City of Culver City, California

Agenda Item Report

Meeting Date: 03/12/2012	Item Number: C-4
CITY COUNCIL AGENDA ITEM: Adoption of a Resolution Establishing a Post-Employment Welfare Benefits Program Trust	
Contact Person/Dept.: Jeff Muir/Finance Department	Phone Number: (310) 253- 5865
Fiscal Impact: Yes [x] No []	General Fund: Yes [x] No []
Public Hearing: [] Action Item: []	Attachments: [X]
Commission Action Required: Yes [] No [X]	Date: ________________
Public Notification: (Email) Meetings and Agendas – City Council (03/08/12)	
Department Approval: Jeff Muir (03/07/12)	City Attorney Approval: Carol Schwab (by H. Baker) (03/07/12)
Chief Financial Officer Approval: Jeff Muir (03/07/12)	City Manager Approval: John M. Nachbar (03/07/12)

RECOMMENDATION:

Staff recommends the City Council take the following actions relative to the execution of a Governmental Accounting Standards Board (GASB) Statement 43 (GASB 43) qualifying IRS Section 115 trust (Trust) for the purposes of funding GASB Statement 45 (GASB 45) retiree healthcare and other post-employment (OPEB) liabilities:

> Adopt a resolution approving a Post-Employment Welfare Benefits Program Trust Agreement between the City, PFM Asset Management LLC, as Trust Administrator, and Union Bank, N.A., as Trustee and Custodian, and authorizing the City Manager, City Attorney, and Chief Financial Officer to execute all documents and take all necessary actions to implement the Trust.

BACKGROUND:

GASB 43 and GASB 45[i] required government entities to begin treating Other Post Employment Benefits (OPEB) in a similar fashion to pensions. This includes a requirement for independent actuarial calculations to determine the total liability based on the benefit provided, disclosure of this liability in the financial statements, calculation of the Annual Required Contribution (ARC) to fund the total liability over a thirty year period, and recording any unfunded portion of the annual ARC as a liability on the balance sheet. The most common types of OPEB benefits include health insurance and dental, vision, prescription, or other healthcare benefits provided to eligible retirees and, in some cases, their beneficiaries.

Culver City currently provides health care insurance for retirees and their eligible dependents at varying levels based on the hire date and date of retirement. Recent negotiations eliminated all but the statutory minimum City contribution towards retiree medical costs for new hires. There were also reductions in the benefit for current employees. A grandfathering provision was included allowing many current employees to retain their prior level of benefit. Additionally, the benefit level for existing retirees cannot be modified. According to the last actuarial report completed, the City's OPEB liability as of July 1, 2009 is $213,205,000, and the Annual Required Contribution is $11,754,000. The City is seeking an updated actuarial study based on the modifications that were made through negotiations, but the City will still have a significant OPEB liability. The City currently does not pre-fund any of the costs, and therefore the discount rate used by the actuary in calculating the liability is very low. This results in an already large liability being even larger.

Although there is no legal requirement at this time to fund the reported OPEB liability, it is expected to become a requirement at some point in the future. However, similar to pension liabilities, the City should be funding the future costs of the benefit for active employees during their years of service, so that these funds can accumulate with the benefit of compounding investment returns over time to help fund the benefit. As a matter of prudent financial management, the City has already identified a few funding sources and begun setting aside funds to offset this liability. Currently, there is a total of approximately $1.4 million set aside for OPEB.

Although the City has begun setting funding aside, it does not offset the City's OPEB liability unless the funds are deposited in an irrevocable trust, which dedicates the funds to OPEB related expenditures and protect against the funding being used for other purposes in the future. Again, this is similar to the pension benefit, where funds are deposited with CalPERS.

Establishing an OPEB trust to fund these costs will yield three significant benefits for the City as well as its employees and retirees:

1. <u>Protection of retiree healthcare benefits.</u> A trust would ensure that the funding set aside and contributed to this account would be irrevocable and barred from being used for any other purpose.

2. <u>Improve investment returns and bolster benefits plan sustainability.</u> Investing through a trust as opposed to the vehicles allowed for the City's standard investments will generally yield a better return since those funds can be invested in higher-yield securities. Currently, the City's investments are yielding about 1% or less and initial estimates for returns on a trust are approximately 6 to 7 percent. This significantly higher growth rate would reduce the initial liability.

3. <u>Beneficial accounting and actuarial treatment in the City's financial statements.</u> A trust would, even without fully funding it, significantly reduce the City's liability/expenses listed on its financial statements. This could positively affect future bond ratings.

Trust establishment is a separate issue from benefit levels. Establishing a trust will not affect the retiree benefits plan currently in place; it will only change the mechanism through which those benefits are dispersed. Any adjustments in benefits, for current and future retirees, would have to be determined separately through the meet-and-confer process and do not affect the establishment of the trust.

In early 2011, the City Council approved an agreement with PFM Asset Management for the creation of an irrevocable trust for retiree medical benefits. Staff has worked with PFM, as well as legal counsel, to develop the trust document being recommended for approval.

DISCUSSION:

The Trust Agreement will be between the City as "Employer", PFM Asset Management, LLC as the "Trust Administrator / Investment Advisor" and Union Bank N.A., as "Trustee/Custodian". As the Employer, the City may delegate any of its powers and responsibilities under the Trust Agreement relating to the investment and administration of Trust assets (i.e., the "Trust Administrator"). The responsibilities of the Trust Administrator / Investment Advisor and Trustee / Custodian are summarized as follows:

- PFM Asset Management, LLC (PFM) will serve as Trust Administrator and Investment Advisor to the Trust. PFM's responsibilities include managing the assets in accordance with the Investment Policy Statement, coordinating investment and funding planning activities with City staff, recommending policy and asset allocation changes to the Trust Review Committee, reporting investment performance regularly, and providing a variety of other OPEB and market related educational services. The decision to hire PFM to serve in this capacity was made by the City Council in January 2011.

- Union Bank, N.A., (Union Bank) will serve as the Trustee and Custodian. Union Bank will be responsible for asset safekeeping, contribution and distribution processing, investment transaction processing, monthly reporting of asset holdings and transactions, and providing reporting support for the annual audit. The decision to use Union Bank in this capacity was due to their competitive proposed fee structure, and was also approved by City Council in January 2011.

Day-to-day administration of the Trust pursuant to the Investment Policy Statement and the Trust Agreement will be the responsibility of PFM and Union Bank. An OPEB Trust Investment Review Committee comprised of the City Manager, the Chief Financial Officer, and the Human Resources Director will be created to periodically review the trust investments. The Committee shall meet at least annually to compare the Trust's performance against benchmarks, and review the rate of return, and asset allocation with the parameters prescribed by the Investment Policy Statement.

FISCAL ANALYSIS:

Establishment of an OPEB Trust will allow the City to invest funds to pay for retiree health costs in a manner not afforded under the City's investment restrictions. This is expected to lead to higher long-term returns than the City can receive without a trust. This, in turn, will lead to lower costs to the City to meet its obligations to fund retiree health premium costs. Upon full execution of the Trust, an initial deposit of $1.4 million comprising funds that have been set aside for this purpose shall be made.

MOTION:

That the City Council:

1. Adopt a resolution approving the Post-Employment Welfare Benefits Program Trust Agreement between the City, PFM Asset Management LLC, as Trust Administrator, and Union Bank, N.A., as Trustee and Custodian, and authorizing the City Manager, City Attorney, and Chief Financial Officer to execute all documents and take all necessary actions to implement the Trust; and,

2. Authorize the City Attorney to review/prepare the necessary documents; and,

3. Authorize the City Manager to execute such documents on behalf of the City; and,

[i] The official title of GASB 45 is *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions* and was issued in June 2004.