



# OPEB Funding

## The Pros & Cons - A Case Study

Parker Elmore, ASA, MAAA, EA, FCA  
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With the issuance of GASB 45 in 2004 and the recent issuance of GASB 75 in 2015 for governmental Other Postemployment Benefits (“OPEB”) Plans, many municipal entities are considering pre-funding their OPEB liabilities and wondering if it makes sense. To help you decide, we thought it might be helpful to share a case study of a client who faced a similar dilemma

### What Was The Situation?

The Town of Middleborough, Massachusetts (“Middleborough”) is a mature town settled in 1660, incorporated in 1669 and home to nearly 25,000 people. While the town has a manufacturing base along with their residential population, their ability to raise revenue is constrained by Massachusetts Proposition 2 ½ which caps their locally raised revenue at 2.5% of the fully & fair cash value (the “Levy Limit”) of all taxable real & personal property in the Town. As with many municipalities across the United States, Middleborough offers medical & life insurance benefits to their long time employees upon their retirement for the rest of their lives with the retirees paying 25% to 40% of the costs of such coverage. As of July 1, 2012, Middleborough had an Actuarial Accrued Liability (“AAL”) under GASB 45 of \$79.5 million, an Annual Required Contribution (“ARC”) of \$8.8 million and annual net pay-as-you-go (“pay-go”) costs for retirees of \$2.9 million plus a \$900k per year OPEB funding charge. Additionally, Middleborough is part of a county-wide retirement system which has a mandated funding schedule with required contributions of \$4.9 million for 2014 increasing to \$11.1 million by 2034.

As they looked to the future, they saw the AAL for their OPEB Plan would increase to \$682.7 million by 2054 with pay-go costs increasing to \$19.8 million over the same period. Given the Levy Limit and a stable tax base, the situation needed to be addressed to ensure that retirees would receive their promised benefits in the future without requiring major cuts to town services.

### OPEB, Pensions, Debt & Bond Ratings?

The various ratings agencies have begun looking more closely at the long-term debts of municipalities when doing their analysis. Key among these debts are OPEB and Pension plans. While it has been argued that OPEB plans are not a real debt as they can be changed and renegotiated, the ratings agencies treat these as an obligation of the municipal entity that will need to be satisfied. As such, higher debt in relation to your ability to service such debt will lead to lower ratings assuming all else is equal. Therefore, the key issue is how do you address this obligation (both OPEB and Pension) and begin to get it under control.

### So, What Did We Do?

As Middleborough looked at exploding OPEB costs into the future, growing pay-go costs for their OPEB Plan, significant current & ongoing pension contributions for the next 20 years and constraints on their ability to raise local revenue due to Proposition 2 ½, it may have seemed hopeless. So, working with Judy MacDonald (Treasurer/Collector at Middleborough), we took a holistic look at the entire retirement obligation (pension & OPEB) instead of viewing the OPEB and Pension plans as individual entities. Middleborough faced a mandate via Massachusetts General Law (“MGL”) to fund their pension obligation but there is no such requirement to fund their OPEB plan. Therefore, if we lengthen our view and treat them as one overall liability, we can effectively maintain “pay-as-you-go” funding for the OPEB plan with modest installment payments for the next 20 years and then “rollover” a portion of the pension funding amount to the OPEB plan in 2035 & beyond. While taxpayers may be looking forward to relief in 2035, simply taking 50% of the pension funding amount (releasing the rest to the general budget) will enable them to achieve full funding of the pension plan by 2034 and a 26% funded level in the OPEB plan by 2054 – thereby providing additional benefit security to their retirees and protecting the town and their taxpayers from future uncertainties.

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### Additional Incentives To Pre-Fund?

With GASB 45 and even more so with GASB 75, the discount rate used to determine plan liabilities is based on your funding policy (how much you'll set aside each year) as well as your investment policy (how will these funds be invested). In general, the more you fund each year, the higher discount rate your actuary can use for your valuation. As you're likely aware, increases in the discount rate will decrease disclosed plan liabilities on your financial statement – it doesn't change the actual cost of the plan, but it may help for an improved bond rating and therefore lead to lower borrowing costs.

### Does This Work For Everyone?

Each situation is different and we wouldn't presume that this approach makes sense for every organization. Rather, we do encourage you to look at the totality of your long-term obligations and look to solve them. We have clients who have dedicated revenue streams (e.g., meals tax, hotel tax, etc.) to OPEB funding, others with sufficient general revenue to fund and others for whom funding isn't currently financially viable.

### What's the Impact?

The chart below shows how we are able to reduce the current OPEB funding schedule by redeploying Pension funding after 2034 to create current budgetary relief while creating a path to full funding of the obligation for both programs. This approach still allows the Pension plan to be fully funded in 2034, but increases the OPEB funding in 2054 from 15% to 26%.

### If I Have Questions, Who Can I Contact?

If you have any questions about OPEB funding and what it may mean for your OPEB Plan and the impact on your OPEB accounting, please let us know.

Parker Elmore, ASA, EA, MAAA, FCA is a consulting actuary in both the Las Vegas & Connecticut offices of Odyssey Advisors. Contact him at [pelmore@odysseyadvisors.com](mailto:pelmore@odysseyadvisors.com).

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## Have Questions About The New GASB OPEB Statement?

Visit [GASB75.com](http://GASB75.com) for the latest information on the new GASB OPEB statements, as well as [OdysseyAdvisors.com](http://OdysseyAdvisors.com) for all of your retirement needs.

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### Total Medical, Dental & Life Insurance - Funding Scenarios - 4.0% Long Term Rate Of Return On Plan Assets

Fiscal Year	Total Actuarial Accrued Liability as of July 1	Original Funding Schedule				Deferred Pension Funding			
		Annual Funding/ (Payments)	Plan Assets as of July 1	Unfunded Accrued Actuarial Liability ("UAAL")	Funded Percentage	Annual Funding/ (Payments)	Plan Assets as of July 1	Unfunded Accrued Actuarial Liability ("UAAL")	Funded Percentage
2015	95,169,125	900,000	4,664,002	90,505,123	4.90%	900,000	4,664,002	90,505,123	4.90%
2016	100,017,051	900,000	5,768,386	94,248,665	5.77%	200,000	5,579,680	94,437,371	5.58%
2017	105,211,858	900,000	6,916,945	98,294,913	6.57%	200,000	6,006,828	99,205,030	5.71%
2018	110,721,665	900,000	8,111,446	102,610,219	7.33%	200,000	6,451,062	104,270,603	5.83%
2019	116,575,091	900,000	9,353,727	107,221,364	8.02%	200,000	6,913,065	109,662,026	5.93%
2020	122,771,621	900,000	10,645,700	112,125,921	8.67%	200,000	7,393,548	115,378,073	6.02%
2021	129,298,183	900,000	11,989,352	117,308,831	9.27%	200,000	7,893,251	121,404,932	6.10%
2022	136,163,219	900,000	13,386,750	122,776,469	9.83%	200,000	8,412,942	127,750,277	6.18%
2023	143,344,134	900,000	14,840,044	128,504,090	10.35%	200,000	8,953,420	134,390,714	6.25%
2024	150,849,885	900,000	16,351,469	134,498,416	10.84%	200,000	9,515,518	141,334,367	6.31%
2025	158,760,330	900,000	17,923,351	140,836,979	11.29%	200,000	10,100,100	148,660,230	6.36%
2026	167,037,708	900,000	19,558,109	147,479,599	11.71%	200,000	10,708,065	156,329,643	6.41%
2027	175,679,116	900,000	21,258,257	154,420,859	12.10%	200,000	11,340,348	164,338,768	6.46%
2028	184,686,155	900,000	23,026,411	161,659,744	12.47%	200,000	11,997,923	172,688,232	6.50%
2029	194,103,690	900,000	24,865,291	169,238,399	12.81%	200,000	12,681,801	181,421,889	6.53%
2030	203,889,920	900,000	26,777,726	177,112,194	13.13%	200,000	13,393,034	190,496,886	6.57%
2031	214,124,369	900,000	28,766,659	185,357,710	13.43%	200,000	14,132,716	199,991,653	6.60%
2032	224,864,927	900,000	30,835,149	194,029,778	13.71%	200,000	14,901,985	209,962,942	6.63%
2033	236,110,021	900,000	32,986,378	203,123,643	13.97%	200,000	15,702,025	220,407,996	6.65%
2034	247,972,123	900,000	35,223,657	212,748,466	14.20%	4,742,337	16,534,067	231,438,056	6.67%
2035	260,458,416	900,000	37,550,427	222,907,989	14.42%	4,742,337	22,031,683	238,426,733	8.46%
2036	273,666,020	900,000	39,970,268	233,695,752	14.61%	4,742,337	27,749,204	245,916,816	10.14%
2037	287,560,730	900,000	42,486,902	245,073,828	14.77%	4,742,337	33,695,426	253,865,304	11.72%
2038	302,189,288	900,000	45,104,202	257,085,086	14.93%	4,742,337	39,879,497	262,309,791	13.20%
2039	317,633,311	900,000	47,826,194	269,807,117	15.06%	4,742,337	46,310,931	271,322,380	14.58%
2040	334,117,442	900,000	50,657,065	283,460,377	15.16%	4,742,337	52,999,622	281,117,820	15.86%
2041	351,390,281	900,000	53,601,171	297,789,110	15.25%	4,742,337	59,955,861	291,434,420	17.06%
2042	369,525,426	900,000	56,663,041	312,862,385	15.33%	4,742,337	67,190,349	302,335,077	18.18%
2043	388,660,618	900,000	59,847,386	328,813,232	15.40%	4,742,337	74,714,217	313,946,401	19.22%
2044	409,044,222	900,000	63,159,105	345,885,117	15.44%	4,742,337	82,539,039	326,505,183	20.18%
2045	430,314,360	900,000	66,603,293	363,711,067	15.48%	4,742,337	90,676,854	339,637,506	21.07%
2046	452,690,670	900,000	70,185,248	382,505,422	15.50%	4,742,337	99,140,182	353,550,488	21.90%
2047	476,190,108	900,000	73,910,481	402,279,627	15.52%	4,742,337	107,942,043	368,248,065	22.67%
2048	501,110,870	900,000	77,784,724	423,326,146	15.52%	4,742,337	117,095,978	384,014,892	23.37%
2049	527,179,956	900,000	81,813,936	445,366,020	15.52%	4,742,337	126,616,071	400,563,885	24.02%
2050	554,897,026	900,000	86,004,317	468,892,709	15.50%	4,742,337	136,516,968	418,380,058	24.60%
2051	584,149,134	900,000	90,362,313	493,786,821	15.47%	4,742,337	146,813,900	437,335,234	25.13%
2052	615,056,307	900,000	94,894,629	520,161,678	15.43%	4,742,337	157,522,710	457,533,597	25.61%
2053	647,983,062	900,000	99,608,238	548,374,824	15.37%	4,742,337	168,659,872	479,323,190	26.03%
2054	682,669,338	900,000	104,510,391	578,158,947	15.31%	4,742,337	180,242,521	502,426,817	26.40%

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