

Assumptions for June 30, 2021 OPEB Actuarial Valuation

December 2, 2021

Bill Hallmark, ASA, EA, FCA, MAAA

Michael Schionning, FSA, MAAA

Agenda



- Background
- Assumptions
 - Discount rate
 - Health care trend rates
 - Dependent coverage elections
 - Health/Dental plan elections
 - In-Lieu elections
 - 115 Trust administrative expenses
- Board Decisions



- OPEB plan is mostly closed
 - Only Tier 1 members who did not elect the VEBA can receive full benefits
 - Benefits for others who qualify for catastrophic disability
- Member contributions are fixed at 8.0% of pay
- City contributions are set by the Board
 - City can cap contributions at 11% of pay, but so far has not done so
- June 30, 2021 valuation
 - Develops City contribution for FYE 2023
 - Used as basis for GASB 74/75 reporting in September for FYE 2022

Two Types of Subsidies

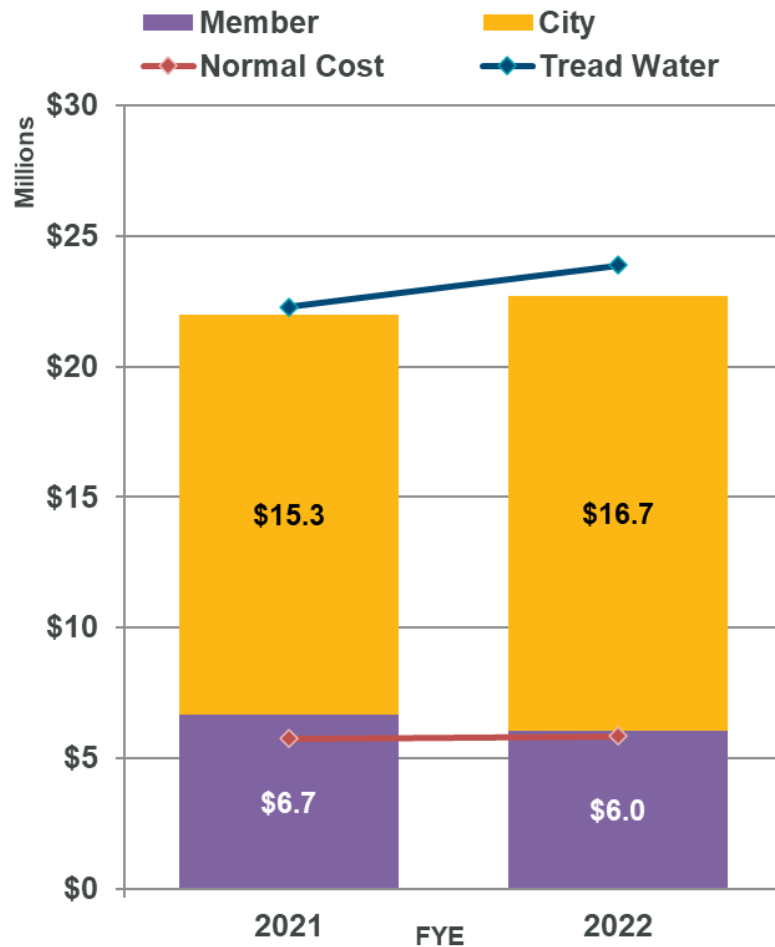


- Explicit subsidy – Pre-Funded
 - The plan pays the premium for health coverage selected by the retiree, up to 100% of the premium for the lowest cost plan offered to active employees
 - The explicit subsidy is the focus of our funding valuation
- Implicit subsidy – Pay-as-you-go
 - Difference between the expected claims cost and the total premium (retiree + plan)
 - Same premium is used for active employees and retirees not yet eligible for Medicare
 - Cost for a retiree generally exceeds the premium
 - City pays for the implicit subsidy on a pay-as-you-go basis through its premiums for active employees
 - Expected claim costs are developed using combined data for Federated and Police and Fire
 - Value is disclosed in the funding valuation and is a key part of required financial reporting

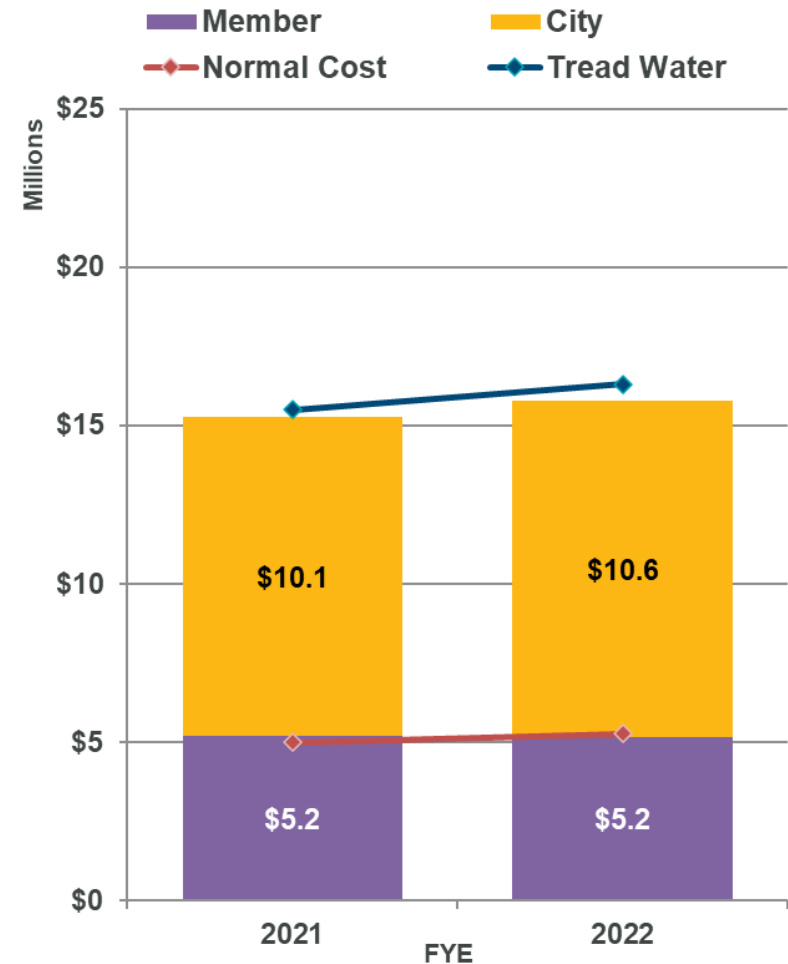
2020 Valuation Results



Contributions - Police



Contributions - Fire

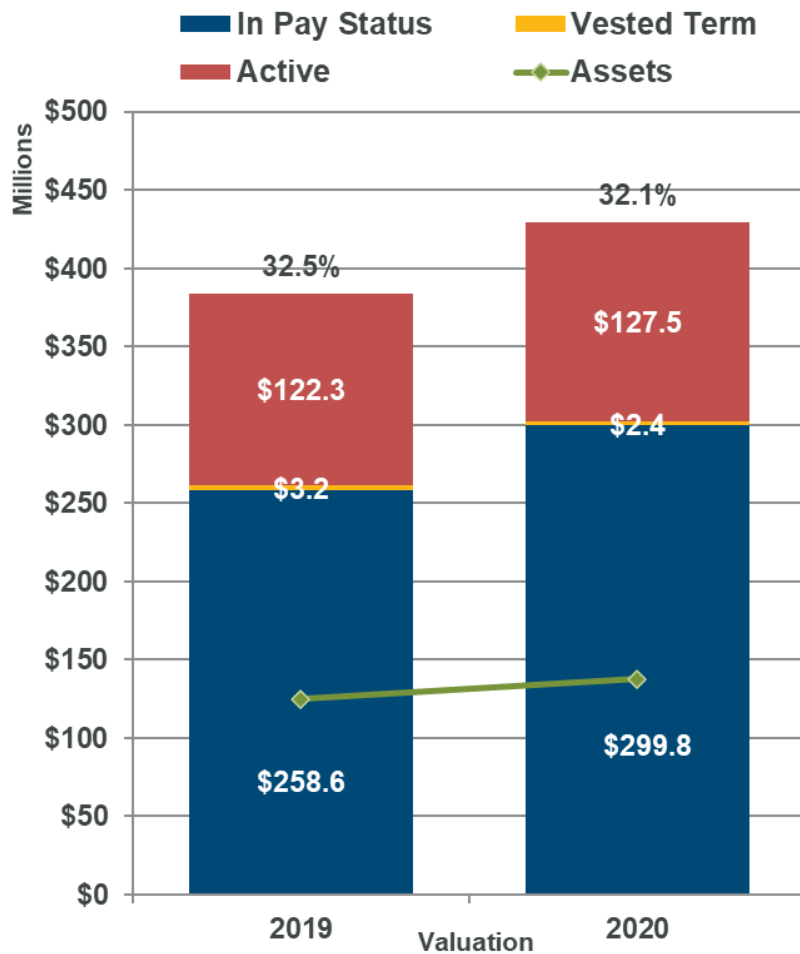


City's optional cap for FYE 2022 is approximately \$27 million

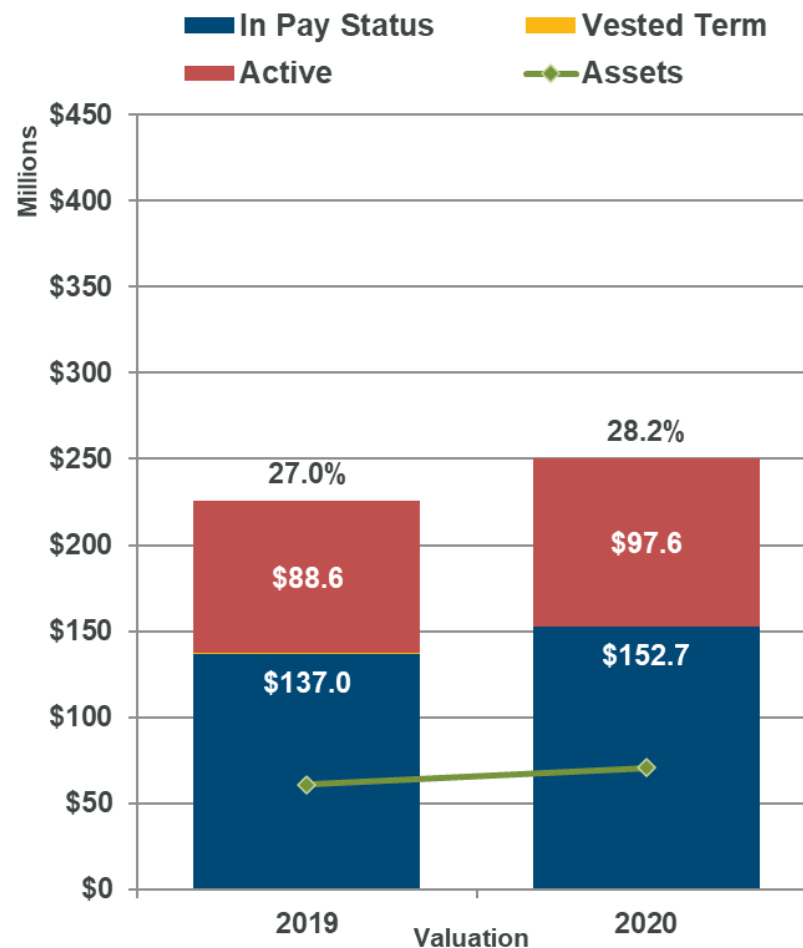
2020 Valuation Results



Funded Status - Police



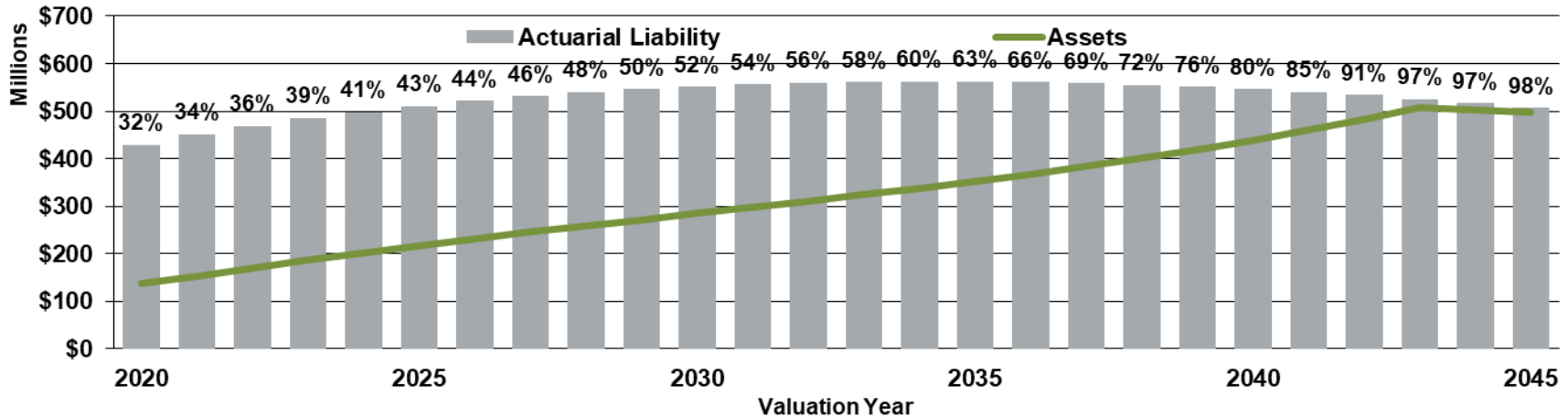
Funded Status - Fire



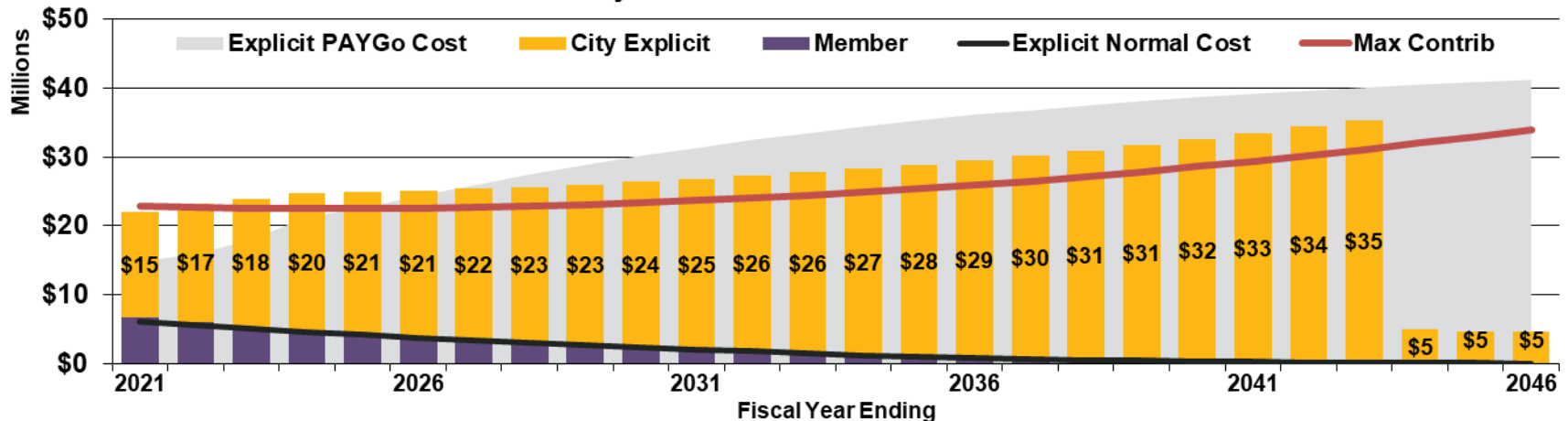
2020 Valuation Projections – Police



Projected Assets and Liabilities - Police



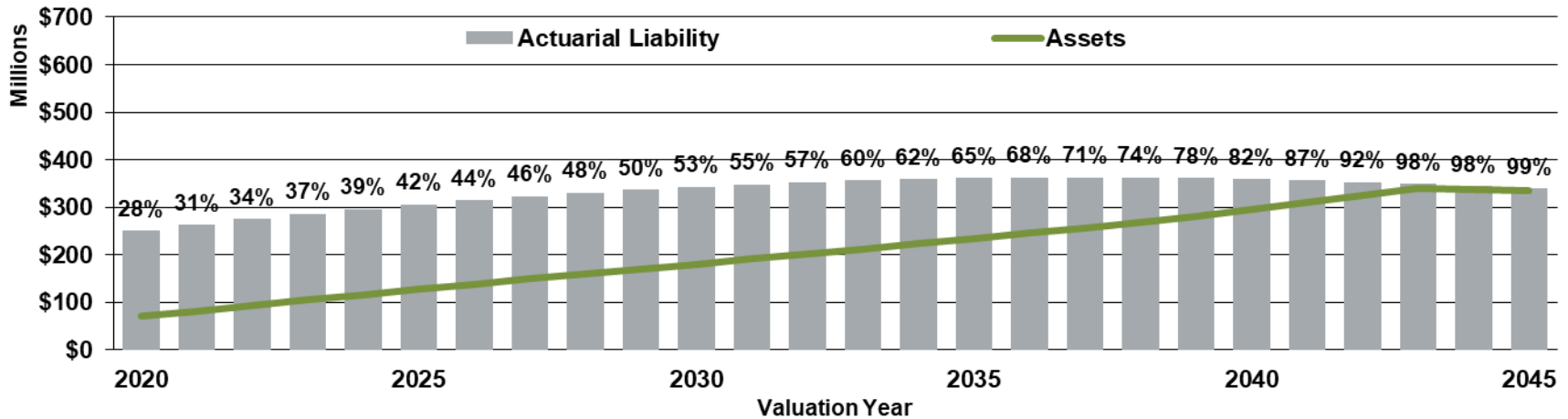
Projected Contributions - Police



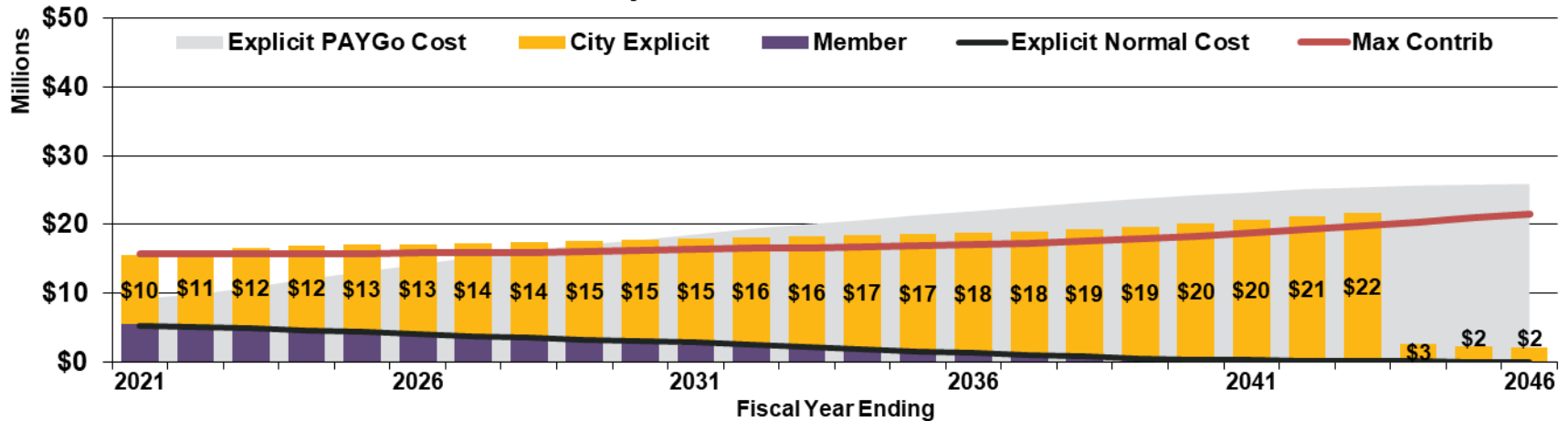
2020 Valuation Projections – Fire



Projected Assets and Liabilities - Fire



Projected Contributions - Fire



Changes in Explicit Subsidy



Maximum Annual Explicit Subsidy

Year	Member Only	Member + Spouse	Member + Child(ren)	Member + Family	Approximate Increase
2016	\$5,603	\$11,206	\$9,805	\$16,809	
2017	\$5,882	\$11,765	\$10,294	\$17,647	5.0%
2018	\$4,916	\$9,833	\$8,604	\$14,749	-16.4%
2019	\$5,340	\$10,681	\$9,346	\$16,021	8.6%
2020	\$5,807	\$11,615	\$10,163	\$17,422	8.7%
2021	\$6,172	\$12,344	\$10,801	\$18,516	6.3%
2022	\$6,120	\$12,288	\$10,752	\$18,431	-0.8%

- Maximum explicit subsidy = premium for the lowest cost health plan offered to active employees
 - Changes in 2022 from the Kaiser \$3,000 deductible plan to the Anthem \$1,500 Deductible Select HMO for member only coverage
 - Remains the Kaiser \$3,000 deductible plan for all other coverage levels
- Maximum explicit subsidy decreases by 0.84% for member only coverage and by 0.46% for all other coverage levels compared to the assumed increase of 8.0%
 - All pre-Medicare plans receive maximum subsidy
 - All Medicare-eligible plans now have premiums below the maximum subsidy
 - Medicare eligible plan premiums decreased 0.5% to 3.1%



OPEB Assumptions

Summary of Recommendations



OPEB Assumption	Recommendation
Discount Rate	<ul style="list-style-type: none">• Current assumption (6.25%) remains reasonable but is at high end of range<ul style="list-style-type: none">• 6.25%• 6.00%• Lower
Health Care Trend Rates	<ul style="list-style-type: none">• Update short-term trends
Dependent Coverage Elections	<ul style="list-style-type: none">• No changes
Health/Dental Plan Elections	<ul style="list-style-type: none">• Minor change to include new health plan
In-Lieu Elections	<ul style="list-style-type: none">• Increase proportion of Medicare eligible members assumed to qualify for retiree plus spouse coverage credit
115 Trust Administrative Expenses	<ul style="list-style-type: none">• Decrease per person administrative expenses
Claims costs	<ul style="list-style-type: none">• No changes in assumptions used to develop claims costs

Expected Return on Assets



- Different asset allocation than pension trust
- Meketa provided forward-looking capital market assumptions for 2021
 - 10-Year time horizon
 - 20-Year time horizon
- Horizon survey includes 39 consultants over a 10-year horizon and 24 consultants over a 20-year horizon
- Lower interest rates and higher valuations have reduced future expected returns

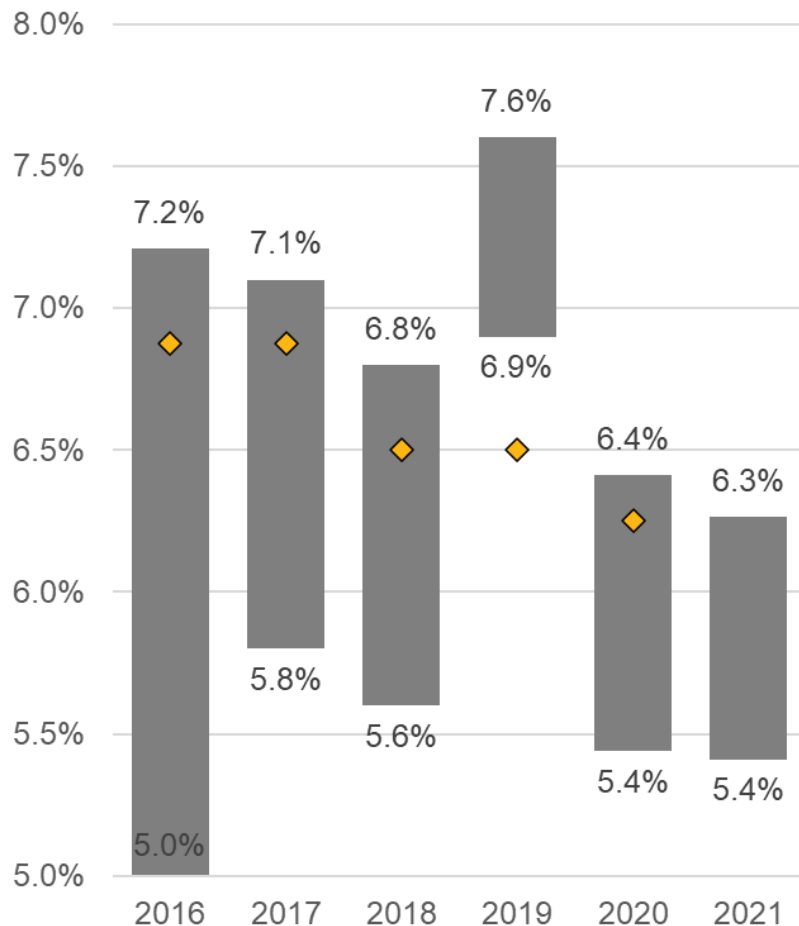
Expected Distribution of Average Annual Passive Returns				
Percentile	10-Years		20-Years	
	Meketa	Horizon	Meketa	Horizon
95th	11.68%	12.17%	10.60%	11.10%
75th	7.84%	8.24%	7.92%	8.35%
60th	6.21%	6.58%	6.77%	7.18%
55th	5.73%	6.08%	6.43%	6.83%
50th	5.25%	5.59%	6.09%	6.48%
45th	4.77%	5.11%	5.76%	6.14%
40th	4.29%	4.61%	5.41%	5.79%
25th	2.72%	3.01%	4.30%	4.65%
5th	-0.82%	-0.60%	1.77%	2.06%

We did not exactly match Meketa's geometric return calculations. Meketa's calculations produced median returns of 5.41% over 10 years and 6.27% over 20 years.

Expected Return on Assets



10-20 Year Expected Return on Assets
vs. Discount Rate



- Capital market assumptions fluctuate
 - Interest rates
 - Valuations (P/E ratios)
- Discount rate typically falls between 10- and 20-year expectations
 - 10 years ~ 40% of the present value of benefits
 - 20 years ~ 70% of the present value of benefits
- Current discount rate of 6.25% remains reasonable but at the high end
 - May consider reduction to 6.0% or lower

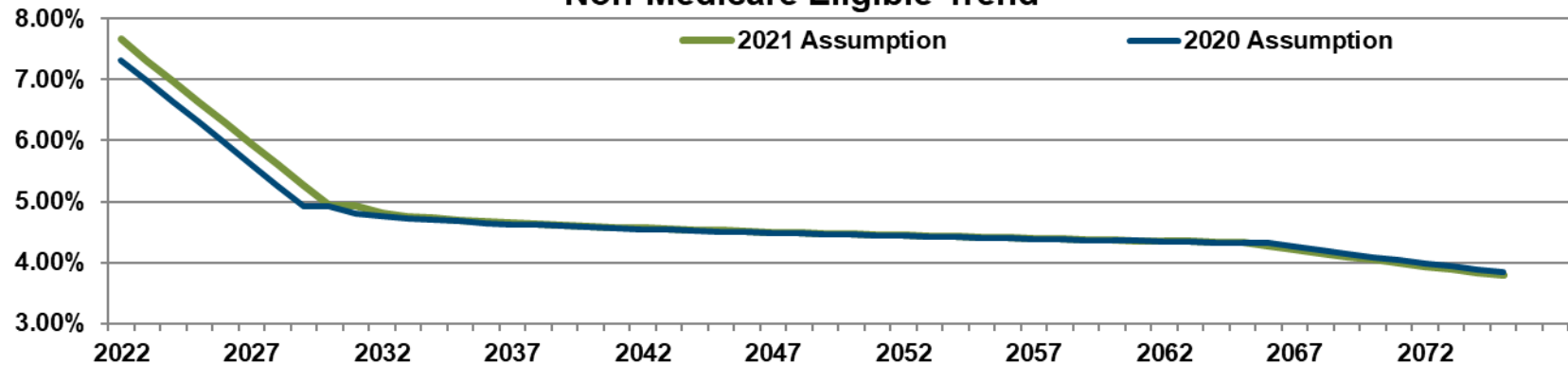


- Developed medical trend assumptions using 2021 Getzen model published by the Society of Actuaries
 - Initial trends reflect short-term expectations
 - Non-Medicare Eligible = 7.66%
 - Medicare Eligible = 4.10%
 - Adjusts linearly to long run trend of 4.93% in 2030
 - Nominal per capita GDP growth plus 1.1% excess medical cost growth
 - Grades down to nominal per capita GDP growth of 3.78% in 2075
- The trend for dental remained at 3.5% for all years

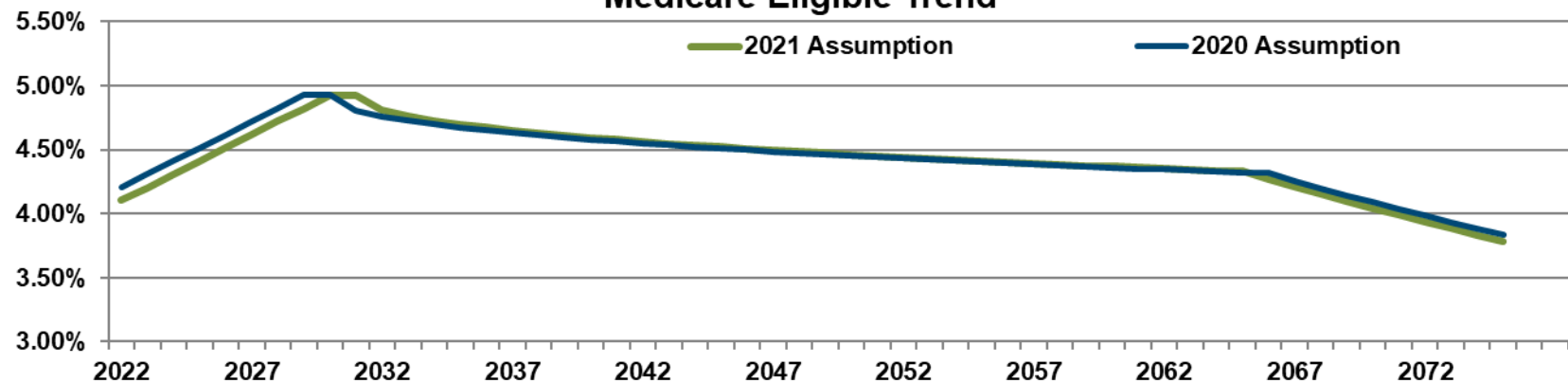
Comparison of Health Trend Rates



Non-Medicare Eligible Trend



Medicare Eligible Trend



Health/Dental Plan Elections



Assumed Plan Elections for Future Retirees*			
	2020 Valuation	2021 Enrollment	2021 Valuation
Pre-Medicare Medical Plans			
Kaiser DHMO	4%	5%	4%
Kaiser \$25 Co-pay	62%	62%	62%
Kaiser HDHP	6%	6%	6%
Anthem DHMO	2%	3%	2%
Anthem Select \$20 Co-pay	9%	9%	8%
Anthem Traditional \$20 Co-pay	N/A	N/A	1%
Anthem HDHP PPO	7%	9%	7%
Anthem Select PPO	8%	6%	8%
Anthem Classic PPO	2%	2%	2%
Medicare-Eligible Medical Plans			
Kaiser Senior Advantage	43%	43%	43%
Anthem Medicare HMO	1%	1%	1%
Anthem Medicare PPO	56%	56%	56%
Dental Plans (All Retirees)			
Delta Dental PPO	99%	99%	99%
DeltaCare HMO	1%	1%	1%

* Eligible for coverage and elect coverage

- 2021 enrollment elections only differ very slightly from 2020 assumptions
- No changes recommended except to allocate some of the Anthem Select Co-pay to the new Anthem Traditional Co-pay



- Measure F added an “In-Lieu” option
 - Retirees can waive health coverage in exchange for a credit equal to 25% of the explicit subsidy for the tier of coverage for which they qualify
 - Credit can be applied to pay future premiums
- Experience is very limited
 - Assumptions set last year based on 3 years of experience
 - Re-assess this year based on another year of experience

In Lieu Coverage Tier / Duration



- In-Lieu Coverage Credit
 - Very little data
 - Assumed same coverage tier as other retirees
 - Recommend updating rates
 - Continue to monitor
- Duration of In-Lieu Coverage
 - Very little data on duration so far
 - Recommend continuing with current assumption of 5 years
 - Continue to monitor as experience develops

Assumed In-Lieu Coverage Tier			
	2020 Valuation	2021 Enrollment	2021 Valuation
Pre-Medicare			
Retiree Only	25%	21.3%	25%
Retiree + Spouse	20%	22.7%	20%
Retiree + Family	55%	56.0%	55%
Medicare Eligible			
Retiree Only	50%	32.1%	40%
Retiree + Spouse	50%	67.9%	60%

Administrative Expenses



- Current assumption would be \$42.23 per member for FYE 2023
 - Increases each year with assumed wage inflation
- Analysis adjusts historical administrative expenses to the current year with assumed wage inflation of 3.00% per year (3.25% prior to 2020)
- Average adjusted expense per member is increased from 2021 to 2023 with future assumed wage inflation of 3.00% per year
- We recommend an assumption of \$41 per member for FYE 2023 increasing with assumed future wage inflation
 - Partially reflects lower expenses of last three years

FYE	Adjusted Administrative Expenses	Members	Adjusted Expense / Member
2021	\$ 109,768	4,024	\$ 27.3
2020	124,955	3,936	31.7
2019	132,382	3,871	34.2
2018	173,386	3,763	46.1
2017	206,309	3,613	57.1
2016	163,178	3,613	45.2
2015	148,141	3,578	41.4
2014	127,766	3,582	35.7
2013	100,499	3,608	27.9
2021 Average Adjusted Expense / Member			\$ 38.5
FYE 2023 Expense per Member			\$ 41.0



- OPEB Assumptions as summarized on Slide 10
 - Discount rate
 - 6.25%
 - 6.00%
 - Health care trend rates
 - Dependent coverage elections
 - Health/Dental plan elections
 - In-Lieu elections
 - Administrative expenses



- The purpose of this presentation is to present recommended assumptions for the June 30, 2021 Valuation for the City of San José Police and Fire Department Postemployment Healthcare Plan.
- This presentation was prepared exclusively for the Board of Administration for the purpose described herein. Other users of this presentation are not intended users as defined in the Actuarial Standards of Practice, and Cheiron assumes no duty or liability to any other user.
- In preparing our presentation, we relied on information (some oral and some written) supplied by the Plan. This information includes, but is not limited to, the plan provisions, employee data, and financial information. We performed an informal examination of the obvious characteristics of the data for reasonableness and consistency in accordance with Actuarial Standard of Practice No. 23.
- Cheiron utilizes ProVal actuarial valuation software leased from Winklevoss Technologies (WinTech) to calculate liabilities and project benefit payments. We have relied on WinTech as the developer of ProVal. We have a basic understanding of ProVal and have used ProVal in accordance with its original intended purpose. We have not identified any material inconsistencies in assumptions or output of ProVal that would affect this valuation.
- Health care trends for this valuation were developed using the Society of Actuaries (SOA) Long-Run Medical Cost Trend Model. The SOA Long-Run Medical Cost Trend Model and its baseline projection are based on an econometric analysis of historical U.S. medical expenditures and the judgments of experts in the field. The long-run baseline projection and input variables have been developed under the guidance of the SOA Project Oversight Group.

Certification (continued)



- We have relied on the Society of Actuaries as the developer of the Model. We have reviewed the Model and have a basic understanding of the Model and have used the Model in accordance with its original intended purpose. We have not identified any material inconsistencies in assumptions or output of the Model that would affect this valuation.
- This presentation has been prepared in accordance with generally recognized and accepted actuarial principles and practices and our understanding of the Code of Professional Conduct and applicable Actuarial Standards of Practice set out by the Actuarial Standards Board as well as applicable laws and regulations. Furthermore, as credentialed actuaries, we meet the Qualification Standards of the American Academy of Actuaries to render the opinion contained in this presentation. This presentation does not address any contractual or legal issues. We are not attorneys and our firm does not provide any legal services or advice.

William R. Hallmark, ASA, EA, FCA, MAAA
Consulting Actuary

Michael W. Schionning, FSA, MAAA
Principal Consulting Actuary

Appendix – Meketa's CMAs



Meketa's Capital Market Assumptions - Police & Fire Section 115 Trust Portfolio

Asset Class	Allocation	Standard Deviation	Geometric Return	
			10-Year	20-Year
Short-term Investment Grade Bonds	5.0%	1.0%	0.90%	1.30%
Investment Grade Bonds	14.0%	4.0%	1.20%	1.80%
Long-term Government Bonds	5.0%	12.0%	1.60%	2.50%
US Equity	30.0%	18.0%	5.20%	6.80%
Developed Market Equity (non-US)	14.0%	19.0%	6.70%	7.10%
Emerging Market Equity	15.0%	24.0%	7.50%	8.10%
Core Private Real Estate	12.0%	12.0%	5.00%	5.50%
Commodities (naive)	5.0%	17.0%	3.40%	3.70%
Total	100.0%	12.1%	5.41%	6.27%

Getzen Health Trend Model Parameters



- Initial 2021 Trend Rate (Updated from prior valuation)
 - Non-Medicare Eligible = 8.00% in 2021, 7.66% in 2022
 - Medicare Eligible = 4.00% in 2021, 4.10% in 2022
- Linear decline to long run trend in 2030
- Long run trend = 4.97% (Same as Getzen baseline)
 - Inflation = 2.25%
 - Real GDP per capita = 1.5%
 - Excess medical cost growth = 1.1%
- Capacity constraints
 - Expected GDP Share in 2030 = 20.3%
 - Resistance point = 20.0%
 - Applies resistance to growth in health spending as a percentage of GDP starting in 2030
 - Some evidence resistance already applies – health spending has declined slightly from 18.0% of GDP in 2016 to 17.9% in 2017 and 17.8% projected for 2019
 - Year limited to GDP growth = 2075

Appendix – Dependent Coverage Elections



Actual Pre-Medicare Dependent Coverage Elections



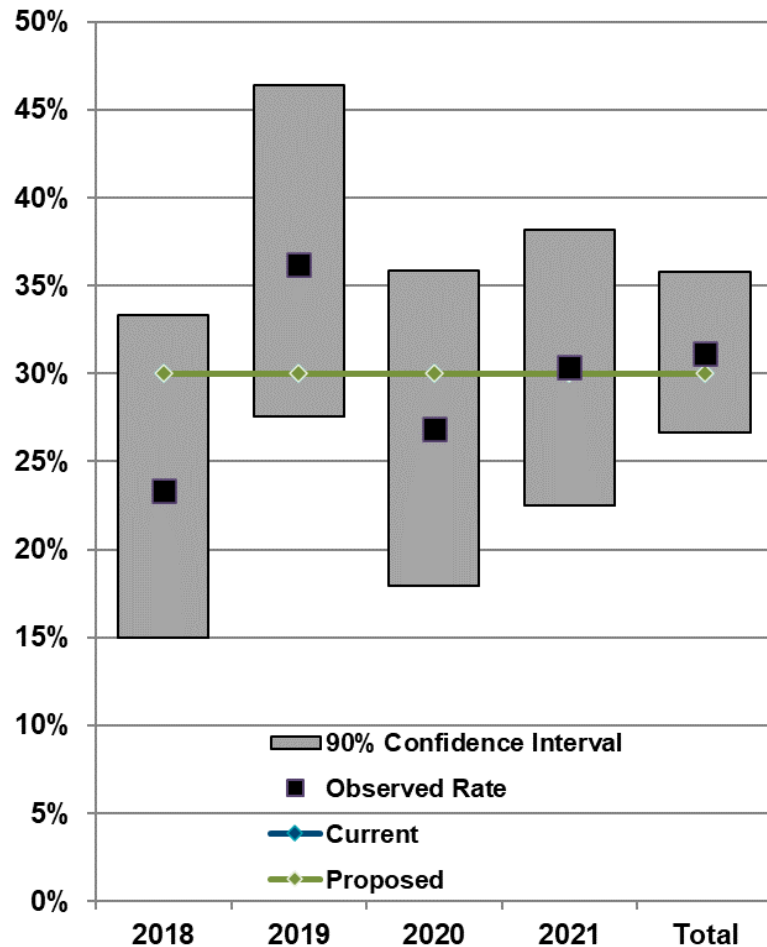
We recommend no changes

Coverage Tier	Assumed Future Retiree Tier Elections					
	Current		Proposed			
	Pre-Medicare Male	Pre-Medicare Female	Pre-Medicare Male	Pre-Medicare Female	Medicare Male	Medicare Female
Retiree Only	20%	52%	20%	52%	27%	74%
Retiree and Children	7%	22%	7%	22%	0%	0%
Retiree and Spouse	34%	13%	34%	13%	73%	26%
Retiree and Family	39%	13%	39%	13%	0%	0%

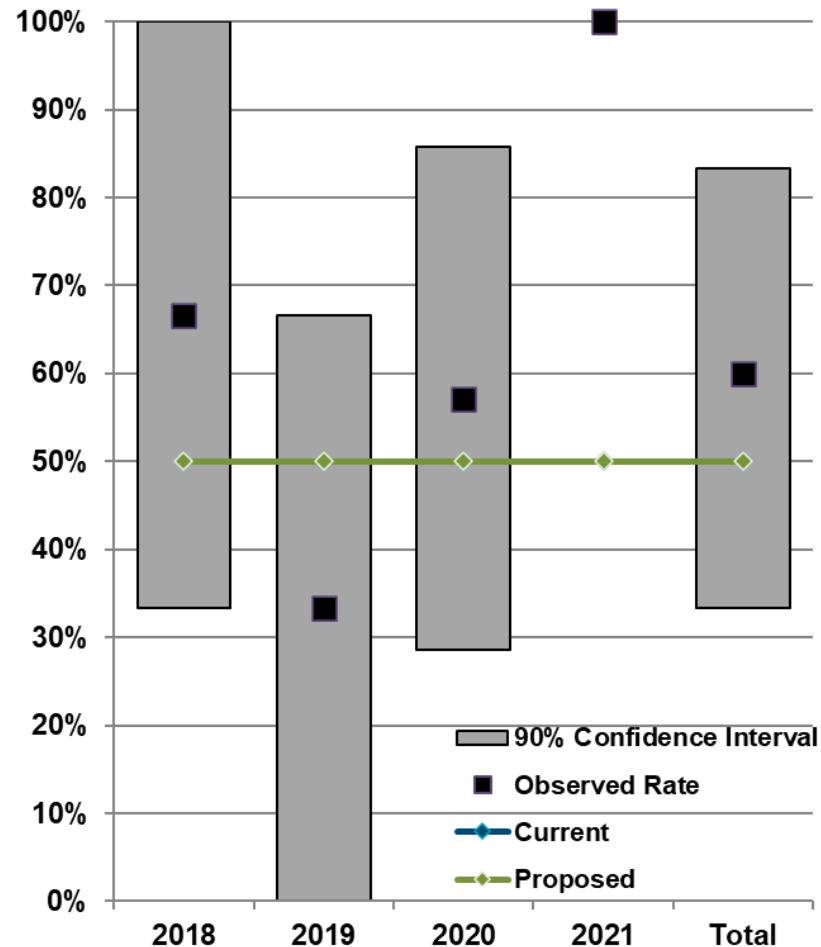
Probability Elect In-Lieu



**Probability Elect In-Lieu
Active Members**



**Probability Elect In-Lieu
Vested Terminated Members**



Appendix – Aggregate Claims Costs



- Claims costs are developed by age for each health plan offered
- Aggregate claims costs reflect the average cost based on plan election assumptions as of 7/1/2021
- Claim costs will be developed using combined data for Federated and Police and Fire

Appendix – Contribution Policy



- City contributions =
 - Normal cost +
 - Administrative expenses +
 - UAL amortization –
 - Member contributions
- UAL Amortization
 - 25 years with a 3-year phase-in and out
 - Payments increase with wage inflation each year
 - 3.00% in 2021 valuation for FYE 2023
- No asset smoothing