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July 15, 2021

Lisa Okada
HR Benefits Director
San Mateo County

Re: Study of Proposed Benefit Changes for Organization of Sheriff's Sergeants (OSS) Active Members

Dear Lisa:

As requested, we have estimated costs to San Mateo County (the County) for various benefit changes to the Postemployment Benefits Other than Pension (OPEB) Plan for Organization of Sheriff's Sergeants (OSS) active members.

The results shown in this letter summarize estimated costs to the County of adopting these OPEB plan revisions. We are not advocating either for or against these changes.

The calculations in this letter are for current OSS active employees only. They do not include current retirees. Additionally, consistent with GASB 75, these are "closed group" calculations, meaning that they do not reflect the impact of future hires.

Executive Summary

Based on the July 1, 2020 census, the proposed changes would increase the Total OPEB Liability (TOL) associated with the sick leave benefits of the OSS active members compared to the current plan from about $5.6 million to $6.3 million, a cost of about $0.7 million as of July 1, 2020.

Explicit and Implicit Subsidies

The County's obligation includes both an explicit subsidy and an implicit subsidy. The County's direct payments attributable to sick leave hours constitute the explicit subsidy. Under the current plan, the County pays monthly premiums for active members upon retirement for a duration based on the sick leave hours balance at retirement.

The County contracts with Kaiser and Blue Shield Health Plans to provide health coverage to its actives and pre-Medicare (prior to age 65) retirees. These insurers charge the same premium for actives and retirees without Medicare. Therefore, the County is paying a higher rate for active employees than they otherwise would if the retirees were in a separate plan. This creates an "implicit" subsidy of retiree premiums. GASB requires including the value of this subsidy in the TOL. It is our understanding that, under the current proposal, employees will continue to access the subsidized premiums.

Therefore, there is no reduction in the value of the implicit subsidy under the proposed changes.

Summary of OSS Proposed Benefits

Convert Old Sick Leave to Retiree Health Savings at Retirement

Under the proposed buy-out, each member would receive a lump sum at retirement rather than a future stream of monthly payments in retirement. The lump sum amount would be based on the member's sick leave balance on June 30, 2021, divided by eight, multiplied by either $675.00 (Tier One) or $400.00 (Tier Two), depending on the current sick leave conversion level for the employee. The funds remain in the County's OPEB Trust until the employee retires. This lump sum would be deposited into the employee's Retiree Health Savings Account (RHSA) upon retirement if, and only if, the person meets the eligibility requirements to receive a pension benefit through SamCERA.

Existing tier two employees ($400 per 8 hours) will receive an additional credit of 288 hours of sick leave at retirement if they have 20 or more years of service with San Mateo County.

We have modeled the effects of these plan design changes on the Total OPEB Liability (TOL), and service cost (SC), under GASB 75.

Create Retiree Health Savings Account

Employees and the County will contribute $50 per month to a RHSA beginning in July 2021. In April 2023, the contribution will be increased to $75 per month. Since this is not a defined benefit plan, it would not incur OPEB costs. However, the one-year cost of this proposed benefit relative to the Service Cost of the current and proposed OPEB benefits helps to illustrate the value of the proposed $50 monthly contribution made by the County.

Total OPEB Liability

The TOL represents the value of benefits allocated to past service for the current OSS active members under the actuarial cost method. The Net OPEB Liability (NOL) is the TOL minus the assets, and that is the amount shown on the balance sheet for the County's financial reporting. It also serves as a funding target for the County's established funding policy.

The table below shows the TOL as of July 1, 2020, as though the benefit changes had taken effect as of the July 1, 2020 actuarial valuation.

In the final column, numbers in parentheses indicate that the proposed benefits are a decrease from the current plan and numbers without parentheses are an increase.

Total OPEB Liability as of July 1, 2020

	Implicit Health Premium Subsidy (A)	Current Plan Sick Leave Benefit (B)	Current Postretirement Benefits (C) = (A) + (B)	Proposed Sick Leave Conversion (D)	Proposed Postretirement Benefits (E) = (A) + (D)	Increase (Decrease) in TOL from Current Plan (F) = (E) - (C)
OSS	$3,927,627	$1,645,591	$5,573,218	$2,380,775	$6,308,402	$735,184

Service Cost

The service cost (SC) represents the value of benefits earned during the year on an on-going basis. This is the portion of the present value of projected benefit payments allocated to the current year of service by the actuarial cost method. It is a component of the expense calculation for financial reporting.

The table below shows the amounts for 2020-2021, as though the benefit changes had taken effect as of the July 1, 2020 valuation.

Annual Service Cost as of July 1, 2020

	Implicit Health Premium Subsidy	Current Plan Sick Leave Benefit	Current Postretirement Benefits	Proposed Sick Leave Conversion	Proposed Postretirement Benefits	Increase (Decrease) in SC from Current Plan
	(A)	(B)	(C) = (A) + (B)	(D)	(E) = (A) + (D)	(F) = (E) - (C)
OSS	$198,488	$73,601	$272,089	$99,583	$298,071	$25,982

While the above chart shows the increase in the service cost for 2020-2021, it is important to note that savings in service cost would emerge over time, since the new hires will have zero service cost under the proposed benefits plan scenarios. By comparison, if the current benefit program remains in place, its service cost would be fairly stable into the future, assuming that the population remains stable.

Based on 63 active OSS members, the one-year cost of a County contribution of $50 per month per active OSS member to RHSAs would be $50 x 12 x 63 = $37,800. A County contribution of $75 per month would be $56,700 ($75 x 12 x 63).The RHSA contribution would not incur OPEB costs as it is not a defined benefit plan. By comparison, the service cost of the sick leave benefit portion of the current benefit program was $73,601 as of the July 1, 2020 actuarial valuation.

Impact on GASB Expense

Another consideration is the impact of the studied plan changes on the GASB 75 Expense calculations. There would be two changes to the GASB expense. First the updated Service Cost would be included in the calculation. Second, GASB requires the change in TOL due to change in plan design be recognized immediately in the first year. If the studied plan changes were adopted, the GASB expense under the program studied compared to the current plan would increase in the first year due to the change in service cost of $25,982 and increase due to the change in TOL by $735,184, for a net impact of an increase in the GASB expense by $761,166 in the first year. After the first year, the GASB expense would be affected by the changes in the service cost.

Monthly contributions to an RHSA are not covered under GASB 75 and therefore are not included in the expense calculation.

Data, Assumptions, and Methods

Except as otherwise noted, all data, assumptions, and methodology for our baseline calculations match our July 1, 2020 actuarial valuation report dated September 22, 2020 with the following exception:

> Members Valued: The proposed changes only impact active employees. As of July 1, 2020, there were 63 OSS active members covered under the San Mateo County OPEB Plan. Please see Appendix C of our July 1, 2020 actuarial valuation report for a summary of the Membership Data.

Election of Sick Leave Lump Sum Benefit: All members (100%) are assumed to elect the lump sum upon retirement. This is an increase from the 95% assumed to elect sick leave benefits for our valuations. This is distinct from the assumption that 95% of members will elect to maintain coverage under the County health plans, which is unchanged from the valuation.

Old Sick Leave Utilization: Employees are assumed to use none of their Old Sick Leave benefits. The entirety of the Old Sick Leave hours retained is converted at the applicable rate and deposited into the employee's RHSA upon retirement.

Caveats

In preparing this letter, we relied, without audit, on information (some oral and some in writing) supplied by the County's staff and labor representatives. This information includes, but is not limited to, statutory provisions, employee data, and financial information. We found this information to be reasonably consistent and comparable with information used for other purposes. The study results depend on the integrity of this information. If any of this information is inaccurate or incomplete, our results may be different and our calculations may need to be revised.

All costs, liabilities, rates of interest, and other factors for the County have been determined on the basis of actuarial assumptions and methods which are individually reasonable (taking into account the experience of the County and reasonable expectations); and which, in combination, offer our best estimate of anticipated experience affecting the County. Further, in our opinion, the actuarial assumptions in the aggregate are reasonable and are related to the experience of the Plan and to reasonable expectations and represent our best estimate of anticipated experience under the Plan.

Milliman has developed certain models to estimate the values included in this letter. The intent of the models was to estimate retiree medical annual trends and costs by age and gender. In addition, the valuation results were developed using models employing standard actuarial techniques. We have reviewed the models, including their inputs, calculations, and outputs for consistency, reasonableness, and appropriateness to the intended purpose and in compliance with generally accepted actuarial practice and relevant actuarial standards of practice.

Given the substantial uncertainty regarding the impact of COVID-19 on plan costs, including whether the pandemic will increase or decrease costs during the term of our projections, we have chosen not to make an adjustment in the expected plan costs. It is possible that the COVID-19 pandemic could have a material impact on the projected costs.

This analysis is only an estimate of the County's liability as of a single date. It can neither predict the County's future condition nor guarantee future financial soundness. Actuarial calculations do not affect the ultimate cost of benefits, only the timing of contributions. While the study is based on array of individually reasonable assumptions, other assumption sets may also be reasonable and results based on those assumptions would be different. No one set of assumptions is uniquely correct. Determining results using alternative assumptions is outside the scope of our engagement.

Future actuarial measurements may differ significantly from the current measurements presented in this letter due to such factors as the following: plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the methodology used for these measurements and changes in plan provisions or applicable law. Due to the limited scope of our assignment, we did not perform an analysis of the potential range of future measurements. The County has the final decision regarding the appropriateness of the assumptions.

Actuarial computations presented in this letter are for purposes of determining changes to liabilities due to proposed benefit changes for active participants. The calculations in this report have been made on a basis consistent with our understanding of the Plan's current and proposed benefits. Determinations for purposes other than meeting these requirements may be significantly different from the results contained in this letter. Accordingly, additional determinations may be needed for other purposes.

Milliman's work is prepared solely for the internal business use of the County for a specific and limited purpose. To the extent that Milliman's work is not subject to disclosure under applicable public records laws, Milliman's work may not be provided to third parties without Milliman's prior written consent. Milliman does not intend to benefit or create a legal duty to any third party recipient of its work product. Milliman's consent to release its work product to any third party may be conditioned on the third party signing a Release, subject to the following exceptions:

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No third party recipient of Milliman's work product should rely upon Milliman's work product. Such recipients should engage qualified professionals for advice appropriate to their own specific needs.

The consultants who worked on this assignment are actuaries. Milliman's advice is not intended to be a substitute for qualified legal or accounting counsel.

Specifically, we have not explored any legal issues with respect to the proposed plan changes. We are not attorneys and cannot give legal advice on such issues. We suggest that you review this proposal with counsel.

The signing actuaries are independent of the plan sponsor. We are not aware of any relationship that would impair the objectivity of our work.

On the basis of the foregoing, we hereby certify that, to the best of our knowledge and belief, this letter is complete and accurate and has been prepared in accordance with generally recognized and accepted actuarial principles and practices, which are consistent with the principles prescribed by the Actuarial Standards Board and the *Code of Professional Conduct* and *Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States* published by the American Academy of Actuaries.

We are members of the American Academy of Actuaries and meet the Qualification Standards to render the actuarial opinion contained herein.

Please let us know if you would like to discuss this further.

Sincerely,

Daniel Wade, FSA, EA, MAAA
Principal and Consulting Actuary

Arthur Rains-McNally, FSA, EA, MAAA
Consulting Actuary

Jessica M. Gardner, ASA, MAAA
Actuary

Attachments

DRW/ACRM/JMG/nlo