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Board of Fire and Police Pension Commissioners
360 East Second Street, Suite 400
Los Angeles, CA 90012

**Re: FY 2007-2008 Retiree Health Plan Contribution**
**Three-Year Phase-in of City Contribution Rates**

Dear Members of the Board:

On December 7, 2006, the Board elected to phase in the impact of new actuarial assumptions on the City's retiree health plan contribution for the 2007-08 fiscal year. The recommended (i.e., pre-phase-in) contribution rates for Fiscal Year 2007-08 are contained in Segal's December 12, 2006 report entitled *Actuarial Valuation and Review of Other Postemployment Benefits (OPEB.)* This letter provides the "phased-in" contribution rates for Fiscal Year 2007-08 and an analysis of the financial reporting and future contribution rate impact of the three-year phase-in.

## Phase-in Contribution Rates for 2007-08

The following table shows the full impact, by Tier, of the newly adopted actuarial assumptions on the City's retiree health plan beginning-of-year contributions for fiscal year 2007-08. This is the portion of the increase from the current contribution rates that will be phased-in over three years. Depending on the tier, the impact is measured as a dollar amount or as a percentage of payroll, consistent with Page 10 of the actuarial report. The phased-in City contribution rates for 2007-08 (which includes only one-third of the Impact of the New Actuarial Assumptions) are provided on the attached table.

| Tier: | Impact of New Actuarial Assumptions: |
|---|---|
| Tier 1 | $219,643 |
| Tier 2 | 0.76% of Total payroll |
| Tier 3 | 2.07% of Tier 3 payroll |
| Tier 4 | 1.92% of Tier 4 payroll |
| Tier 5 | 1.70% of Tier 5 payroll |

**Impact of Three-Year Phase-in on Financial Reporting**

The retiree health plan contributions recommended in Segal's June 30, 2006 actuarial valuation report represent the Annual Required Contribution (ARC) under Governmental Accounting Standards 43 and 45 for the 2007-8 fiscal year. These are before any phase-in, and reflect the full impact of the new actuarial assumptions.

The application of a phase-in of contributing the full amount of the City's ARC will result in the City recording a liability (Net OPEB Obligation or "NOO") equal to shortfall of the actual contribution relative to the ARC. We estimate that the NOO accrued during 2007-08 (the first year of the phase-in) will be approximately $20 million. An additional NOO of approximately $10 million will be accrued in the 2008-09 fiscal year, the second year of the phase-in.

**Impact of Three-Year Phase-in on Future Contributions**

The NOO's accrued during the phase-in will be amortized over a 15-year period consistent with the period of time actuarial gains and losses are amortized under the Board's current amortization policy. In effect, these amortization payments are the "financing cost" of delaying the full impact of the new actuarial assumptions. We estimate that the NOO amortization will result in an additional contribution of about 0.23% of compensation in each year during the 15-year amortization period.

More specifically, the 2009-10 contribution requirement will be about $2 million higher than if the phase-in had not taken place. Contributions for each of the following 14 years will go from about $3 million higher to about $5 million higher than if the phase-in had not taken place (the dollar amounts increase only because they are a fixed 0.23% of an increasing payroll). In the final year of the NOO amortization (FY2024-25) the contribution requirement will be about $2 million higher than if the phase-in had not taken place.

The net impact of the initial phase-in and the subsequent additional amortization costs are reflected in the five-year projection of contributions that we sent you on January 5. If you have any other questions, please let us know.

Sincerely,

Paul Angelo, FSA, EA, MAAA

DZJ/jc

**Attachment**

**Fiscal Year 2007-08 Retiree Health Plan Contribution**
**Impact of New Assumptions**

## 2007-2008 Fiscal Year Contribution Requirements (Adjusted for Three Year Phase-in)

| | Tier 1 | Tier 2 | Tier 3 | Tier 4 | Tier 5 |
|---|---|---|---|---|---|
| Normal cost | $0 | $601,781 | $3,559,605 | $1,216,049 | $29,624,001 |
| Amortization of the unfunded actuarial accrued liability over 30 years | $1,153,308 | $29,148,729 | $1,308,046 | $953,049 | $3,358,829 |
| Total annual required contribution, beginning of year | $1,153,308 | $29,750,510 | $4,867,651 | $2,169,098 | $32,982,830 |
| Percent of compensation | N/A | 2.72% | 5.39% | 5.09% | 3.53% |
| Adjustment for timing (payable throughout the year) | $46,724 | $1,205,291 | $197,204 | $87,877 | $1,336,242 |
| Total annual required contribution | $1,200,032 | $30,955,801 | $5,064,855 | $2,256,975 | $34,319,072 |
| Payroll | N/A | $1,092,814,844 | $90,311,641 | $42,595,593 | $935,317,449 |
| Percent of compensation | N/A | 2.83% | 5.61% | 5.30% | 3.67% |