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Columbia Heights Fire Department Relief Association Volunteer Division



Annual Actuarial Valuation

December 31, 1990

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Appendix I Meaning of Unfunded Accrued Liabilities

June 18, 1991

Board of Trustees
Columbia Heights Fire Department Relief Association (Volunteer Division)
Columbia Heights, Minnesota

Submitted in this report are the results of the December 31, 1990 actuarial valuation of the assets, actuarial values and contribution requirements associated with the benefits provided by the Columbia Heights Fire Department Relief Association Volunteer Division.

The valuation results contained in Section A provide the actuarial information needed to determine the employer's "minimum obligation" effective January 1, 1992. Section A also contains comments regarding the valuation results.

The valuation was based upon information furnished by the Association concerning benefits, financial transactions, active members, terminated members, retirants and beneficiaries. Data was checked for year to year consistency but was not otherwise audited by us. This information is summarized in Section B.

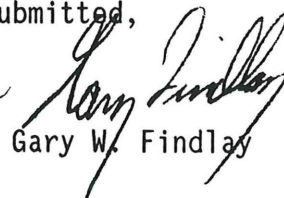
A description of the actuarial funding method and the risk experience assumptions used is contained in Section C. The economic risk experience assumptions, as well as the actuarial funding method to be used, are established by state law.

Information needed to comply with Statement No. 5 of the Governmental Accounting Standards Board is contained in Section D.

The actuarial valuation was prepared using generally accepted actuarial principles and practices based upon the methods, assumptions, summary of plan provisions and the member and financial data described in this report.

Respectfully submitted,


J. Daniel Petersen


Gary W. Findlay

Section A

Valuation Results

COMMENTS

Economic Assumptions and Financing Method

The economic assumption of 5% annual investment return is established by state law. State Law also specifies that the annual minimum obligation of the municipality shall be determined by adding (i) the employer normal cost to (ii) the level dollar amount required to amortize the unfunded actuarial accrued liability by December 31, 2010.

It is worth noting that when the same assumptions and methods are applied to plans which differ in nature, the valuation results may not be comparable. Caution should be exercised when attempting to assess the financial condition of one Association relative to another on the basis of valuation results produced using the assumptions and methods mandated by state law.

Overfunding Condition of Plan

This year, as in the past several years, plan assets substantially exceed actuarial accrued liabilities. It is our understanding that this situation is in large part due to the asset allocation procedure followed at the time that the volunteer plan separated from the plan for paid firefighters.

The plan has a surplus of \$238,196. However, the state guidelines act makes no provision for dealing with surplus assets in volunteer plans which have recurring benefit payments. Consequently, the legally mandated contribution is the normal cost of \$24,749.

Rather than continue to overfund the plan, it would be advisable to contact the staff of the Legislative Commission on Pensions and Retirement to discuss the possibility of a special law to deal with this unusual situation.

Columbia Heights Fire Department Relief Association (Volunteer Division)

CONTRIBUTION RATE TO PROVIDE BENEFITS

Member portion & Employer portion
Effective January 1, 1992

<u>Contributions for</u>	<u>If Paid Equally Throughout Year</u> <u>Dollars</u>
Normal cost of annuities:	
Age & service	19,125
Disability	2,406
Death before retirement	3,218
Refunds of member contributions	<u>0</u>
Total Normal Cost	24,749
Amortization of unfunded actuarial accrued liabilities (UAAL) (19 year level dollar payment)	
Retired lives	0
Active members	<u>0</u>
Total	0
Total Cost of Benefits	24,749
Member contributions	0
COMPUTED EMPLOYER RATE:	
(a) If Paid Equally Throughout Year	24,749
(b) IF PAID AT CALENDAR YEAR END	25,360

Columbia Heights Fire Department Relief Association (Volunteer Division)

Present Actuarial Condition

The Association's accrued actuarial assets were in excess of \$856 thousand on December 31, 1990 -- a considerable sum of money if unencumbered and allocated among a small group of persons.

The following schedule puts the \$856 thousand into perspective by showing the relationship between accrued actuarial assets, actuarial accrued liabilities, and the number of persons with actual and potential claims on the Association's assets.

	<u>Accrued Actuarial Assets</u>	<u>Actuarial Accrued Liabilities</u>	<u>Unfunded Actuarial Accrued Liabilities</u>	<u>% Funded</u>
Retirants and Beneficiaries				
Retired Members (13)		\$308,927		
Surviving Spouses (0)		0		
Surviving Children (0)		<u>0</u>		
Total (13)	\$308,927	\$308,927	\$ 0	100.0%
Deferred Members (2)	105,800	105,800	0	100.0
Active Members (24)	<u>441,533</u>	<u>203,337</u>	<u>(238,196)</u>	217.1
Total	\$856,260	\$618,064	\$(238,196)	138.5%

Actuarial accrued liabilities represent the value, computed as of December 31, 1990 of:

- (i) retirement allowances likely to be paid the 13 retirants and beneficiaries; and
- (ii) the contributions assumed to have been made for the 24 active members from entry into the plan until December 31, 1990.

The value of retirement allowances likely to be paid the 13 retirants and beneficiaries, discounted for investment earnings and mortality, was computed to be \$308,927 as of December 31, 1990. To put this amount in perspective, the \$308,927, together with investment earnings, will just be sufficient to pay the 13 retirants and beneficiaries their allowances for their remaining lifetimes. This assumes the 13 retirants and beneficiaries live and die according to the assumed mortality and the \$308,927 is invested to yield an average annual return of 5.0% over the remaining lifetimes of the retirants and beneficiaries.

With respect to the active members, the actuarial accrued liability of \$203,337 represents the amount that would have been accumulated by December 31, 1990. This assumes the normal cost had been contributed from the date of hire until December 31, 1990 for the 24 actives, and that these amounts had earned 5.0% interest. It also assumes that the members in the past have lived, died, withdrawn and retired according to the actuarial assumptions shown in this report.

Historical Funding Ratio Schedule
(\$ in thousands)

<u>Valuation Date December 31</u>	<u>Actuarial Accrued Liabilities</u>	<u>Accrued Actuarial Assets</u>	<u>Percent Funded</u>
1978	\$216	\$380	175.9%
1979	N/A	N/A	N/A
1980	277	430	155.2
1981	310	422	136.1
1982	316	506	160.1
1983	306	548	179.1
1983*	323	548	169.7
1984	N/A	N/A	N/A
1985	328	619	188.6
1986	388	660	170.2
1990	427	856	200.5
1990#	618	856	138.5

* After change in assumptions.

After change in benefits.

Columbia Heights Fire Department Relief Association (Volunteer Division)

Computed Contributions - Comparative Schedule

Year Ended December 31		<u>Total Normal Cost</u>
<u>Valuation</u>	<u>Fiscal</u>	
1978	1980	\$ 6,835
1979	1981	N/A
1980	1982	8,184
1981	1983	N/A
1982	1984	8,391
1983	1985	7,583
1983	1985*	8,210
1984	1986	N/A
1985	1987	14,110
1986	1988	13,247
1990	1992	13,861
1990	1992#	24,749

* After change in assumptions.

After change in benefits.

Section B
Valuation Data
and
Summary of Benefit Provisions

Columbia Heights Fire Department Relief Association (Volunteer Division)

Retirants and Beneficiaries December 31, 1990

By Type of Annuity Being Paid

<u>Type of Annuity Being Paid</u>	<u>No.</u>	<u>Monthly Amounts</u>	<u>Computed Actuarial Accrued Liabilities</u>
Retirants receiving:			
Age & Service	13	\$2,876.00	\$308,927
Disability	<u>0</u>	<u>0.00</u>	<u>0</u>
Totals	13	2,876.00	308,927
Beneficiaries receiving:			
Spouse			
Child	<u>0</u>	<u>0.00</u>	<u>0</u>
Totals	<u>0</u>	<u>0.00</u>	<u>0</u>
Totals	13	\$2,876.00	\$308,927

Columbia Heights Fire Department Relief Association (Volunteer Division)

Retirants and Beneficiaries December 31, 1990

By Attained Ages

<u>Attained Ages</u>	<u>Number</u>		
	<u>Age & Service</u>	<u>Disability</u>	<u>Death Before Retirement</u>
50-54	1		
55-59	3		
60-64	2		
65-69	1		
75-79	1		
80-84	3		
85-89	<u>2</u>	<u>—</u>	<u>—</u>
Totals	13	0	0

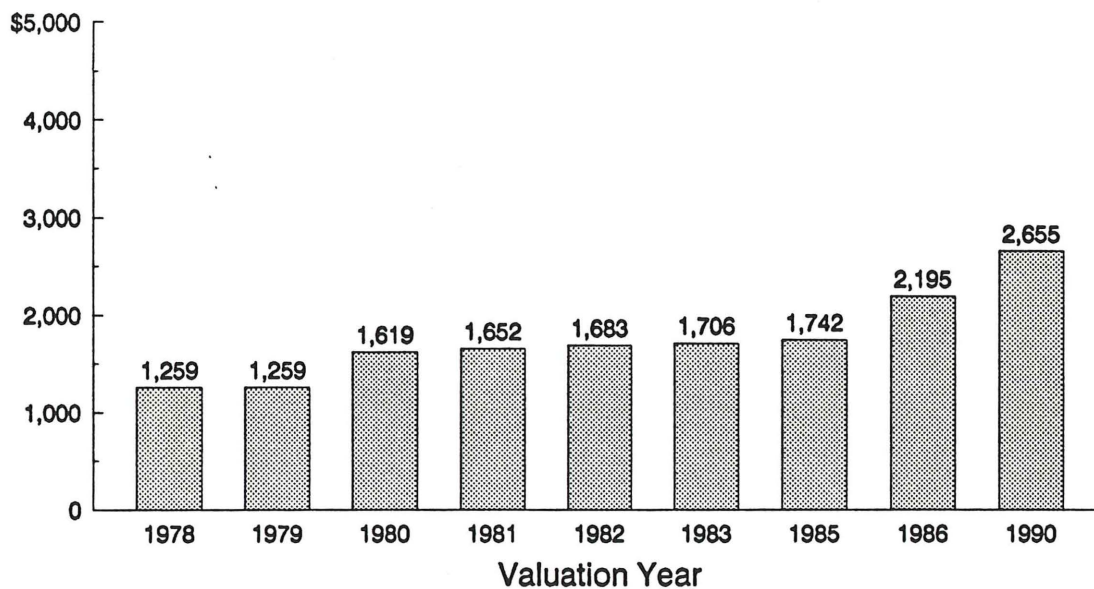
Columbia Heights Fire Department Relief Association (Volunteer Division)

Retirants and Beneficiaries Added to and Removed from Rolls

Comparative Statement

<u>Valuation Date December 31</u>	<u>No. Added to Rolls</u>	<u>No. Removed from Rolls</u>	<u>Rolls End of Year No.</u>	<u>Annual Allowances</u>	<u>Discounted Value of Total Allowances</u>
1978			10	\$12,588	\$138,888
1979			10	12,588	135,468
1980			10	16,193	164,360
1981	1		11	18,173	188,024
1982	1		12	20,192	211,190
1983	1		13	22,172	245,601
1985		1	12	20,900	224,124
1986			12	26,337	271,836
1990	1		13	34,512	308,927

Average Annual Allowances



Columbia Heights Fire Department Relief Association (Volunteer Division)

Active Members December 31, 1990

By Attained Age and Years of Service

Attained Age	Years of Service to Valuation Date							Totals
	0-4	5-9	10-14	15-19	20-24	25-29	30 Plus	
Under 20	1							1
20-24	2							2
25-29	2	3						5
30-34	4	3						7
35-39	3		2					5
40-44			2					2
50-54				2				2
	—	—	—	—				—
Totals	12	6	4	2				24

While not used in the financial computations, the following group averages are computed and shown because of their general interest.

Age: 32.4 years.

Service: 5.9 years.

Columbia Heights Fire Department Relief Association (Volunteer Division)

Comparative Schedule

Of Active Members

Valuation Date December 31	Active Members	Valuation Payroll	Average			
			Age	Service	Pay	% Incr.
1978	20	\$N/A	33.3 yrs.	5.8 yrs.	\$N/A	N/A%
1979	20	N/A	33.5	6.3	N/A	N/A
1980	20	N/A	34.3	7.2	N/A	N/A
1981	21	N/A	31.7	5.8	N/A	N/A
1982	22	N/A	32.1	6.3	N/A	N/A
1983	20	N/A	32.0	6.3	N/A	N/A
1985	27	N/A	30.8	5.3	N/A	N/A
1986	25	N/A	32.0	6.4	N/A	N/A
1990	24	N/A	32.4	5.9	N/A	N/A

Section C

Valuation Methods and Assumptions

Columbia Heights Fire Department Relief Association (Volunteer Division)

Valuation Methods and Assumptions

The Entry Age Normal Cost method was used to determine the normal cost of all benefits. The rate of investment return (interest) as required by state law used in making the valuation was 5.0 percent per annum, compounded annually. Age & service retirement was assumed to occur at age 58, or attained age if older.

Mortality Table*

Sample Ages	Single Life Values: Present Value of \$1 Monthly			
			Future Life	
			Expectancy (Years)	
	Men	Women	Men	Women
45	\$177.21	\$189.58	29.50	34.00
50	163.12	177.21	25.20	29.50
55	147.50	163.12	21.16	25.20
60	130.52	147.50	17.42	21.16
65	112.87	130.52	14.05	17.42
70	95.20	112.87	11.09	14.05
75	77.77	95.20	8.52	11.09
80	61.71	77.77	6.39	8.52

* UP-1984 Table set forward 2 years for males and set back 3 years for females.

Sample Rates of Separation from Active Employment Before Retirement, Death or Disability

Sample Ages	% of Active Members Separating within Next Year
20	1.50%
25	1.25
30	1.00
35	0.75
40	0.50
45	0.25
50+	0.00

Anticipated Disability Retirements

<u>Sample Ages</u>	<u>% of Active Members Becoming Disabled within Next Year</u>
20	0.08%
25	0.08
30	0.08
35	0.08
40	0.20
45	0.26
50	0.49
55	0.89

Section D

**The Pension Benefit Obligation
and Certain Other Disclosures
Required by Statement No. 5 of the
Governmental Accounting Standards Board**

PENSION BENEFIT OBLIGATION

The amount shown below as the "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases, estimated to be payable in the future as a result of employee service to date. The measure is the actuarial present value of credited projected benefits and is intended to (i) help users assess the plan's funding status on a going-concern basis, (ii) assess progress being made in accumulating sufficient assets to pay benefits when due, and (iii) allow for comparisons among public employee retirement plans. The measure is independent of the actuarial funding method used to determine contributions to the plan.

The pension benefit obligation was determined as part of an actuarial valuation of the plan as of December 31, 1990. Significant actuarial assumptions used in determining the pension benefit obligation include (a) a rate of return on the investment of present and future assets of 5.0% per year compounded annually, (b) the assumption that benefits will not increase after retirement.

At December 31, 1990, the assets in excess of the pension benefit obligation were \$265,453, determined as follows:

Pension Benefit Obligation:

Retirants and beneficiaries currently receiving benefits and terminated employees not yet receiving benefits	\$414,727
Current employees --	
Accumulated employee contributions including allocated investment income	0
Employer financed	<u>168,770</u>
Total Pension Benefit Obligation	\$583,497
Net assets available for benefits, at cost (market value was \$870,879)	<u>848,950</u>
Unfunded Pension Benefit Obligation	<u>\$265,453</u>

Changes in plan benefits which were first evaluated as of December 31, 1990 caused the Pension Benefit Obligation to increase by \$174,000.

CONTRIBUTIONS REQUIRED AND CONTRIBUTIONS MADE

The Association's funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are designed to accumulate sufficient assets to pay benefits when due. The normal cost and actuarial accrued liability are determined using an entry age actuarial funding method.

During the year ended December 31, 1990, employer contributions totaling \$27,000 were made in accordance with contribution requirements determined by an actuarial valuation of the plan as of December 31, 1986. The employer contributions consisted of \$13,247 for normal cost and \$13,753 for amortization of the unfunded actuarial accrued liability.

Significant actuarial assumptions used to compute contribution requirements were the same as those used to compute the standardized measure of the pension benefit obligation.

Computed Contribution Comparative Schedule

Fiscal Year <u>December 31</u>	Valuation Date <u>December 31</u>	<u>Contribution Rates</u>		<u>Dollar Contribution</u>	
		<u>Normal Cost</u> <u>% of Valuation</u> <u>Payroll</u>	<u>UAAL</u> <u>Dollars</u>	<u>For Fiscal Year</u> <u>Computed</u>	<u>Actual</u>
1990	1986	\$13,247	0	13,247	27,000
1992	1990	24,749	0	24,749	

REQUIRED SUPPLEMENTARY INFORMATION

ANALYSIS OF FUNDING PROGRESS

Valuation Date <u>December 31</u>	(1) Net Assets Available for Benefits	(2) Pension Benefit Obligation <u>(PBO)</u>	(3) Percent Funded <u>(1)/(2)</u>	(4) Unfunded PBO <u>(2)-(1)</u>
1986	\$645,087	\$364,354	177.0%	\$0
1990	848,950	583,497	145.5	0

Analysis of the dollar amounts of net assets available for benefits, pension benefit obligation, and unfunded pension benefit obligation in isolation can be misleading. Expressing the net assets available for benefits as a percentage of the pension benefit obligation provides one indication of the plan's funded status on a going-concern basis. Analysis of this percentage over time indicates whether the system is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the plan.

Appendices

APPENDIX I

MEANING OF UNFUNDED ACCRUED LIABILITIES

Almost every pension plan (public or private) has "unfunded accrued liabilities", so whatever they are, they aren't rare. Since the term is not part of everyday conversation, it needs some definition.

"Accrued liabilities" are the present value \$ of plan promises to pay benefits in the future based upon service already rendered - - - a liability has been established ("accrued") because the service has been rendered, but the resulting monthly cash benefit may not be payable until years in the future. Accrued liabilities \$ are the result of complex mathematical calculations, which are made by the plan's actuary (which is the name given to the specialist who makes such calculations).

If "accrued liabilities" at any time exceed the plan's accrued assets (cash & investments), the difference is "unfunded accrued liabilities". This is the common condition. If the plan's assets equalled the plan's "accrued liabilities", the plan would be termed "fully funded". This is a rare condition.

Each time a plan adds a new benefit which applies to service already rendered, an "accrued liability" is created, which is also an "unfunded accrued liability" because the plan can't print instant cash to cover the accrued liability. Payment for such unfunded accrued liabilities is spread over a period of years, commonly in the 20-40 year range.

Unfunded accrued liabilities can occur in another way: If actual financial experience is less favorable than assumed financial experience, the difference is added to unfunded accrued liabilities. In plans where plan benefits are directly related to an employee's pay near time of retirement (a common plan provision) rather than his average pay throughout his working career, unfunded accrued liabilities have been increasing in recent years because unexpected rates of pay increase have created additional accrued liabilities which could not be matched by reasonable investment results. Some of these unexpected pay increases are the direct result of inflation, which is a very destructive force on financial stability.

The existence of unfunded accrued liabilities is not bad, then (any more than a mortgage on your house is "bad"), but the changes from year to year in amount of unfunded accrued liabilities are important - - - "bad" or "good" or somewhere in between.

Nor are unfunded accrued liabilities a bill payable immediately (your food costs are payable immediately), but it is important that policy-makers prevent the amount from becoming unreasonably high and it is vital that your plan have a sound method for making payments toward them so that they are controlled.

The existence of large amounts of unfunded accrued liabilities indicates that total contributions in past years were less than level - - - an almost certain history if retired life liabilities are not fully funded now.