age as the retiree.

Salary increases: Salary increases are expected to be 3% per year in all past and future years.

Retirement: Retirement rates are taken from the 2010 CalPERS OPEB Assumptions Model (for classified, management and confidential employees) and from the 2010 valuation of Cal STRS (for certificated employees). Sample rates are:

	10 Years Service	20 Years Service	30 Years Service
CalPERS			
Age 55	4.8 %	7.9 %	9.9 %
Age 58	5.0 %	8.3 %	10.3 %
Age 61	9.0 %	14.9 %	18.6 %
Age 64	13.3 %	21.9 %	27.3 %
STRS Males			
Age 55	2.7 %	2.7 %	8.0 %
Age 58	2.7 %	2.7 %	14.0 %
Age 61	6.3 %	6.3 %	47.5 %
Age 64	10.8 %	10.8 %	30.0 %
STRS Females			
Age 55	4.5 %	4.5 %	9.0 %
Age 58	4.1 %	4.1 %	16.0 %
Age 61	9.0 %	9.0 %	47.5 %
Age 64	13.5 %	13.5 %	35.0 %

Baseline Medical Costs: The estimated per person baseline medical claims for covered retired employees and spouses in the 2014-2015 year are as follows (rates are shown for certain ages only):

Age	
50	$ 8,483
55	9,975
60	11,904
62	12,926
64	14,033

Turnover (withdrawal): Likelihood of termination within the next year is taken from the 2010 CalPERS OPEB Assumptions Model (for classified and confidential employees) and from the 2010 valuation of Cal STRS (for certificated and management employees). Sample rates are:

	5 Years Service	10 Years Service	15 Years Service
CalPERS			
Age 20	12.04 %		
Age 30	9.82 %	8.01 %	7.69 %
Age 40	7.58 %	5.72 %	5.34 %
Age 50	1.35 %	0.74 %	0.53 %
STRS	3.90 %	1.80 %	0.90 %