
CITY OF ANN ARBOR
RETIREE HEALTH CARE BENEFIT
PLAN & TRUST (VEBA)

SUMMARY
ANNUAL REPORT

For the Fiscal Year Ended
June 30, 2021

**CITY OF ANN ARBOR
RETIREE HEALTH CARE BENEFIT PLAN & TRUST
532 S Maple Rd.
Ann Arbor, MI 48103**

Phone (734) 794-6710 Fax: (734) 994-9205 Web Address: www.a2gov.org

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Daniel Gustafson, Pension Analyst
Maria Buffone, Accountant
Laura Hollabaugh, Management Assistant

ACTUARY

Gabriel, Roeder, Smith and Co.

AUDITORS

Yeo & Yeo CPA's

CUSTODIAL BANK

The Northern Trust Company

INVESTMENT MANAGERS

| | |
|---|----------------------------------|
| AEW Core Property Trust | Loomis Sayles |
| Arboretum | The Northern Trust Company |
| Artisan International Value | Rhumblin |
| Beach Point Capital Management | Rhumblin HEDI |
| BlackRock Global Renewable Power Fund III | Sky Harbor Capital Management |
| Carlyle | Stone Harbor Investment Partners |
| Dimensional Fund Advisors | Summit Credit Partners |
| DRA Growth and Income Funds | SVB Strategic Investors Fund |
| First Eagle | Torchlight Debt Fund VII |
| GQG | Vanguard REIT |
| Income Research and Management | WCM |
| Ironside Direct & Partnership Funds | |

INVESTMENT MANAGEMENT CONSULTANT

Meketa Investment Group

LEGAL COUNSEL

Michael J. VanOverbeke; VanOverbeke, Michaud & Timmony, P.C.

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CITY OF ANN ARBOR RETIREE HEALTH CARE BENEFITS PLAN AND TRUST

Annual Report For Year Ending June 30, 2021

The City of Ann Arbor Retiree Health Care Benefits Plan and Trust (VEBA Trust) was established to provide health and life insurance benefits or such other benefits, approved by the City or approved by collective bargaining agreements, for the welfare of the Retirees of the City who are eligible to receive a retirement benefit from the City of Ann Arbor Employees' Retirement System, and the spouses and eligible dependents of such Retirees. Health care benefits under the Plan are provided for pursuant to the City of Ann Arbor Health Care Plan, Chapter 21 of the City Code.

The Health Care Benefits Plan was established during the year ending June 30, 1999. The City is now "pre-funding" for the health and life insurance coverage provided to retirees and beneficiaries. Assets are being set aside during an active participant's career in order to provide health and life insurance coverage after retirement. This contrasts with a "pay as you go" practice of paying health and life insurance premiums as they come due.

The investment performance of the Plan was a positive 25.2% for Fiscal Year Ended June 30, 2021. The annual money weighted rate of return was 25.68%. These returns are net of fees.

The Actuarial Determined Contribution (ADC) is \$13,001,479 for Fiscal Year 2021/2022, and \$9,403,669 for Fiscal Year 2022/2023 as detailed in page 6 of this report. The projected annual required contribution rate for advance-funding of the post-retirement health and life insurance coverage for Fiscal Year 2023 is 15.95% of active participant payroll vs. 21.60% last year.

The City will not realize any short-term budgetary gain from advance-funding for post-retirement health and life insurance benefits. Long-range gains will occur, and the reserve created is a valuable side effect. Eventually, if the recommended funding contributions in subsequent years are made, the Plan will be fully actuarially funded. **In the year ending June 30, 2021, \$15,625,495 was contributed to the fund, including benefits paid from City assets. This contribution exceeded the recommended contribution requirement for the year ended 2021.**

At the September 17, 2020 Board meeting, the Board of Trustees approved a change to the assumed rate of investment return (i.e., the discount rate) from 7.0% to 6.5% over a 5-year period, with a reduction of 0.1% per year starting with the 2020 valuation analysis. The actuary will only recognize the 0.1% reduction for all future years in the valuation. The Board will annually review the reduction in the assumed rate of return over this 5- year period to determine if additional modifications or time-line considerations should be addressed. Please note that the 6.8% discount rate is used to compute liabilities/future contributions in this valuation. The fund assumed a 6.9% investment return during July 1, 2020 through June 30, 2021 and 6.8% thereafter.

Sincerely,


Jeremy Flack (Dec 21, 2021 16:40 EST)

Jeremy Flack
Chairperson, Board of Trustees


Wendy Orcutt (Dec 21, 2021 15:19 EST)

Wendy Orcutt
Executive Director

Investment Summary & Highlights

Historical Asset Class Performance (%) Annualized Returns Over Rolling Calendar Year Periods as of December 31, 2020

| Asset Class | <u>1 Year</u> | <u>3 Years</u> | <u>5 Years</u> | <u>7 Years</u> | <u>10 Years</u> |
|---|---------------|----------------|----------------|----------------|-----------------|
| Total Plan | 12.0% | 8.6% | 9.8% | 7.3% | 8.0% |
| Domestic Equity | 18.1 | 13.0 | 14.7 | 11.4 | 13.2 |
| International Developed Market Equity | 16.5 | 10.5 | 11.7 | 7.3 | 7.8 |
| International Emerging Market Equity | 20.2 | 6.9 | 13.7 | 7.2 | NA |
| Investment Grade Fixed Income | 7.3 | 5.2 | 4.3 | 4.0 | 4.0 |
| High Yield Fixed Income | 7.3 | 6.0 | 8.2 | 5.5 | 6.6 |
| Treasury Inflation Protected Securities | 8.4 | 5.0 | 4.2 | 3.0 | NA |
| Bank Loans | 2.8 | 4.1 | 4.3 | 3.8 | NA |
| Emerging Market Debt | 1.9 | 1.3 | 5.5 | 0.2 | NA |
| Natural Resources | 29.9 | 15.0 | NA | NA | NA |
| Real Estate | -0.4% | 5.7% | 6.4% | 7.8% | 8.8% |

Note: Source is Meketa Investment Group. Returns are net of fees on a rolling calendar year basis. May contain differences from audited financial statements due to timing, manner of presentation, and accounting requirements. Performance updates are available quarterly on the Retirement System's website.

Actuarial Section

MEMBERSHIP

| | <u>2021</u> | <u>2020</u> |
|--|-------------|-------------|
| Retirees and Beneficiaries currently covered | 1048 | 1070 |
| Spouses of Retirees currently covered | 552 | 558 |
| Active Participants | | |
| Traditional Plan | 284 | 318 |
| RHRA Plan | <u>423</u> | <u>407</u> |
| Sub-total Active Participants | <u>707</u> | <u>725</u> |
| Total | 2307 | 2353 |

The Retiree Health Care Benefits Plan financial objective is to meet long-term benefit promises through contributions that remain approximately level from year to year as a percent of active participant payroll.

CITY'S COMPUTED CONTRIBUTIONS TO THE BENEFITS PLAN
FOR THE FISCAL YEAR END JUNE 30, 2023

| Contributions for | General | General RHRA | Police | Police RHRA | Fire | Fire RHRA | Total |
|---|---------------------|---------------------|--------------------|--------------------|--------------------|--------------------|---------------------|
| 1. Total Normal Cost of Benefits: | \$1,233,504 | \$372,548 | \$392,549 | \$106,813 | \$377,110 | \$55,811 | \$2,538,335 |
| 2. Member Contributions | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 3. Employer Normal Cost (1.- 2.) | 1,233,504 | 372,548 | 392,549 | 106,813 | 377,110 | 55,811 | 2,538,335 |
| 4. Payment for Active Unfunded Actuarial Liabilities (UAL) | 855,34 | 0 | 326,041 | 0 | 222,804 | 0 | 1,404,579 |
| 5. Payment for Inactive UAL | 3,006,174 | 0 | 1,289,159 | 0 | 850,955 | 0 | 5,146,288 |
| 6. Interest | 176,291 | 12,889 | 69,464 | 3,695 | 50,197 | 1,197 | 314,467 |
| 7. Preliminary Actuarially Determined Contribution (ADC) (3. + 4. + 5. + 6.) | \$5,271,703 | \$385,437 | \$2,077,213 | \$110,508 | \$1,501,066 | \$57,742 | \$9,403,669 |
| 8. Projected Fiscal Year Payroll | \$13,779,634 | \$25,695,813 | \$4,001,920 | \$8,007,857 | \$4,004,973 | \$3,478,416 | \$58,968,613 |
| 9. Preliminary ADC as a Percent of Projected Payroll | 38.26% | 1.50% | 51.91% | 1.38% | 37.48% | 1.66% | 15.95% |
| 10. Prior Fiscal Year Budgeted Contribution[^] | | | | | | | \$13,001,479 |
| 11. Prior Fiscal Year Budgeted Contribution with 2% Increase¹ | | | | | | | \$13,261,509 |
| 12. Estimated City Contribution (Greater of 7. & 11.) | | | | | | | \$13,261,509 |

[^] Provided by the City.

¹Funding policy temporarily suspended in FYE20 and FYE21 due to COVID-19.

Unfunded actuarial accrued liabilities were amortized as a level dollar amount over a period of 20 years for fiscal year ending June 30, 2023. The amortization period decreases by two each year thereafter until a 15-year rolling amortization is reached. Once the Plan reaches 100% funded status, the amortization period will be set at 1 year.

Assumptions and Methods Used to Determine Contributions for the FYE June 30, 2021

| | |
|-----------------------------|--|
| Valuation Date: | 6/30/2019 |
| Methods and assumptions: | |
| Actuarial cost method | Entry Age Normal; level percent of pay |
| Amortization method | Level percent of pay |
| Asset valuation method | Actuarial value |
| Discount Rate | 7% |
| Assumed Rate of Return | 7% |
| Amortization Period | 24 years* |
| Inflation | 3.5% |
| Salary Increases | 3.50% per annum plus merit component that varies by age |
| Healthcare cost trend rates | Medical Pre-65: 8.25% decreasing 0.25% per year to an ultimate of 4.50%; Medical Post-65 6.25% decreasing to an ultimate of 3.50% in 2031. |

*At the September 21, 2017 meeting, the Board adopted a closed level dollar amortization starting at 30 years, decreasing 2 years annually until the amortization period reaches 15 years.

SCHEDULE OF EMPLOYER CONTRIBUTIONS

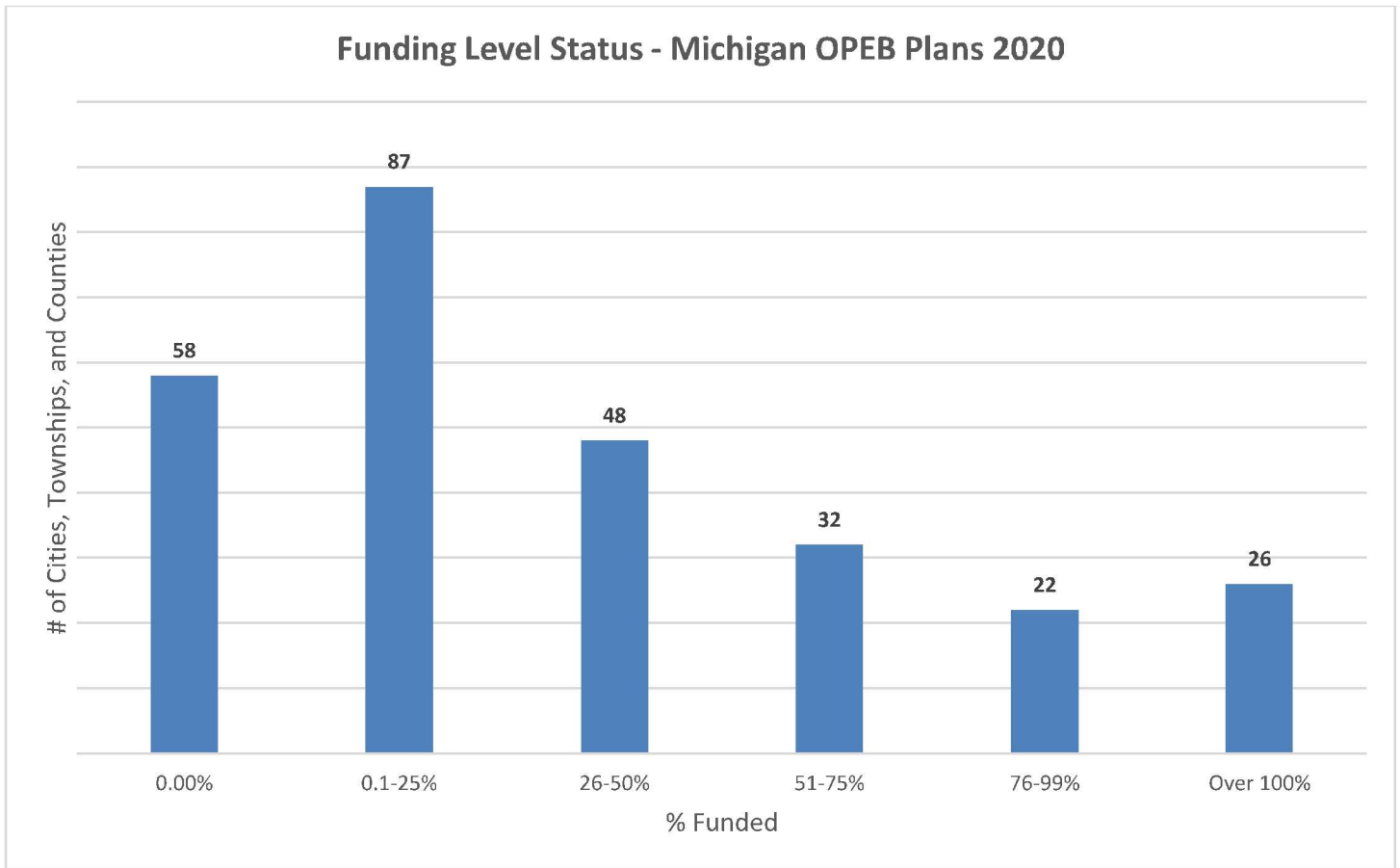
| Year Ended June 30, | Annual Required Contribution | Current Premiums Paid by the City | Pre Funding Contributions to Trust | Percentage Contributed |
|------------------------|---------------------------------|--------------------------------------|--|------------------------|
| 2021 | \$11,663,630 | \$14,516,628 | \$1,108,867 | 134% |
| *2020 | 12,129,387 | 11,468,614 | 772,922 | 101.0 |
| 2019 | 9,234,000 | 13,171,225 | 2,816,543 | 173.1 |
| 2018 | 10,641,000 | 14,272,653 | 3,451,332 | 166.6 |
| 2017 | 11,168,000 | 13,360,000 | 3,460,057 | 150.6 |
| 2016 | 11,179,000 | 12,095,622 | 3,075,389 | 135.7 |
| 2015 | 11,974,000 | 10,758,954 | 4,220,778 | 125.1 |
| 2014 | 12,203,000 | 10,650,463 | 4,537,637 | 124.6 |
| 2013 | 12,379,000 | 9,207,043 | 5,790,086 | 121.1 |
| 2012 | 14,859,285 | 8,889,686 | 2,163,202 | 74.4 |
| 2011 | 14,395,148 | 9,181,437 | 4,839,659 | 97.4 |

*NOTE: Due to the COVID-19 crisis, the City temporarily suspended the funding policy for FYE20 & FYE21 and only contributed the ADC (Actuarially Determined Contribution).

FUNDING LEVEL STATUS

The City of Ann Arbor is “pre-funding” for the health insurance coverage provided to retirees and beneficiaries. In addition to contributing the Actuarial Determined Contribution (ADC), the City has historically contributed well above that amount. Per the June 30, 2021 GASB 74/75 Report, the Retiree Health Care Plan is funded at 77.89%, an increase from the prior year’s 66.8% funded level. As referenced earlier on page 4, the Board has adopted a lower assumed rate of return which will also result in higher contributions to the Plan.

As you can see in the chart below, a great number of Systems are using a “pay as you go” approach. Of the 273 plans included in the sample, 21% are making no advance payments to their Plan, 70% of the plans are funded at 50% or less, with only 17% funded at 76% or higher.



* This graph includes 273 Cities, Townships and Counties with a minimum of \$1,000,000 in OPEB liabilities. The source of the data is the State of Michigan Local Retirement System Status Report.

ACCOUNTING INFORMATION FOR GASB 74/75

The components of the New OPEB Liability of the City at June 30, 2021 are as follows:

| | |
|---|---------------|
| Total OPEB Liability | \$313,723,384 |
| Plan Fiduciary net position | 244,344,934 |
| New OPEB Liability | 69,378,450 |
| Plan Fiduciary net position as a percentage of the total OPEB Liability | 77.89% |

Sensitivity of the Net OPEB Liability to Changes in the Discount Rate

| Decrease to 5.9% | Discount Rate – 6.9% | Increase to 7.9% |
|------------------|----------------------|------------------|
| \$106,592,154 | \$69,378,450 | \$38,460,719 |

Sensitivity of the Net OPEB Liability to Changes in Healthcare Cost Trend Rate

| 1% Decrease | Current | 1% Increase |
|--------------|--------------|---------------|
| \$35,826,110 | \$69,378,450 | \$109,641,582 |

SCHEDULE OF REQUIRED SUPPLEMENTARY INFORMATION SCHEDULE OF THE NET OPEB LIABILITY MULTIYEAR (\$ in thousands)

| FY Ending, June 30, | Total OPEB Liability | Plan Net Position | Net OPEB Liability | Plan Net Position as a % of Total OPEB Liability | Covered Payroll ⁽¹⁾ | Net OPEB Liability as a % of Covered Payroll |
|------------------------|-------------------------|----------------------|-----------------------|---|-----------------------------------|---|
| 2017 | \$254,029,000 | \$157,339,000 | \$96,690,000 | 61.94% | \$53,583,000 | 180.45% |
| 2018 | 261,367,000 | 171,807,000 | 89,560,000 | 65.73 | 55,458,000 | 161.49 |
| 2019 ⁽²⁾ | 293,406,401 | 186,331,562 | 107,074,839 | 63.51 | 57,077,636 | 187.60 |
| 2020 | 289,866,913 | 193,649,479 | 96,217,434 | 66.81 | 57,970,915 | 165.98 |
| 2021 | 313,723,384 | 244,344,934 | 69,378,450 | 77.89 | 60,232,543 | 115.18 |

⁽¹⁾ Covered payroll was provided by the City of Ann Arbor and may or may not meet the GASB Statement Nos. 74 and 75 definition of Covered Payroll.

⁽²⁾ Results for 2018 and prior years were calculated by the City's prior actuaries.

FINANCIAL SECTION

The purpose of the Financial Section is to provide the reader with the present financial position and condition of the Plan & Trust.

This section contains:

**Independent Auditors' Report &
Audited Financial Statements**

City of Ann Arbor
Retiree Health Care Benefits Plan and Trust
Statement of Fiduciary Net Position
June 30, 2021

Assets

| | |
|---|------------------------|
| Investments, at fair value | |
| Equities | \$ 152,180,543 |
| Fixed income | 66,785,073 |
| Other | <u>24,646,220</u> |
| Total investments | 243,611,836 |
| Equity in City of Ann Arbor pooled cash and investments | 690,086 |
| Accrued interest and dividends | <u>217,416</u> |
| Total assets | <u>244,519,338</u> |

Liabilities

| | |
|--|---------------------------|
| Accrued liabilities | <u>174,404</u> |
| Net position restricted for benefits | <u>\$ 244,344,934</u> |

City of Ann Arbor
Retiree Health Care Benefits Plan and Trust
Statement of Changes in Fiduciary Net Position
For the Year Ended June 30, 2021

Additions

| | |
|--|-----------------------|
| Investment income | |
| From investing activities | |
| Net appreciation in fair value of investments | \$ 46,799,880 |
| Interest and dividends | <u>3,148,134</u> |
| Total investment income | 49,948,014 |
| Investment management fees | <u>(219,322)</u> |
| Net investment income from investing activities | <u>49,728,692</u> |
| | |
| From securities lending activities | |
| Gross earnings | 353 |
| Borrower rebates paid | (723) |
| Securities lending fees | <u>320</u> |
| Net investment income from securities lending activities | <u>(50)</u> |
| | |
| Total net investment income | 49,728,642 |
| | |
| Employer contributions | <u>15,625,495</u> |
| | |
| Total additions | <u>65,354,137</u> |
| | |
| Deductions | |
| Participant benefits | 14,516,628 |
| Administrative expenses | <u>142,054</u> |
| | |
| Total deductions | <u>14,658,682</u> |
| | |
| Change in net position | 50,695,455 |
| | |
| Net position - beginning of year | <u>193,649,479</u> |
| | |
| Net position - end of year | <u>\$ 244,344,934</u> |