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Other Postemployment Benefits (OPEB) Actuarial Funding Policy Statement

CITY OF ROCHESTER HILLS, MICHIGAN

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LAUTERBACH & AMEN, LLP

TABLE OF CONTENTS

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Purpose of the Actuarial Funding Policy Statement

General Purpose

This Actuarial Funding Policy Statement sets forth the procedures that the Retiree Health Care Trust Board of Trustees for the City of Rochester Hills, Michigan have adopted to make funding contributions to the Other Postemployment Benefits Trust. The policy identifies goals and objectives of the City. The policy sets out the decision-making process for handling various aspects of OPEB funding, and defines the ongoing items to be reviewed in assessing the ongoing effectiveness of this policy.

Goals and Objectives

The key goals and objectives considered in the preparation of the investment policy are noted below:

→ Make sure that benefits are secure for fund participants now and in the long-term.

→ Keep the recommended costs of the plan stable across generations of taxpayers.

→ Develop recommendations that are more cost-effective in the long-term.

→ Provide year-to-year contribution stability/budgeting for the Municipality.

→ Address any transition items needed at the policy implementation.

Operation of the Policy

It is the intention of the City to review the policy on an annual basis. The intention is to review the effectiveness of the policy and determine if it continues to meet the goals and objectives as set forth.

The City retains the right to amend the policy, as necessary, to keep the policy in line with the goals and objectives.

The Actuarial Cost Method

General Purpose

The intent of any Actuarial Cost Method is to set aside the appropriate number of dollars during an employee's working career so that the OPEB Plan has the dollars necessary to make payments at retirement. The Actuarial Cost Method will set the pattern by which contributions are made to the Funds during the working career of the employee and provide two key measures for reporting:

- → Normal Cost – The amount of money to contribute for each active employee for the upcoming year of service.
- → Accrued Liability – The amount of money that is expected to be in the OPEB Plan already, based on all past service already worked by members of the Plan.

Selection

The Entry Age Normal (EAN) Cost Method (Level Percent of Pay) has been chosen to measure the Normal Cost and Accrued Liability for the Fund.

The EAN Method is a cost-based actuarial method which focuses on budgeting annual costs during the working career of an employee. The Normal Cost level is set with the expectation that it will increase annually at the same rate as expected payroll increases during an employee's working career.

UNFUNDED ACCRUED LIABILITY

General Purpose

The Actuarial Cost Method will provide a method for setting the annual contribution pattern for current year services, as well as setting the expected level of assets needed to be on budget for past services rendered by employees. When the OPEB Plan's actuarial assets do not match the expected assets under the budget, an unfunded/overfunded liability exists.

Unfunded Liability

The Unfunded Actuarial Accrued Liability may be amortized over a period either in level dollar amounts or as a level percentage of projected payroll.

Unfunded Liability
In any year where the Total OPEB Liability exceeds the Actuarial Value of Assets, the following sources of gains and losses will be separately identified:

- Actuarial Experience Gains/Losses
- Assumptions Changes
- Plan Changes

Each source of gain/loss will be amortized by level dollar contributions to a 100% funding target over separate, closed 15-year periods.

Overfunded Liability
In any year where the Total OPEB Liability is less than the Actuarial Value of Assets, the following will occur:

- The City will fresh start any outstanding bases from prior years. Bases established in prior years will be removed

- The total amount of overfunding (excess of the Actuarial Value of Assets over the Total OPEB Liability) will be amortized as a credit towards the contribution determination by level dollar contributions to a 100% funding target over 25 years as of the date the surplus was established

ACTUARIAL VALUE OF ASSETS

General Purpose

The Actuarial Value of Assets is the figure used annually to determine the level of underfunding in the OPEB Plan. The Actuarial Value of Assets does not necessarily equal the fair Market Value of Assets. While the Actuarial Value of Assets does not represent dollars that are available on that day to make benefit payments, use of an Actuarial Value of Assets recognizes that assets will not all be distributed at a single point in time.

The objective of using an Actuarial Value of Assets that differs from the Market Value of Assets is to redistribute contributions over the life of the OPEB Plan in a manner that is less volatile. The overall level of contributions over the life of the Plan is not expected to change. To achieve this, gains and losses on the Market Value of Assets are recognized in the Actuarial Value of Assets over a period of time. In order to be successful as part of long-term funding, the Actuarial Value of Assets should be equally likely to fall above or below the market value of assets.

Key parameters:

→ Years – the number of years to smooth market value gains and losses.

→ Corridor – A limitation placed on the Actuarial Value of Assets. This parameter will limit the Actuarial Value of Assets in relation to Market Value of Assets.

Selection

The Actuarial Value of Assets will be equal to the Market Value of Assets, with unexpected gains and losses on the Market Value of Assets smoothed over a 5-year period.

It is anticipated that the Actuarial Value of Assets will not stray too far from the Market Value of Assets with the 5-year smoothing parameter. The City has selected a corridor of 80% to 120% to ensure that the Actuarial Value of Plan Assets do not stray too far from the Fair Value of Assets.

OPERATIONAL PROCEDURES

Funding Recommendations

The City's Chief Financial Officer (CFO) or his/her designee will use the policies and procedures set forth in this document to recommend a contribution amount to be made by the CFO to the Retiree Healthcare Trust Board each year.

State of Michigan Public Act 202 of 2017

In December of 2017 the Protecting Local Government Retirement and Benefits Act (Public Act 202) was signed into law and immediately effective. The Department of the Treasury for the State of Michigan establishes annual uniform actuarial assumptions of retirement systems that must be used for reporting purposes. The uniform parameters include parameters for the payment towards unfunded liability. The Retiree Healthcare Trust Board will review the actuarially determined contribution based on these assumptions annually. The intention of the City is to contribute at least the Actuarially Determined Contribution (ADC) determined under PA 202. The ADC under PA 202 will serve as a minimum contribution regardless of the results determined using the parameter in the City's Policy.

Actuarial Assumptions

The City will review the actuarial assumptions used for determining the Plan's costs at least every 3-5 years. The City will use assumptions that are the best estimate of the future anticipated experience under the plan. By getting the best estimate on actuarial assumptions, short-term changes in unfunded liability are expected to be offset over a long-term period of time. Review of the assumptions every 3-5 years will help to minimize the impact of assumption changes that have deviated from actual experience over a long period of time.

If any events occur that could impact assumptions immediately (for example, a change in the Investment Policy or strategy), the City will assess the associated assumption on a more immediate basis and will not be limited by the 3-5 year cycle.

See Addendum 1 for current selections.

Monitoring the Funding Policy

The City will review, on an annual basis, a report that is intended to monitor the progress of the Funding Policy. This review will include but not be limited to:

- → A review of the progress being made on the unfunded liability that exists at implementation.
- → A review of the anticipated gains and losses that will be recognized in the upcoming actuarial value of assets under the funding policy.
- → An analysis of cash flow to monitor the continuous ability of the funds to pay benefits.
- → An analysis of the causes of any changes in unfunded liability over the preceding year.
- → An analysis of the actuarial expectations versus actual experience over the past year.

ADDENDUM 1 – CURRENT ACTUARIAL ASSUMPTIONS

Economic Assumptions

Assumption	Selection	Reason
Expected Rate of Return on Assets	5.00%	Based on the current target allocation in the OPEB Trust and discussion with the Investment Consultant.
Total Payroll Increases	2.50%	Based on the current employee population.
Insurance Claims and Healthcare Trend Rates	N/A	There is no implicit liability to the City due to the Retiree-only medical insurance. The explicit benefits are fixed, not subject to future increases.

Demographic Assumptions

Assumption	Selection	Reason
Election at Retirement	100%	Represents the anticipated percentage of employees who will continue City OPEB benefits in retirement.
Spousal Election	80%	Represents the anticipated percentage of employees continuing coverage in retirement who will elect spousal coverage.
Retiree/Spouse Mortality	MERS 2020	Based on the MERS Experience Study Report for the period January 1, 2014 through December 31, 2018.
Termination Rates	MERS 2020	Based on the MERS Experience Study Report for the period January 1, 2014 through December 31, 2018.
Disability Rates	MERS 2020	Based on the MERS Experience Study Report for the period January 1, 2014 through December 31, 2018.
Retirement Rates	MERS 2020	Based on the MERS Experience Study Report for the period January 1, 2014 through December 31, 2018.