Unfunded Liabilities

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Agenda

• State of Affairs
• Bridging the Funding Gap
• State Reporting Requirements
• Accounting and Financial Reporting
State of Affairs
Current Status of Unfunded Liabilities

• **Defined Benefit (Pension) Liabilities**
  - Total Pension Liabilities = $35.4 billion
  - Total Pension Assets = $28 billion
  - Unfunded Pension Liability = $7.4 billion

• **Retiree Healthcare (OPEB) Liabilities**
  - Total OPEB Liabilities = $13 billion
  - Total OPEB Assets = $3 billion
  - Unfunded OPEB Liability = $10 billion

• **Funding levels vary significantly across communities, and the accuracy of these funding levels is highly dependent on the significant and numerous actuarial assumptions utilized**

*Financial Information from “Responsible Retirement Reform for Local Government Task Force” report prepared in July 2017*
How Did We Get Here?

• Pension and OPEB benefits used as a tool to attract and retain talent
• More prevalent defined benefit offerings by public employers
• Lack of statutory and constitutional funding requirements (OPEB)
• Actuarial assumptions used in valuations vs. reality
• Revenue challenges
Bridging the Funding Gap
Potential Plan Changes

• **Approach will be different for retirees, actives, and future hires**
  - Revisions to multipliers
  - Exclusion of items from final average compensation
  - Increased employee contributions or retiree cost sharing of health care premiums
  - Use of cash stipends as a replacement tool for retiree health care
  - Close plans – offer Defined contribution plan for new hires
  - Eligibility requirements
  - Reviewing benefits cost structure – similar benefits, offered at lower cost

• **These changes in most cases are subject to collective bargaining negotiations, which will likely result in achieving less than the desired changes**
Build Budget Capacity

• Establish a target and timeline to achieve certain funding levels – goals should include short, intermediate and long-term thresholds

• Ensure alignment between funding policy and established milestones for funding

• If there is a gap between funding required and funding available to successfully implement the funding policy, establish a methodology to “build” budget capacity over time to required thresholds
Pension/OPEB Bonds

• Public Act 46 of 2015 extended issuance until December 31, 2018
• Issuing debt to fund the Pension/OPEB liability
  • Goal:
    ▪ Fund the Pension/OPEB liability as of a certain date
    ▪ Achieve investment earnings in excess of borrowing rate
  • Challenges:
    ▪ Total OPEB Liability can be volatile
    ▪ Debt service requirement from local government
    ▪ Investments achieve a better rate than the borrowing rate
State Reporting Requirements
Public Act 202

- Annual reporting for all local governments that offer or provide defined pension and/or OPEB retirement benefits

- “Underfunded Status”
  - OPEB:
    - <40% funded based, AND
    - ARC for all OPEB systems is greater than 12% of governmental funds revenue
  - Pension:
    - <60% funded based, AND
    - ARC for all pension systems is greater than 10% of governmental funds revenue
Public Act 202

• If “Underfunded Status”
  • Community has the opportunity to file a “waiver” to provide a plan for how the underfunding is being addressed
  • If “waiver” is not approved, the local unit will need to submit a Corrective Action Plan (CAP) to the Municipal Stability Board
Public Act 202

• **CAP Considerations**
  • Pension:
    ▪ Close current benefit plans and offer defined contribution pension plan
    ▪ Limit multiplier
    ▪ Reduce of limit new accrued benefits
    ▪ Adjust Final Average Compensation

• **OPEB:**
  ▪ Close current benefit plan and offer defined contribution health care plan
  ▪ Cost sharing of premiums/copays
  ▪ Capping employer costs
  ▪ If spouse has available coverage, utilize those benefits
Accounting and Financial Reporting
Accounting and Financial Reporting

• GASB 68 (Pensions) and GASB 75 (OPEB) not only required the recording of unfunded pension and OPEB liabilities on the government-wide financial statements, they also did the following:
  • Resulted in more scrutiny of actuarial assumptions, resulting in many revisions that ultimately increased measurements of total pension and OPEB liabilities.
  • Parameters established regarding assumptions for GASB 68 and 75. These assumptions are potentially different than those used for funding valuations.
  • Disclosures regarding sensitivity to certain assumptions (discount rate and health care cost trend).
Accounting and Financial Reporting

- For local units that have significant unfunded pension and OPEB liabilities on the government-wide financial statements, it likely results in an unrestricted net position deficit.

<table>
<thead>
<tr>
<th>Net Position</th>
<th></th>
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<tbody>
<tr>
<td>Net investment in capital assets</td>
<td>$104,000,000</td>
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<tr>
<td>Restricted</td>
<td>$12,000,000</td>
</tr>
<tr>
<td>Unrestricted (deficit)</td>
<td>$(6,000,000)</td>
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<tr>
<td>Total Net Position</td>
<td>$110,000,000</td>
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Questions?
Thank you!

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