Odyssey ADVISORS

East Coast
11 Hayward Ave, Building 4
Colchester, CT 06415
(860) 537-9080

West Coast
1350 E. Flamingo Road, Suite 254
Las Vegas, NV 89119
(702) 979-2880

April 15, 2017

Personal and Confidential

Ms. Linda Cole
Assistant Town Treasurer
Halifax Town Hall
499 Plymouth Street
Halifax, MA 02338

Re: GASB 74 and 75 – Summary of Results

Dear Ms. Cole:

The purpose of this letter is to summarize our actuarial valuation of the Town of Halifax Other Postemployment Benefits Plan (the "Plan") for the fiscal year ending June 30, 2017 with a valuation date of June 30, 2016 and a measurement date of June 30, 2016 in accordance with Statement Nos. 74 and 75 of the Governmental Accounting Standards Board ("GASB 74/75").

GASB 74 and 75 Impact

The Town has adopted GASB 74 and 75 for its Fiscal Year ending June 30, 2017. The adoption of GASB 74/75 introduces a new actuarial cost method and discount rate as well as new disclosures and methodologies for reporting plan liabilities and OPEB expenses. Significant changes have been made to the recognition of OPEB expenses, making the comparison of Net OPEB Expense in the current valuation to the expenses reported under GASB 45 misleading. The liability reported on the Town's balance sheet will increase dramatically as GASB 74/75 require the recognition of liabilities immediately rather than recognizing liabilities (Net OPEB Obligation) over a 30 year period as GASB 45 allowed. Please keep these changes in mind when considering any comparison to previously reported liabilities and expenses. If you or your auditors have questions on this, feel free to give us a call.

What caused plan liabilities to change from FY 15 to FY 17?

Plan experience was less favorable than expected - for the year ending on the reporting date of June 30, 2017, the Plan saw an experience loss of $2,740,707 or 16.86%. This was mainly due to premiums for Non-Medicare integrated plans increasing more than the expected 10% increase. This was somewhat offset by premiums for Medicare integrated plans increasing less than the expected 10% increase. The actuarial experience loss is amortized into the net OPEB expense over time until fully recognized.

Over the two year period, the Total OPEB Liability (“TOL”) went from $11,363,813 as of June 30, 2014 to $19,174,741 as of June 30, 2016 for an increase of $7,810,928. During that same period the Town’s Net OPEB Liability (“NOL”) increased from $11,258,022 as of June 30, 2015 to $18,995,307 as of June 30, 2017 for a total change of $7,737,285. For a 30-year projection of future costs and liabilities refer to Exhibit C of our GASB 75 report.

Assumption changes

Some key assumptions have changed since the prior valuation, their impact is detailed below.

- ✓ Based on recommendations by PERAC, the mortality table was updated from the RP-2000 Mortality Table projected to 2017 to RP-2000 Healthy Annuitant Mortality Table projected generationally with scale BB and a base year 2009 for males and females. increasing the disclosed liability by $1.18 million.
- ✓ Due to the GASB 75 standards the discount rate was changed from 4.00% to 3.00% increasing the disclosed liability by $2.82 million.
- ✓ GASB 75 requires a change in the actuarial cost method. As such, it has been updated to Entry Age Normal from Projected Unit Credit which increased the disclosed liability by $1.29 million.
- ✓ Assumption changes caused Normal Cost to increase by $160 thousand.

It is important to remember that actuarial assumptions or changes in such do not impact the actual cost of the Plan. Rather, they impact the timing of the recognition of such costs.

Key Drivers of Plan Liabilities

A key driver of plan costs and liabilities is post-age 65 (Medicare Integrated) Plan costs. In the current valuation post-age 65 liabilities represent 87% of the total plan liabilities. Consequently, plan design changes that affect post-65 plan costs will have the most impact on future liabilities.

The age at which participants retire and the percentage of participants who elect coverage for themselves and/or a spouse are also drivers of plan liabilities. Unlike a pension plan where a participant receives a reduced benefit for early retirement, a participant in a retiree welfare plan will receive a higher benefit by retiring early (more years of benefits to be received plus more years before Medicare). A key issue to keep in mind is that participant behavior (as far as retirement is concerned) is affected by many factors including the economy, personal health and work satisfaction.

Future Healthcare Cost Inflation

The future healthcare cost inflation assumption has a significant impact on plan liabilities. In our report we use a long term 5.00% inflation assumption for healthcare costs. This is based on a 2.75% general inflation assumption plus an additional 2.25% inflation assumption due to increased healthcare utilization. The Town's ability to manage future increases in healthcare costs will be a major driver of future plan performance. In the event that healthcare trend rates were 1% higher than forecast and employee contributions were to increase at the forecast rates, the Total OPEB Liability would increase to $28,637,154 or by 49.3% and the corresponding Service Cost would increase to $1,252,272 or by 80.6%. If such healthcare trend rates were 1% less than forecast and employee contributions were to increase at the forecast rate, the Total OPEB Liability would decrease to $12,709,725 or by 33.7% and the corresponding Service Cost would decrease to $348,413 or by 49.8%.

Assumptions

The assumptions used in the GASB 74 and 75 report for mortality rates, termination rates, and retirement rates mirror the assumptions used by PERAC. The long term healthcare inflation trend assumption is 5.00% as described in the previous paragraph.

Odyssey ADVISORS

East Coast
11 Hayward Ave, Building 4
Colchester, CT 06415
(860) 537-9080

West Coast
1350 E. Flamingo Road, Suite 254
Las Vegas, NV 89119
(702) 979-2880

What are some key plan metrics?

While an actuarial valuation under GASB 74/75 can be very complex with many variables, we find it helpful to look at several key metrics shown below to better allow you to manage your plan.

Representative Plan Statistics

	June 30, 2016	June 30, 2014
Total OPEB Liability	19,174,741	11,363,813
Per Eligible Active Plan Participant	96,491	48,120
Per Retiree/Spouse Plan Participant	68,284	50,483
Total Annual Service Cost (annual benefit accrual)	693,532	449,591
Per Eligible Active Plan Participant	5,638	3,568
Expected Employer Share of Retiree Costs	388,896	368,764
Per Retiree/Spouse Plan Participant	3,635	3,512
Net OPEB Liability as a % of Payroll	N/A	N/A
Average Annual Medical Plan Premium (Single Coverage)	7,752	6,675
Average Annual Medical Plan Premium (Family Coverage)	24,963	21,033
Projected 2020 Excise Tax Thresholds		
Annual Medical Plan Premium (Single Coverage)	11,850	
Annual Medical Plan Premium (Family Coverage)	30,950	

Odyssey ADVISORS

East Coast
11 Hayward Ave, Building 4
Colchester, CT 06415
(860) 537-9080

West Coast
1350 E. Flamingo Road, Suite 254
Las Vegas, NV 89119
(702) 979-2880

Impact of Patient Protection and Affordable Care Act ("PPACA") Excise Tax

Under the Patient Protection and Affordable Care Act ("PPACA"), an excise tax will be imposed for tax years beginning after December 31, 2019 (formerly December 31, 2017, but amended by Consolidated Appropriations Act) for high cost employer sponsored health coverage. The law specifies a 40% excise tax, to be paid by the provider of such coverage, of the excess value beyond a basic dollar amount plus an additional "kicker" for qualified retirees or those engaged in a high risk profession. The threshold amounts for 2020 are estimated at $11,850 for single coverage and $30,950 for family coverage with a "kicker" amount of $1,650 for single coverage and $3,450 for family coverage, but the actual thresholds have not yet been released. The estimated 2020 thresholds are based on the threshold amounts for 2018 (original legislation) of $10,200 for single coverage and $27,500 for family coverage, which have been increased by general CPI.

For purposes of the fiscal year ending June 30, 2017, the TOL for the excise tax is $258,153 and the increase in OPEB Expense is $41,754. Given your premiums through the 2017 fiscal year and the excise tax threshold, your average single premiums are $4,098 below the excise tax threshold and your average family premiums are $5,987 below the excise tax threshold. As more regulatory guidance becomes available, the calculation of the excise tax liability will evolve.

Liabilities & Benefit Payments in today's dollars

With the growth of medical care costs over time, the nominal accrued liabilities ("TOL") and benefit payments can appear daunting. However, it is important to remember that a dollar paid in the future is worth less than a dollar paid today. As such, another way to view the projected liabilities and benefit payments is in 2017 dollars so you can compare them to your current budget and ability to pay. As part of our analysis, we have developed projections of plan liabilities & expenses over the next 40 years assuming that the Town's benefit eligible active population remains constant (i.e., employees who terminate or retire are replaced). While the full 40 year projection in 2017 dollars in shown in the report, below are some selected years:

Fiscal Year	Number of Retirees, Spouses & Surviving Spouses	Present Value at 2.75% of Total OPEB Liability	Present Value at 2.75% of Employer Share of Premiums / Claims including "implicit cost"
2017	107	19,174,741	388,896
2022	119	20,962,959	504,380
2027	128	22,845,055	609,550
2032	130	25,041,391	639,373
2037	128	27,554,924	722,798
2042	126	30,439,090	823,889
2047	126	33,670,029	899,853

Looking at these liabilities and expenses over the next 40 years, we would offer the following highlights/observations:

- ✓ The present value of the Plan's TOL will reach its maximum in 2056 at $41.2 million ($118 million in 2056 dollars).
- ✓ The present value of the Plan's benefit payments will reach a peak of $1.03 million in 2056 ($2.96 million in 2056 dollars).
- ✓ The Plan will see the number of retirees & beneficiaries receiving benefits increase from 107 to a maximum of 130 in 2029 before beginning to decline.

East Coast
11 Hayward Ave, Building 4
Colchester, CT 06415
(860) 537-9080

West Coast
1350 E. Flamingo Road, Suite 254
Las Vegas, NV 89119
(702) 979-2880

We have an "unfunded liability". How do we fund it? Can we fund it?

The Plan currently has an unfunded liability of approximately $18,995,307 and this amount is expected to grow over time in the foreseeable future. While some municipal entities across America have chosen to fund this liability, over 95% are not currently dedicating funding to it. The State of Massachusetts has passed legislation allowing municipal entities to establish a Trust for Other Postemployment Benefits ("OPEB") under M.G.L. Chapter 32B, Section 20 for purposes of accumulating assets to pre-fund the liabilities under GASB 75. This legislation was amended effective November 9, 2016 to clarify who may adopt such a Trust and provide guidance on the ongoing operation of such a Trust. To the best of our knowledge, the Town of Halifax has established an irrevocable trust for the purposes of prefunding liabilities under GASB 74/75.

Pre-Funding – if you were to elect to "pre-fund" the OPEB expenses each year by contributing the entire Actuarial Determined Contribution, you would be allowed to use a long-term interest rate based on your underlying investment policy. Assuming a balanced portfolio (60% equities and 40% fixed income), you may be able to use a 6.50% discount rate vs. the 3.00% used in our analysis. The impact of such funding would be to reduce disclosed plan liabilities to $10,958,594 and the OPEB Expense to $(2,389,151). This would require additional funding of $960,500 in the first year which would increase by 0.00% per year until the plan reaches full funding. While this does not impact the ultimate cost of the plan, it would reduce disclosed liabilities and expenses.

In this report, we have outlined several options for pre-funding (including pay-as-you-go, funding over 30 years and funding the annual normal cost):

- Pay-as-you-go – pay annual retiree premiums as they come due with little to no funding set aside in a trust.
- 30-year funding – the concept is to contribute to achieve full funding over a 30 year period.
- Funding annual normal cost – the concept is to fund the excess of the normal cost over current year benefit payments. This approach prevents the liability from growing in current dollars.

Odyssey ADVISORS

East Coast
11 Hayward Ave, Building 4
Colchester, CT 06415
(860) 537-9080

West Coast
1350 E. Flamingo Road, Suite 254
Las Vegas, NV 89119
(702) 979-2880

Please be aware the options presented represent a sampling of your options. The ultimate choice to fund, not to fund or the level of funding will depend on your circumstances. Should you decide that pre-funding is an appropriate option for you we would be happy to help you design a funding schedule that best fits your needs.

Change in cost sharing –You are currently charging retirees 50% of premiums for their contribution. Under Massachusetts law, the maximum allowable contribution rate is 50% - therefore, changing the underlying plan design is currently your only alternative.

GASB 74 and 75 at a glance

The Governmental Accounting Standards Board ("GASB") issued GASB 74 and 75 "*Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions"* on June 2, 2015 which is effective for your June 30, 2018 fiscal year and beyond. This standard largely mirrors the GASB 67 and 68 standards for pension plans. The new standards require increased disclosure and tie interest rates used in the valuation to the plan's underlying investment and funding policy. This may increase the pressure on many entities to begin funding their OPEB liabilities.

On October 18, 2016 GASB released the implementation guide for GASB 74. This report reflects our current understanding of the implementation guide. As more guidance becomes available the methodologies in our report may evolve.

If you or your auditors have questions on this, feel free to give us a call.

Sincerely,

Parker E. Elmore, ASA, EA, FCA, MAAA
President, CEO & Actuary