

TO: BOARD OF SUPERVISORS
FROM: John Cullen, County Administrator
DATE: January 15, 2008
SUBJECT: OPEB – Post Retirement Medical Benefits Trust Agreement



Contra Costa County

SPECIFIC REQUEST(S) OR RECOMMENDATION(S) & BACKGROUND AND JUSTIFICATION

RECOMMENDATIONS:

APPROVE and AUTHORIZE Chair and designated Trustees to execute Post Retirement Medical Benefit Trust Agreement and Post Retirement Medical Benefits Plan for the County of Contra Costa; AUTHORIZE County Administrator to make any non-substantive changes to form of trust and plan documents.

FISCAL IMPACT:

The result of the recommendations herein, if implemented, will have significant future impact on the County's overall fiscal stability and ability to deliver services.

BACKGROUND:

On September 25, 2007 the Board of Supervisors approved the selection of an irrevocable trust structure (Internal Revenue Code Section 115) for OPEB funding for Contra Costa County and directed staff to return in January 2008 with the documents necessary to establish the trust. Attached for your Board's consideration are copies of the Retirement Medical Benefit Trust (Trust) Agreement and Post Retirement Medical Benefits Plan (Plan) for the County of Contra Costa. These documents were developed by the OPEB fiscal task force, which consists of the County Auditor-Controller, Treasurer-Tax Collector, Finance Director, Chief of Internal Audit, County Counsel, and outside tax counsel.

Trust Agreement/Benefits Plan

The purpose of the Trust is to hold assets to pay post retirement health benefits and the purpose of the Plan is to provide post retirement health benefits for certain retired employees and their spouses and dependents. The Trust will be legally established with the deposit of \$1.00 required by law during fiscal year 2007/08. It is the County's intent to begin pre-funding benefits in the 2008/09 fiscal year. The Trust, which consists of assets contributed by the County (and other participating employers), will be administered by the financial officials typically responsible for safeguarding the County's assets. For purposes of transparency, the Trustee will provide for monthly accounting of trust transactions and arrange for public distribution of this information. The Trustee shall separately account for all contributions, distributions, payments, expenses, gains and losses attributable to the County and each other Employer that participates in the Trust.

CONTINUED ON ATTACHMENT: YES

SIGNATURE: _____

____ RECOMMENDATION OF COUNTY ADMINISTRATOR ____ RECOMMENDATION OF BOARD COMMITTEE

____ APPROVE ____ OTHER

SIGNATURE(S): _____

ACTION OF BOARD ON _____ APPROVE AS RECOMMENDED _____ OTHER _____

VOTE OF SUPERVISORS

____ UNANIMOUS (ABSENT _____)
AYES: _____ NOES: _____
ABSENT: _____ ABSTAIN: _____

I HEREBY CERTIFY THAT THIS IS A TRUE AND CORRECT COPY OF AN ACTION TAKEN AND ENTERED ON THE MINUTES OF THE BOARD OF SUPERVISORS ON THE DATE SHOWN.

CONTACT: Lisa Driscoll (335-1023)

CC: All County Departments

ATTESTED _____
JOHN CULLEN, CLERK OF THE BOARD OF SUPERVISORS
AND COUNTY ADMINISTRATOR

BY _____, DEPUTY

The Trustees shall act as fiduciaries in accordance with section 17, article XVI of the California Constitution, and as such the Trustees must discharge their duties with care, skill, prudence and diligence. It is the County's intent that the Trustees will engage a professional investment manager.

Allocation of Resources/Discount Rate

It is intended that this Trust meet the requirements of GASB 45 as necessary for Trust assets to be treated as assets that reduce any liability of the County (and other Employers) for such benefits. Prefunding the County's OPEB liability using an irrevocable trust allows the County to reduce its long-term liability for retiree health benefits and use investment earnings instead of taxpayer dollars to pay future costs. The County will make regular contributions to the Trust. These funds will be professionally invested and grow similar to our CCCERA pension funds. In the future, the County can use investment earnings to pay OPEB costs, similar to our CCCERA pension plan in which four out of five dollars paid in retirement benefits come from investment earnings rather than taxpayer dollars or employer contributions. Government accounting rules allow employers that prefund to use a higher "discount rate" assumption, which reduces future OPEB liabilities on financial statements. For example, without prefunding, Contra Costa has a projected OPEB liability of \$2.6 billion. By prefunding this Trust, the County's long-term liability will be reduced to \$2.1 billion – a savings of more than \$458 million. Reducing long-term liabilities on financial statements can also result in a higher bond rating, which would reduce the County's future borrowing costs.

On June 26, 2007, the Board of Supervisors adopted the allocation of specific future eligible resources to meet the requirements for OPEB funding. The following table lists those annual resources identified thus far (in millions):

Resource	Beginning FY	Amount
Redirect Workers Compensation	2008/09	\$10
Redirect UAAL Rate Adjustment	2009/10	\$10
Redirect POB Bond payments	2014/15	\$33
Redirect POB Bond payments	2022/23	\$47
Total Annual Future Resource Redirection	2024 - onward	\$100

If these resources were to be put aside beginning in fiscal year 2008/09, there would be \$588 million (plus interest) reserved at the end of fiscal year 2022/23 and \$100 million would be available to be added annually thereafter. In the aggregate, the total potential liability will be even less. The reserved money will be earning a rate of return indicative of a diversified portfolio rather than the lower rate of return of the County's cash pool. Additionally, the Board is committed to a balanced approach to prefunding more of the liability, which will involve reductions of both benefits and services. These actions will further reduce the OPEB liability in future valuations.

IRS Ruling

It is the County's intent to eventually request an IRS ruling on the tax-exempt status of this Trust. Because the Governor's Public Employees Post-Employment Benefits Commission has identified several barriers in the tax laws to efficient operation of public sector retiree health benefits, and the Commission has already started discussions with the IRS to clear these matters up, the County will wait until the Commission's receives the IRS response before requesting it's a ruling. The Trust documents have been drafted to comply with IRS requirements for tax-exempt status.

CalPERS Retiree Health Prefunding Plan

In March of 2007, the California Employers' Retiree Benefit Trust Fund was established, which is the CalPERS equivalent to the trust fund before you today. Technically, Contra Costa County is not currently eligible to put funds into this trust due to the methodology and assumptions used in our 2006 actuarial valuation. The CalPERS Retiree Health Prefunding Plan requires very specific methodology and assumptions be used in calculation of the OPEB liability. Contra Costa is CalPERS compliant on all but one item. CalPERS requires the use of the entry age normal actuarial funding method and Contra Costa used projected unit credit. GASB 45 allows for any one of 6 funding methods to be chosen by the plan sponsor but the funding method is the one item on which CalPERS is very restrictive. CalPERS' advice on requiring the entry age normal actuarial

funding method was new in 2007, when they started their trust fund for postretirement medical plans. The County's 2006 valuation was completed prior to the announcement of CalPERS requirement. In the future, should the Board wish to move to the California Employers' Retiree Benefit Trust Fund the County can perform a new valuation and change this assumption.

There are several reasons why a local independent trust currently appears to be a better option for Contra Costa County:

1. Once an entity joins the CalPERS trust, it is difficult to move to another option should a better option emerge. For example, PERS allows the transfer of money to another 115 trust but only if the PERS Board agrees that it is in fact exempt under IRS Code section 115. The PERS Board has not set any standards for this decision and based on PERS rules for transferring from the retirement system, it is likely that the standards will be very conservative. This may mean that the County would face a lengthy delay in moving out of the PERS trust.
2. The California Employers' Retiree Benefit Trust Fund investments are not the same as the CalPERS retirement fund investments. PERS cannot commingle the retiree health assets with the retirement assets and instead is required to have "parallel investments". As a practical matter, it is very unlikely that parallel investing will get the same return as the CalPERS retirement fund investments because of limits on health trust investments in private placements, inability to invest in illiquid but high performing assets like timber, etc.
3. The Benefit Trust Fund will be controlled by the CalPERS Board. There is only one representative on the CalPERS Board from local agencies.
4. The Benefit Trust Fund is new and therefore has no track record, in any manner including administration.
5. There are issues under the contract the County would be required to enter with CalPERS. For example, CalPERS would have ability to draw money from each agency's account to pay for administrative expenses, with no limit on the amount that can be withdrawn. Also CalPERS has not made available any governing trust instrument, and we are informed that they do not intend to establish one. Further, CalPERS has stated that it does not intend to ask the IRS for a ruling on its OPEB trust.
6. CalPERS will not indemnify the County for CalPERS' errors in administration of the Benefit Trust Fund. For example, if CalPERS does not pay a health insurance carrier and coverage is lost and the County is sued, the County has no assurance that it will recover losses arising from CalPERS' errors.

Conclusion

In terms of an OPEB trust structure, there will most likely be many good alternatives within the next 2-3 years of which the County may want to take advantage.. Creation of a County 115 trust would be an interim decision. This interim option would have all the advantages of the CalPERS trust and none of the disadvantages. After there are track records of trust options including the County's Trust and the CalPERS trust, the County can revisit the decision on which trust or trusts to use.