# OPEB and Defined Benefit Pension Plan

# Funding Situation Summary

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## Intent

The intent of this document is to summarize two issues we are currently facing. The first is the low funding level of Other Postemployment Benefits (OPEB). Addressing this issue will include developing a Corrective Action Plan that meets state specifications under Public Act 202 of 2017. The second issue is how to fund the annual payment into the Defined Benefit Pension Plan called the Actuarially Determined Contribution (ADC). This amount has to be paid per the state constitution and other statutes.

These two separate issues are closely related. We need to understand the situation, how it came to be, its seriousness and the potential consequences. This summary outlines the initial steps taken to address the situation and proposes further action.

## Background

### OPEB

In December 2017, Gov. Rick Snyder signed Michigan Public Act 202 – Protecting Local Government Retirement and Benefits Act – into law. The state took this action because of the growing cost of retiree health care systems paired with high levels of underfunding among governmental units across the state. Statewide there are 340 local OPEB systems with $3 billion in assets, $12.1 billion in liabilities and about $9.1 billion in unfunded liabilities. Employer contributions are averaging $530 million annually with required contributions of about $800 million. (Source: State of Michigan, Department of Treasury).

This is having a profound effect on many Michigan communities. Unfortunately, Bloomfield Township falls into the category of communities that have not funded the retiree health care system to the level that the state now requires. The Township, like many other Michigan communities, fails to meet the 40% minimum funding level, and the second requirement that the annual required contribution (ARC) not exceed 12% of governmental fund revenues. For the fiscal year ending March 31, 2017, the Township was 3.5% funded and the ARC as a percentage of governmental fund revenues was 24.9%. On a pay-as-you-go basis, the retiree health care plan premiums are 6.7% of governmental fund revenues, well below the 12% mandate.

Currently, the Township has approximately $172 million of retiree health care liabilities, of which approximately $162 million has not been funded; a funded ratio of 5.8%. Contributing to the problem is the continuously rising health care premiums. As recently as seven years ago, the total liability was only $87 million.

To date the Township has had no difficulty meeting the health care demands for retirees by operating on a pay-as-you-go basis, meaning we are paying the monthly premiums out of our operating budgets. However, the state wants to see municipalities move away from pay-as-you-go and fund these liabilities to a higher degree.

Under PA 202 of 2017, the Township filed required form 5572. Next, the Township filed a Waiver Application, form 5584. The state denied the waiver which means the Township must develop a Corrective Action Plan. This first must be approved by the Board of Trustees and then submitted to the state Municipal Stability Board (MSB) before November 13, 2018. The MSB will review it and decide whether it's sufficient or not in addressing the Township's unfunded liability. The MSB recently released examples of what they would like to see included in the Corrective Action Plan.

**Defined Benefit Pension Plan**

The Township made a significant move in controlling its pension costs in 2005 when it switched from a Defined Benefit pension plan to a Defined Contribution pension plan. In 2013, the Township made another significant and proactive decision to sell pension obligation bonds to fully fund the Defined Benefit pension plan trust.

While the Township issued bonds to cover the pension obligation, the funding level has been decreasing annually since the bond sale. The trust is now below 100% funded and has an Actuarially Determined Contribution (ADC). This is due to many factors including our population's mortality rates and the assets not meeting the actuarially projected return. Most recently the actuary reduced the assumed rate on Township investments from 6% to 5.75%.

As a result, in our current budget year the Township is facing an unexpected expense of $3.7 million. This expense is expected to continue each year for the foreseeable future with a potential to grow larger. This ADC payment is unrelated to PA 202; we would be facing this issue even if this act was not signed into law.

Under Public Act 202, a local unit of government's Defined Benefit pension plan is considered underfunded if it is less than 60 percent funded and the contribution for all of the retirement pensions systems is greater than 10 percent of the local unit of government's annual general fund operating revenue. The Township is still well within these requirements, so PA 202 is not having an effect at this point on the Defined Benefit pension plan.

**Recommended action**

In determining a course of action, the logical first step was to evaluate the scope of the OPEB and Defined Benefit issues and begin considering how they can be rectified. As with any financial challenge there are three overall encompassing courses of action - cut expenses, increase revenue, or a combination of both. With any action, the level of service must be taken into consideration.

The next recommended step in this process is to ask the Board of Trustees to work individually with specific departments to thoroughly review operations and possibly identify changes that could impact the issues. This should be done in a timely manner to be sure that we are able to develop a corrective action plan within the state's requirements. If it is determined that cuts and revenue enhancements will not be sufficient to make up the shortfall, further courses of action will have to be considered and presented to the state in a timely manner.

## Timetable

- Review of departments with assigned Trustee – September, 2018.
- Review of Township determinations and proposed action by Plante & Moran – ongoing.
- Submit OPEB Corrective Action Plan to state – November 13, 2018.
- Further actions may follow.

## Conclusion

Bloomfield Township is a financially strong community that provides top quality services to the residents. It takes pride in offering a high level of service while operating in a fiscally responsible manner. Individual departments are well-funded; however, they are not excessively funded. There is little, if any, waste, which limits the options to reduce costs without severely affecting the level of service provided to residents. The Township has already taken many significant steps over the past 20 years to address some of these issues. Those steps include multiple years of wage freezes, closing the Defined Benefit pension plan to new hires in 2005, moving from a PPO health care plan to a high deductible HRA health care plan in 2010, and since 2011, offering a Retiree Health Savings plan to new hires in lieu of an employer-provided retiree health care plan. In its efforts to resolve the retiree health care costs, the Township will do everything it can to comply with the law in a manner that will cause the least impact for Township residents, while maintaining a fiscally responsible path into the future. The current Township Administration and Board will move forward to correct an issue that has been around for many years. It will be the efforts of the elected officials, staff, retirees, and the residents to make the proper adjustments to continue serving the community at the level that is expected.

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