

## **MEMORANDUM**

TO: Roger L. Stancil, Town Manager

FROM: Kenneth C. Pennoyer, Director of Business Management

SUBJECT: Authorization to Participate in the State Treasurer's Other Post-Employment (OPEB) Fund

DATE: June 22, 2009

### **PURPOSE**

The purpose of this memorandum is to request adoption of the attached resolution authorizing the Town's participation in the State Treasurer's OPEB Fund.

### **BACKGROUND AND DISCUSSION**

New accounting rules for Other Post Employment Benefits (OPEB), effective for the fiscal year beginning July 1, 2008, required the Town to acknowledge health care and life insurance benefits, that will be provided to current and future retirees, in a manner similar to a pension obligation. This change creates impetus for pre-funding the liability to reduce the impact of the rise in annual cost of the benefits and to make changes to the benefits structure to reduce the growth of the liability.

These new rules, also known as GASB 45, have significantly changed the Town's financial statements as we account for and report the liability for the future cost of providing these benefits. Based on the most recent actuarial study the Town's current liability, discounted at 4%, is \$45 million. In order to fully fund this liability on an actuarially sound basis the Town would need to make an annual required contribution (ARC) of \$5.6 million.

In order to address the growing OPEB liability and the resulting potential long-term impact on the Town's credit worthiness and financial sustainability we are recommending the following three phase strategy:

- Participate in the State Treasurer's investment trust for local government OPEB funds beginning with the FY2008-09 budgeted contribution of \$400,000.
- Replace existing benefit for new employees with a defined contribution post-employment health benefit.
- Evaluate changes to benefits and/or changes in eligibility requirements for existing employees.

This agenda item deals with the first bullet point: participation in the State Treasurer's investment trust for local government OPEB funds. Beginning with the FY2008-09 Budget the Town has set-aside \$400,000 to fund the cost of retiree health care. There is also the same amount included in the FY2009-10 budget. Although these amounts represent only a fraction of the annual contribution needed to fully fund retiree healthcare costs, they represent an important first step in addressing the long-term funding requirements.

The calculation of the Town's liability is based in part on its ability to earn interest on the balance of accumulated OPEB funds. Because the Town is limited in its investment options by state statute, the estimated rate of return is only 4%. Recognizing the need to provide better investment options to municipalities that have restricted investment options the State Treasurer's Office created the Municipal OPEB Fund. The Municipal OPEB Fund takes advantage of the Treasurer's expanded investment authority to achieve a higher long-term investment rate. By participating in this fund the Town will significantly reduce its total liability and annually required contribution needed to achieve full funding as calculated by the Town's actuary.

### **The Municipal OPEB Fund**

The terms and conditions for participation in the State Treasurer's Municipal OPEB Fund are contained in the attached Contribution Agreement and summarized below:

- Contributions can only be used to pay post-employment benefits
- The Fund will pay customary third party trustee, custodian and manager fees including 15 basis points to the State Treasurer for administration of the fund.
- The minimum initial contribution is \$100,000 and subsequent contributions must be greater than \$25,000.
- Contributions and withdrawals from the fund occur only on the first business day of each month. A short term investment fund (STIF) will be used to facilitate deposits and withdrawals on other days.
- There can be no withdrawals in the first 12 months of participation in the fund and only two withdrawals per year after the initial 12 month period.
- The fund will be invested consistent with the investment guidelines (Contribution Agreement - Attachment B).
- The target equity exposure of the fund is 70%. Participants acknowledge the investment risks involved in equity investments, including the potential for losses due to unfavorable market conditions.

### **FISCAL NOTE**

Investment of Town's OPEB funds in the State Treasurer's Municipal OPEB Fund will increase the estimated annual return from 4% to 7% due to the broader range of investment options available to the State Treasurer. The estimated rate of return is used by the Town's actuary to determine the total OPEB liability and annually required

contribution needed to achieve full funding. Based on preliminary estimates this would reduce our liability by more than 30%.

In addition to customary third party fees, including custodian, trustee and management fees, the State Treasury will take an administrative fee of 15 basis points (0.15%). The Town has set aside \$400,000 in both the FY2008-09 and FY2009-10 budgets to partially fund the OPEB liability. We anticipate that future annual contributions to the fund will increase to eventually equal the annually required contribution to achieve full funding in 30 years.

### **RECOMMENDATION**

That the Council adopt the attached resolution authorizing participation in the State Treasurer's Local Government Other Post-Employment Benefits Fund.

### **ATTACHMENTS**

1. Contribution Agreement

**A RESOLUTION AUTHORIZING PARTICIPATION IN THE STATE TREASURER'S LOCAL GOVERNMENT OTHER POST-EMPLOYMENT BENEFITS FUND ("OPEB") FUND (2009-06-22/ )**

WHEREAS, the Local Government Other Post-Employment Benefits Fund (the "OPEB Fund") established pursuant to North Carolina General Statutes ("NCGS") Section 147-69.4 consists of contributions made by local governments, public authorities and other entities authorized to make contributions to the OPEB Fund ("Participants"), which contributions are irrevocable; and

WHEREAS, the assets of the OPEB Fund are not subject to the claims of creditors of any Participants and may only be withdrawn by a Participant to provide other postemployment benefits to individuals, who are former employees, or beneficiaries of former employees of the Participant, and who are entitled to other post-employment benefits payable by the Participant within the meaning of NCGS Section 147-69.4; and

WHEREAS, the Council of the Town of Chapel Hill has determined that it is advisable and in the best interests of the Town of Chapel Hill to make contributions to the OPEB Fund, as provided in the Contribution Agreement between the Town of Chapel Hill and the Treasurer.

NOW, THEREFORE, BE IT RESOLVED, that the Town of Chapel Hill hereby acknowledges and approves an initial contribution of \$400,000 to the OPEB Fund (the "Contribution") pursuant to the terms and conditions of the Contribution Agreement between the Town of Chapel Hill and the Treasurer in the form presented to the Council;

FURTHER RESOLVED, that the Town Manager or his designee is hereby authorized and directed to execute and deliver the Contribution Agreement, to take any other actions deemed necessary or appropriate to consummate the transactions provided for therein, and to cause the Contribution to be made;

FURTHER RESOLVED, that the Town Manager or his designee acting on behalf of the Town of Chapel Hill is hereby authorized to take all such other actions as they may deem necessary or appropriate to give effect to the foregoing resolutions.

This the 22<sup>nd</sup> day of June, 2009.