

San José Police and Fire
Postemployment Healthcare Plan



Assumptions for June 30, 2019 OPEB Actuarial Valuation

January 9, 2020

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Agenda



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

Background



- OPEB plan is mostly closed
 - Only Tier 1 members who did not elect 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
- June 30, 2019 valuation
 - Develops City contribution for FYE 2021
 - Used as basis for GASB 74/75 valuation in September for FYE 2020

Two Types of Subsidies

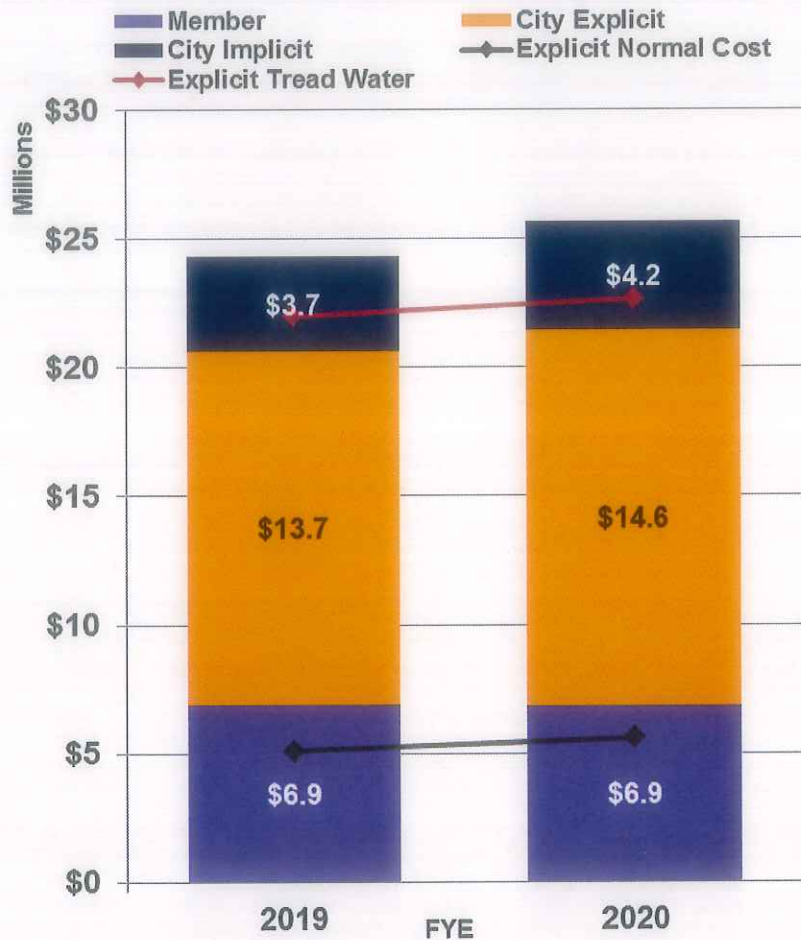


- Explicit subsidy – Pre-Funded
 - The plan pays the premium for health coverage selected by the retiree, up to 100% of the premium for the lowest cost plan offered to active employees
 - The explicit subsidy is the focus of our funding valuation
- Implicit subsidy – Pay-as-you-go
 - Difference between 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 retiree generally exceeds the premium
 - City pays for the implicit subsidy on a pay-as-you-go basis through its premiums for active employees
 - Value is disclosed in funding valuation and is a key part of required financial reporting

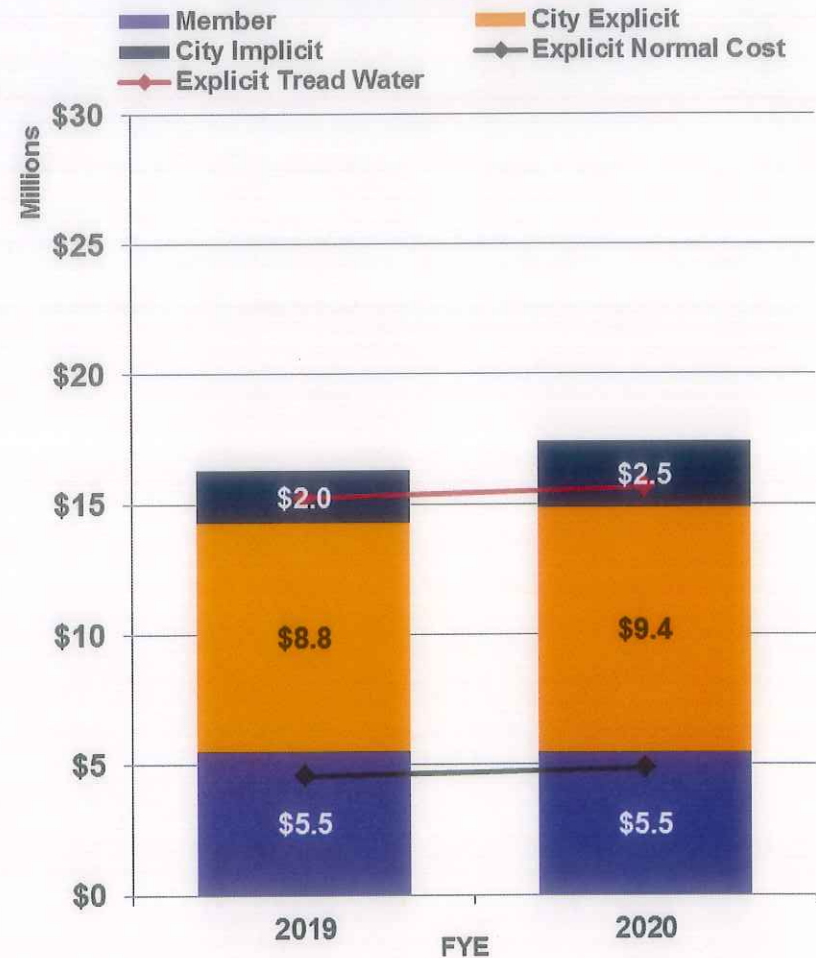
2018 Valuation Results



Contributions - Police



Contributions - Fire



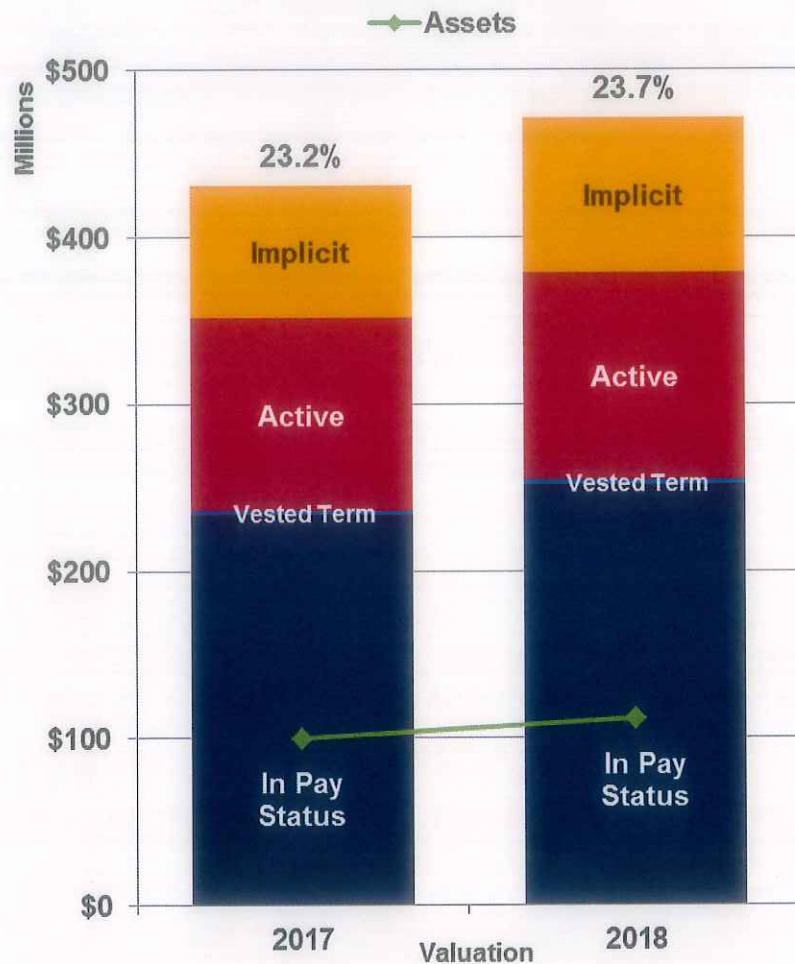
City's optional cap for FYE 2020 is approximately \$25 million

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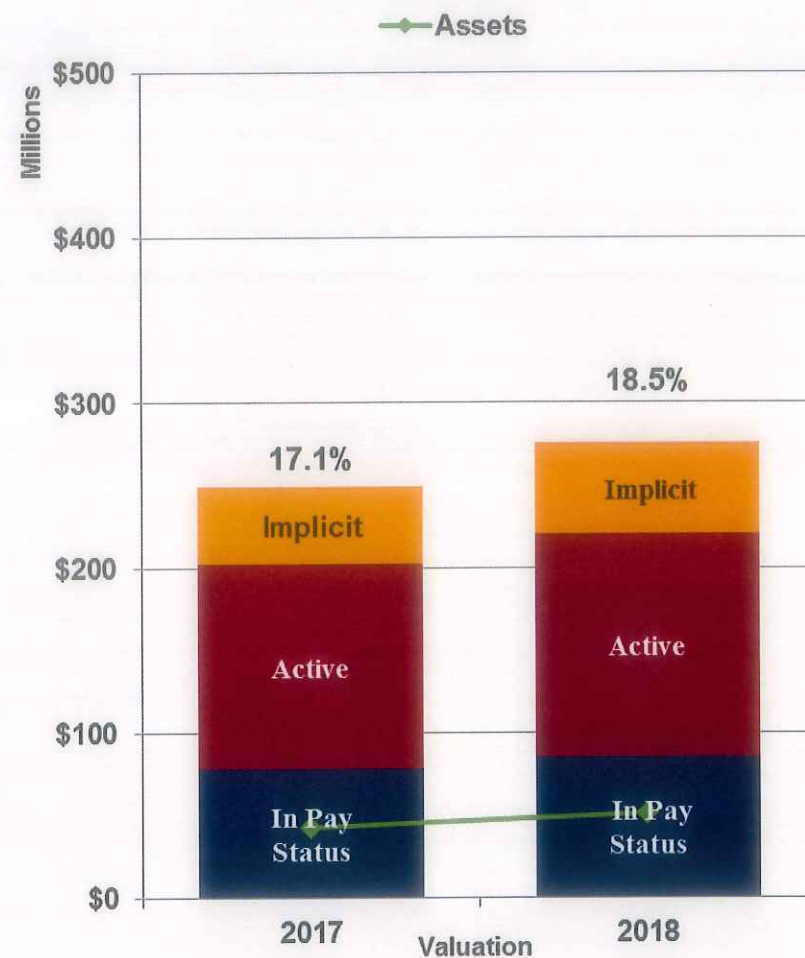
2018 Valuation Results



Funded Status - Police



Funded Status - Fire



Contribution Policy – Set by Board

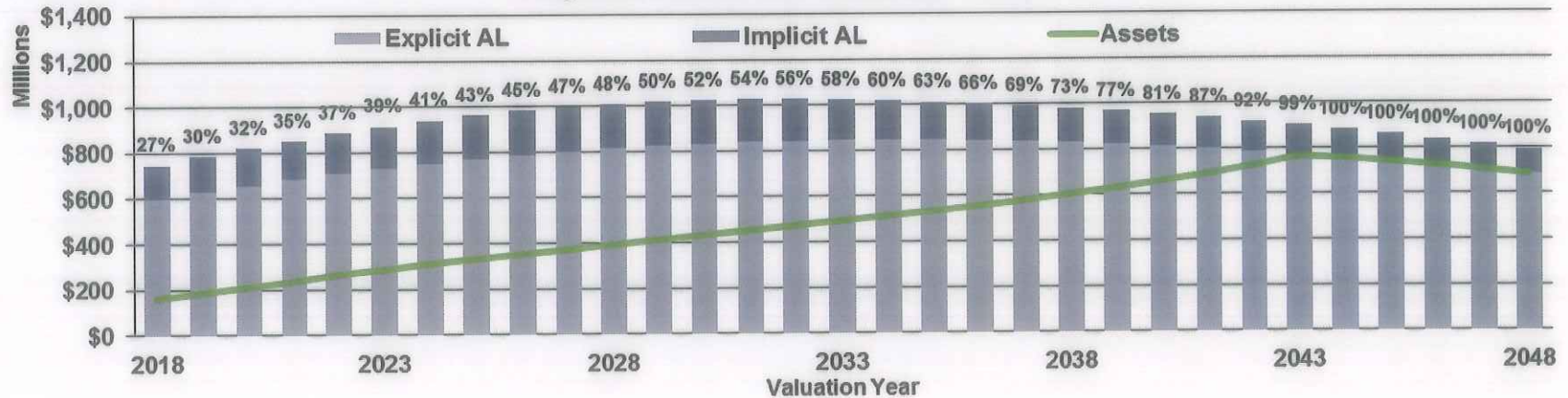


- City contributions =
 - Normal cost +
 - Administrative expenses +
 - UAL amortization –
 - Member contributions
- UAL Amortization
 - 25 years with a 3-year phase-in and out
 - Payments increase 3.25% each year
- No asset smoothing

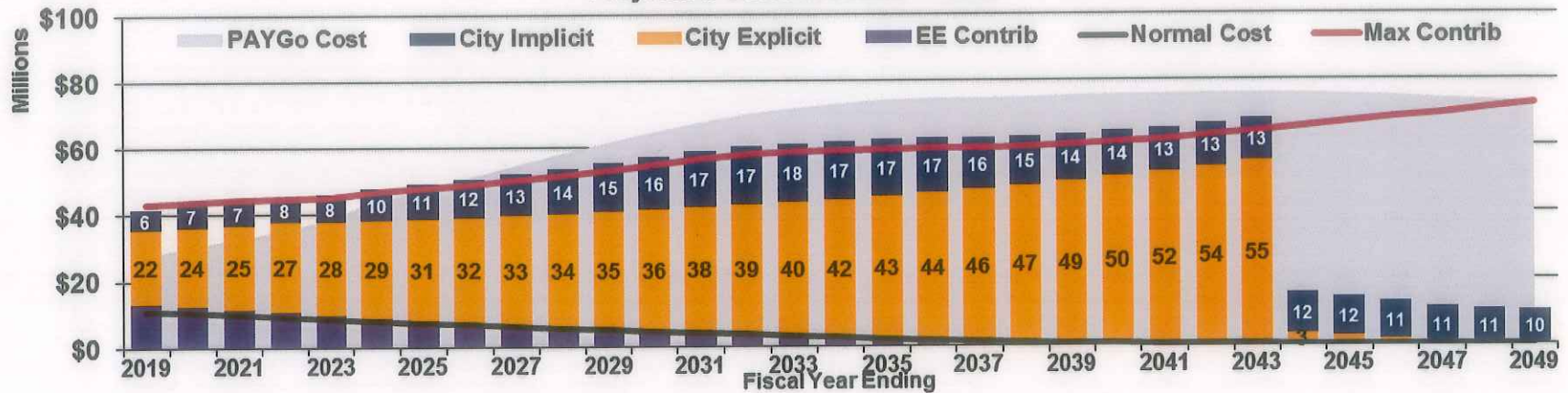
2018 Valuation Projections



Projected Assets and Liabilities - Total



Projected Contributions - Total



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Classic Values, Innovative Advice



Assumptions

Assumptions for 2019 Valuation



- Where applicable, the same assumptions are used as in the pension valuation
- OPEB assumptions:
 - Discount rate
 - Health care trend rates
 - Dependent coverage elections
 - Health/Dental plan elections
 - In-Lieu elections
 - Administrative expenses
 - Claims costs

Expected Return on Assets



- 115 Trust assets account for more than 80% of the assets
 - 115 Assets = \$149.1 million
 - 401(h) Assets = \$36.9 million
- Meketa provided forward-looking capital market assumptions
 - 10-Year Horizon
 - 20-Year Horizon
- Much of the present value of benefits is paid in the nearer term
 - 10 years ~ 40%
 - 20 years ~ 70%
- Expectations are higher than last year due to December 2018 market conditions
 - 10-year 5.6% → 6.9%
 - 20-year 6.8% → 7.6%
- Appendix shows Meketa's assumptions by asset class and the assumed asset allocation

Expected Distribution of Average Annual Passive Returns		
Percentile	Time Horizon	
	10 Years	20 Years
95th	13.0%	11.8%
75th	9.3%	9.3%
60th	7.8%	8.2%
55th	7.3%	7.9%
50th	6.9%	7.6%
45th	6.4%	7.2%
40th	6.0%	6.9%
25th	4.5%	5.9%
5th	1.1%	3.5%

Changes in Capital Market Expectations



- Meketa's capital market assumptions are developed each December
- Market conditions in December 2018 were quite different than either December 2017 or June 2019
- Expected returns from June 2019 are likely to be lower than December 2018
- Current assumption of 6.50% remains reasonable

	Dec 2017	Dec 2018	June 2019
Market Conditions			
10-Yr Treasury	2.40%	2.83%	2.07%
S&P 500	2,674	2,507	2,942
CAPE	32.1	28.3	29.5
Arithmetic Expected Returns – 10 Years			
Short-Term Bonds	1.83%	2.79%	?
US Large Cap	7.1%	7.6%	?
US Small Cap	7.8%	10.0%	?
Developed Non-US	8.1%	10.4%	?
Emerging Markets	12.1%	13.4%	?

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Changes in Explicit Subsidy



Maximum Annual Explicit Subsidy

Year	Member Only	Member + Spouse	Member + Child(ren)	Member + Family	Approximate Increase
2015	\$5,397	\$10,794	\$9,444	\$16,190	
2016	\$5,603	\$11,206	\$9,805	\$16,809	3.8%
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%

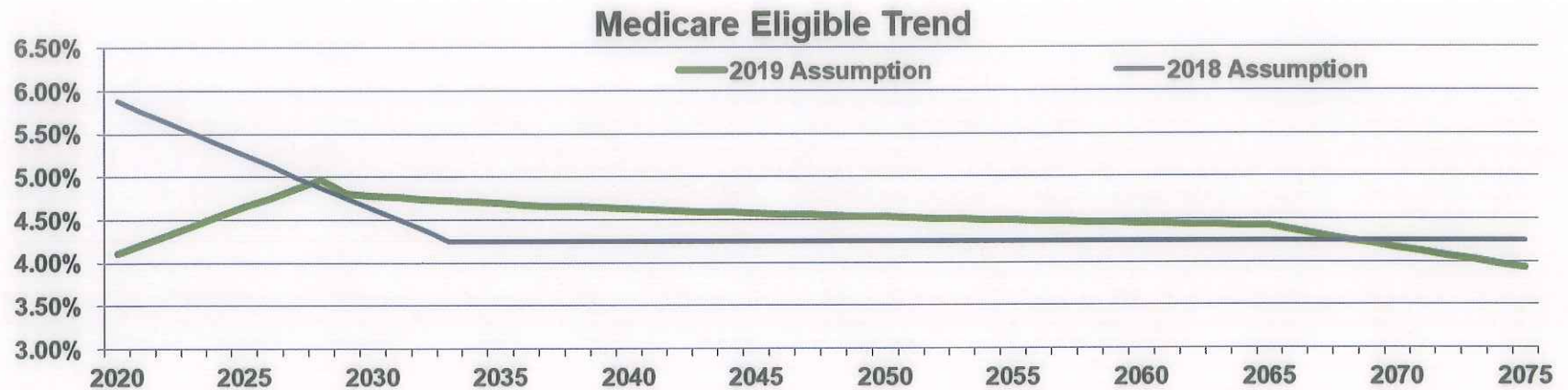
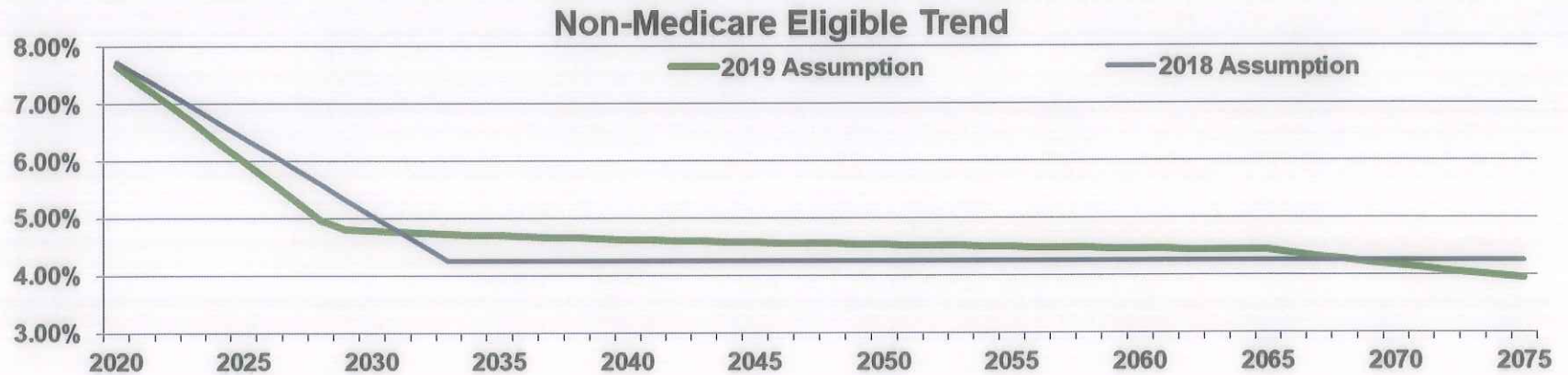
- The maximum explicit subsidy is the premium for the lowest cost health plan offered to active employees
 - The lowest cost plan in 2020 remains the Kaiser \$3,000 deductible plan
- The maximum explicit subsidy paid by the City will increase from 2019 to 2020 by 8.7% for all coverage levels
 - Assumed increase was 8.0%
 - All pre-Medicare plans receive this level of subsidy
 - Some Medicare-eligible plans have premiums below the maximum subsidy

Healthcare Trend Rates



- Developed medical trend assumptions using 2019 Getzen model published by the Society of Actuaries
 - Initial trends reflect short-term expectations
 - Non-Medicare Eligible = 7.66%
 - Medicare Eligible = 4.11%
 - Adjusts linearly to long run trend of 5.0% in 2028
 - Nominal per capita GDP growth plus 1% excess medical cost growth
 - Grades down to nominal per capita GDP growth of 3.9% in 2075
- The trend for dental remains a flat 3.5% for all years

Comparison of Health Trend Rates



Dependent Coverage Elections



Actual Pre-Medicare Dependent Coverage Elections



We recommend no changes to the assumptions

Coverage Tier	Assumed Future Retiree Tier Elections					
	Current		Proposed			
	Pre-Medicare		Pre-Medicare		Medicare	
	Male	Female	Male	Female	Male	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%

Health/Dental Plan Elections



Assumed Plan Elections for Future Retirees*			
	2019 Enrollment	2018 Valuation	2019 Valuation
Pre-Medicare Medical Plans			
Kaiser DHMO	6%	8%	8%
Kaiser \$25 Co-pay	60%	56%	56%
Kaiser HDHP	6%	5%	5%
Sutter Health / Anthem DHMO	1%	1%	1%
Sutter Health / Anthem \$20 Co-pay	9%	7%	7%
Sutter Health Vista / Anthem HDHP PPO	1%	0%	0%
Anthem Select PPO	N/A	N/A	0%
BS PPO \$25 Co-pay / Anthem Classic PPO	17%	23%	23%
Medicare-Eligible Medical Plans			
Kaiser Senior Advantage	43%	41%	41%
BS / Anthem Medicare HMO	5%	6%	6%
BS / Anthem Medicare PPO	52%	53%	53%
Dental Plans (All Retirees)			
Delta Dental PPO	99%	99%	99%
DeltaCare HMO	1%	1%	1%

* Eligible for coverage and elect coverage

- Current enrollment for 2019 was compared to the 2018 plan election assumptions
- Plan changes introduced for 2020 will impact future enrollment:
 - Sutter Health and Blue Shield plans have been replaced with Anthem options
 - Members are expected to elect the corresponding option
- We recommend no changes to the plan election assumptions

In-Lieu Elections

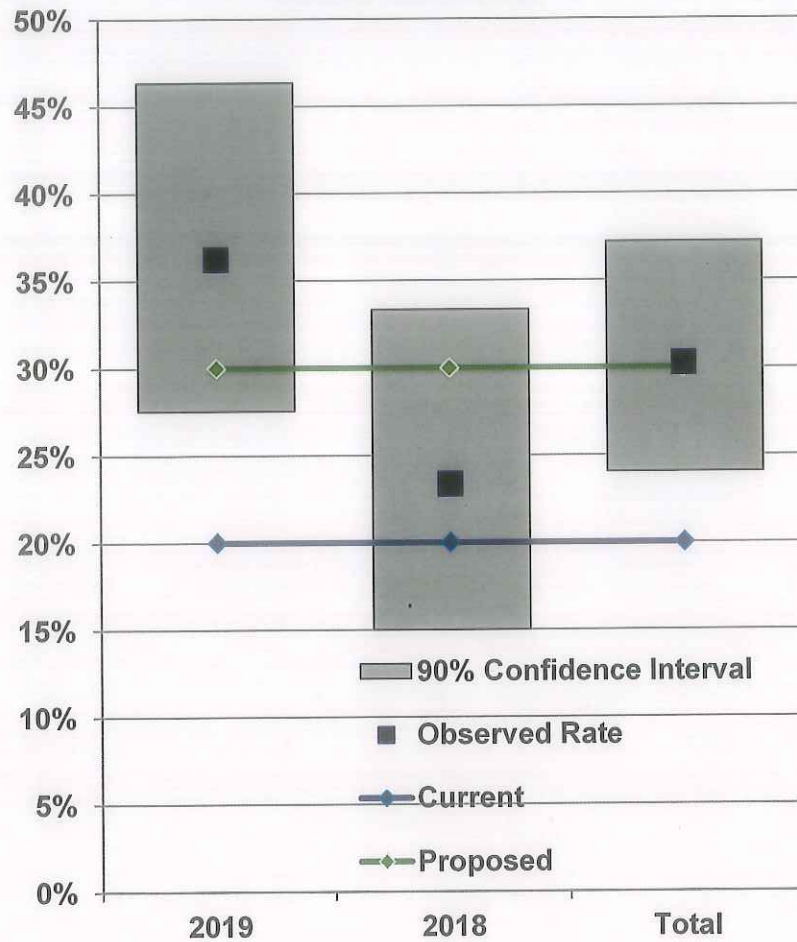


- Measure F added an “In-Lieu” option
 - Retirees can waive health coverage in exchange for a credit equal to 25% of the explicit subsidy for the tier of coverage for which they qualify
 - Credit can be applied to pay future premiums
- Experience is very limited
 - Assumptions set last year based on 0-1 years of experience
 - Re-assess this year based on another year of experience

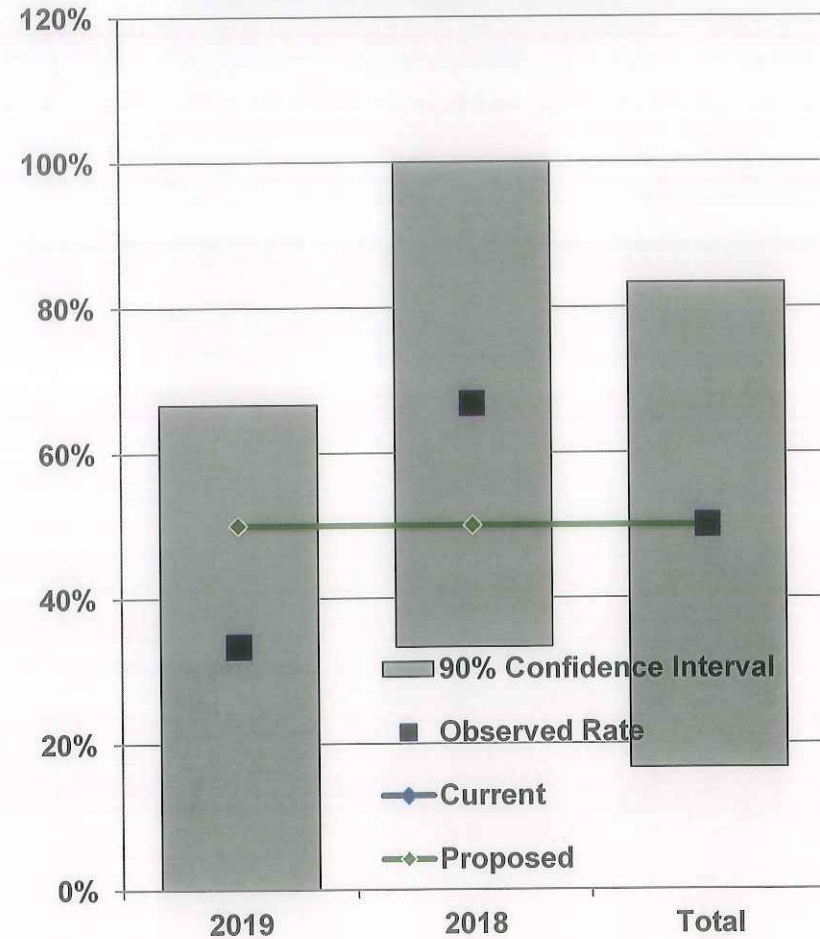
Probability Elect In-Lieu



Probability Elect In-Lieu
Active Members



Probability Elect In-Lieu
Vested Terminated Members



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In Lieu Coverage Tier / Duration



- In-Lieu Coverage Credit
 - No data for 2018 assumptions
 - Assumed same coverage tier as other retirees
 - Minor adjustments with first year of data
 - Continue to monitor
- Duration of In-Lieu Coverage
 - No data for 2018 assumption
 - 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			
	2019 Enrollment	2018 Valuation	2019 Valuation
Pre-Medicare			
Retiree Only	24.8%	25%	25%
Retiree + Spouse	26.7%	30%	25%
Retiree + Family	48.6%	45%	50%
Medicare Eligible			
Retiree Only	66.7%	60%	60%
Retiree + Spouse	33.3%	40%	40%

Administrative Expenses



- Historical administrative expenses are adjusted to 2019 with wage inflation of 3.25% per year
- Average adjusted expense per member is increased to 2021 with future wage inflation
- We recommend an assumption of \$41 per member for FYE 2021 increasing with future wage inflation

FYE	Adjusted Administrative Expenses	Members	Adjusted Expense / Member
2019	\$ 124,481	3,871	\$ 32.2
2018	163,037	3,763	43.3
2017	193,995	3,613	53.7
2016	153,438	3,613	42.5
2015	139,299	3,578	38.9
2014	120,140	3,582	33.5
2013	94,501	3,608	26.2
2019 Average Adjusted Expense / Member			\$ 38.6
FYE 2021 Expense per Member			\$ 41.0

Aggregate Claims Costs



Age	FYE 2020		FYE 2019		% change	
	Male	Female	Male	Female	Male	Female
Medical						
50	\$11,492	\$13,046	\$12,430	\$14,111	-7.5%	-7.5%
55	\$12,797	\$13,893	\$13,840	\$15,026	-7.5%	-7.5%
60	\$15,034	\$14,655	\$16,259	\$15,850	-7.5%	-7.5%
64	\$17,753	\$14,447	\$19,199	\$15,624	-7.5%	-7.5%
65	\$4,676	\$4,125	\$4,848	\$4,277	-3.6%	-3.6%
70	\$4,965	\$4,205	\$5,148	\$4,360	-3.6%	-3.6%
75	\$5,707	\$4,729	\$5,917	\$4,903	-3.6%	-3.6%
80	\$6,480	\$5,363	\$6,719	\$5,561	-3.6%	-3.6%
85	\$6,998	\$5,861	\$7,256	\$6,077	-3.6%	-3.6%
Dental	\$715		\$716		-0.2%	

- 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 1/1/2019
- Aggregate claims costs for FYE 2020 are lower than expected

Board Decisions



- Discount rate
- Health care trend rates
- Dependent coverage elections
- Health/Dental plan elections
- In-Lieu elections
- Administrative expenses
- Claims costs

Certification



- The purpose of this presentation is to present recommended assumptions for the June 30, 2019 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.
- 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.

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Principal Consulting Actuary

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Appendix – Meketa's CMAs



Federated Postemployment Healthcare Plan Portfolio Meketa's Capital Market Assumptions

Asset Class	Allocation	Standard Deviation	Arithmetic Return	
			10-Year	20-Year
Short-term Investment Grade Bonds	29.0%	1.0%	2.8%	3.4%
US Equity	28.0%	17.0%	7.8%	9.5%
Developed Market Equity (non-US)	13.0%	19.0%	10.4%	10.3%
Emerging Market Equity	15.0%	24.0%	13.4%	13.3%
Real Estate	10.0%	15.0%	7.6%	8.1%
Commodities: Real Return	5.0%	20.0%	8.0%	7.2%
Total	100.0%	11.5%	7.5%	8.2%
		Geometric Return	6.9%	7.6%

Getzen Health Trend Model Parameters

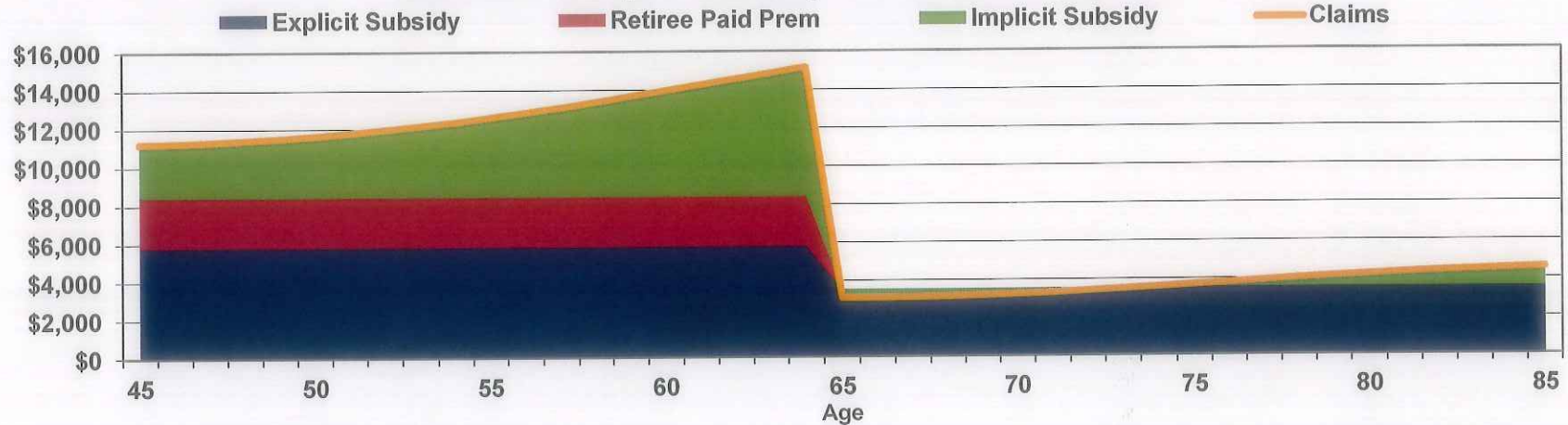


- Initial 2019 Trend Rate (Updated from prior valuation)
 - Non-Medicare Eligible = 8.00%
 - Medicare Eligible = 4.00% in 2019, 4.11% in 2020
- Linear decline to long run trend in 2028
- Long run trend = 4.97% (Same as Getzen baseline)
 - Inflation = 2.5%
 - Real GDP per capita = 1.4%
 - Excess medical cost growth = 1.0%
- Capacity constraints
 - Expected GDP Share in 2028 = 20.5%
 - Resistance point = 20.0%
 - Applies resistance to growth in health spending as a percentage of GDP starting in 2029
 - 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

Illustration of Subsidies



Illustration of Implicit Subsidy - Kaiser \$25 Co-pay Plan



Member Age 64 Illustration

	2019	2020	% Change
Explicit Subsidy	\$ 5,340	\$ 5,807	8.7%
Retiree Paid Premium	<u>2,401</u>	<u>2,611</u>	8.7%
Kaiser \$25 Co-Pay Plan Premium	\$ 7,741	\$ 8,418	8.7%
Implicit Subsidy	<u>9,322</u>	<u>6,752</u>	-27.6%
Total Claims	\$ 17,063	\$ 15,170	-11.1%

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Non-Medicare Plan Claims Costs



Age 64 Claims Costs

	FYE 2020		FYE 2019		% change	
	Male	Female	Male	Female	Male	Female
Medical						
Kaiser \$25 Co-Pay	\$16,604	\$13,515	\$18,698	\$15,217	-11.2%	-11.2%
Kaiser DHMO	11,315	9,207	10,390	8,459	8.9%	8.8%
Kaiser HDHP	10,484	8,534	9,196	7,485	14.0%	14.0%
BS PPO/Anthem PPO	27,265	22,179	24,967	20,313	9.2%	9.2%
Sutter/Anthem \$20 Co-Pay	17,359	14,129	22,088	17,978	-21.4%	-21.4%
Sutter/Anthem DHMO	15,101	12,292	14,809	12,050	2.0%	2.0%
Dental						
Delta PPO		\$727		\$729		0%
DeltaCare HMO		\$316		\$317		0%

Note: Anthem Blue Cross replaces Blue Shield and Sutter Health as the non-Kaiser provider as of January 1, 2020.

- Claims costs had been expected to increase
 - 8.00% for non-Medicare medical costs
 - 3.50% for dental costs
- Renewal increases were
 - In general higher than expected for all plans
 - Lower than expected for the deductible HMO plan
 - Active premiums shifted from a 2-tier structure back to a 4-tier structure
- In 2020, the Sutter and Blue Shield plans are being replaced with Anthem Blue Cross plans

Medicare Eligible Plan Claim Costs



Age 65 Claims Costs

	FYE 2020		FYE 2019		% change	
	Male	Female	Male	Female	Male	Female
Medical						
Kaiser Senior Advantage	\$3,288	\$2,900	\$3,401	\$3,000	-3.3%	-3.3%
BS PPO/Anthem PPO	5,607	4,946	5,742	5,066	-2.4%	-2.4%
BS HMO/Anthem HMO	5,936	5,236	6,831	6,026	-13.1%	-13.1%
Dental						
Delta PPO		\$727		\$729		0%
DeltaCare HMO		\$316		\$317		0%

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 - 6.00% for Medicare medical costs
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