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U.S. States Are Quantifying OPEB Liabilities And Developing Funding Strategies As The GASB Deadline Nears

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U.S. States Are Quantifying OPEB Liabilities And Developing Funding Strategies As The GASB Deadline Nears

The fiscal 2008 deadline for U.S. states to implement GASB 45, which establishes new accounting and reporting practices for other postemployment benefits (OPEB) liabilities, is fast approaching and most have quantified their liabilities and many are developing strategies to manage long-term funding requirements. We believe that with or without prefunding OPEB liabilities, state governments should continue meeting ongoing OPEB cost requirements with no adverse effect on near-term credit quality. However, increasing costs governments face for health care and the growing retiree population could strain budgets and balance sheets over the longer term.

State OPEB Status

Based on the latest Standard & Poor's Ratings Services research, 40 states have completed an actuarial valuation of their OPEB liabilities, which are significant -- nearly \$400 billion. The range of liabilities is vast: From North Dakota's \$52 million, to New Jersey's \$58.1 billion for future obligations. Comparisons are extremely difficult, however, given the variation in actuarial methods and assumptions. OPEB liabilities also factor in future health care cost inflation assumptions, which vary significantly. Due to this variability, the absolute liability reported by a government will be less important than the burden that OPEB costs have on a state's budget and balance sheet. Nearly all states fund their OPEB costs on a pay-as-you-go basis and GASB 45 does not require states to fund this liability. In addition, reported liabilities may not all be payable from a state's general fund.

State Strategies For Managing OPEB

States have focused on a range of strategies to begin managing these liabilities. The OPEB strategies for most states have not significantly altered the liability, but have focused on their ability to maintain current benefit levels, or to begin incrementally increasing appropriations. A number of states have established a task force or commission to review all benefits and funding options and develop a long-term solution. Some states, such as Alabama, Delaware, Georgia, Kentucky, Maryland, Massachusetts, Ohio, South Carolina, Utah, Vermont, and West Virginia have established trust funds to accumulate assets. Here's how other states are responding:

- North Carolina has increased vesting periods and changed benefit levels for new employees to manage future liability.
- In addition to capping and eliminating certain benefits, Utah has moved to full actuarial required contribution (ARC) funding, which will eliminate a net OPEB obligation from accumulating on its balance sheet.
- Virginia has made progress in ARC funding for two of its five OPEB plans.
- Delaware has addressed its liabilities in several ways. In addition to appropriations to a trust fund, the state plans to deposit 0.3% of the state payroll to the trust annually. The state statute also requires annual savings from health care cost containment initiatives to be deposited to the trust fund.
- Ohio is one of the few states that has actively managed OPEB costs and liabilities and has accumulated about \$12 billion in assets.

Broader Concerns For States

In addition to their own liabilities and funding requirements, local issues relating to OPEB will require state attention as information becomes more broadly available. State legislative action may be required to provide local governments the range of options needed to manage their OPEB liabilities, including authorizing trust funds, reserves, and managing benefit levels. In many states, this process is already under way. The fiscal health of local governments, school districts, community colleges and other local entities are also likely to demand state interest. Education is a constitutional obligation in most states and most school districts rely on state aid. A school district's ability to manage its expenditures, including OPEB liabilities, is an important element of fiscal stability. If an educational program is in jeopardy, state intervention or assistance may be necessary. While each state has a different approach to local government funding, and their level of support in distress situations varies widely, the fiscal health of all local government entities may require closer scrutiny if significant liabilities exist.

Long-Term Liabilities Differ From Debt

We've traditionally viewed unfunded postretirement liabilities as debt-like because they represent future payments that usually have some legal basis for funding: constitutional, statutory, or contract-based. However, a postretirement liability is subject to significant variation based on the actuarial methods and assumptions used to calculate it, as well as the performance of any fund assets. OPEB liabilities are likely to be more volatile than pension liabilities because they include future health care cost inflation assumptions, which vary significantly. Because of this inherent variability, pension or OPEB liabilities differ significantly from a debt obligation, which is fixed. For this reason, pension and OPEB liabilities will not appear on the debt statement used to analyze and report on debt ratios in our public finance credit reports unless pension obligation bonds (POBs) or OPEB obligation bonds (OPEBOBs) have been issued.

Liabilities Need To Be Managed

OPEB liabilities are one of many factors that we evaluate for a credit rating and the liabilities' overall effect will be realized over time. State budgets are expected to absorb OPEB costs and address them along with other service costs. How the liability is managed, along with a government's capacity to fund these obligations annually--either on a pay-as-you-go or an accrual basis--will be an important element of the credit review (see Credit FAQ: OPEB Liabilities Pose Minimal Near-Term Rating Risk For Public Finance Credits, Dec. 4, 2006, on RatingsDirect).

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies

Alabama

In a special session on Feb. 26, the state Legislature passed a law directing the State Employees Insurance Board and Public Education Employees Insurance Board to create irrevocable trust funds to help fund future retiree health care costs. The initial contributions will come from the boards' excess reserves. The 2006 actuarial study for the state's public education retiree health benefits estimated a long-term unfunded liability of \$12.5 billion, which is \$2 billion less than the 2005 estimate, and a total annual required contribution of \$962.7 million, assuming a 5% discount rate, as of Sept. 30, 2006. The most recent actuarial study available for the other state employee's retiree health benefits reflected a \$5.3 billion unfunded liability and a \$343.7 million annual required contribution, assuming a 4% discount rate, as of Sept. 30, 2005. The Public Education Employees Health Insurance Plan has already established its trust fund and has transferred \$417 million from its reserves. The State Employees Insurance Board recently voted to make an initial transfer of \$50 million into its trust fund.

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies (cont.)

Alaska

Unlike most states, Alaska's post-employment health care benefits are included in its pension system. There is no separate liability for OPEBs. The pension system has a funded ratio of 71.4%, representing the state's assets versus the actuarial accrued liabilities of both its pension obligations and post-employment health care benefits. The total unfunded liability is \$7 billion.

Arizona

Eligible retirees in Arizona may participate in the Arizona Department of Administration's (ADOA) or Arizona State Retirement System's (ASRS) benefit plans. The unfunded actuarial accrued liability for the ASRS health insurance premium benefit as of June 30, 2006 was \$420 million and the long-term disability program in 2006 was \$380 million. A preliminary 2006 actuarial study estimated the ADOA's actuarial unfunded liability for post-retirement health benefits between \$323 million and \$400 million, assuming a 4.25% discount rate, primarily due to an implicit subsidy of premium rates for retirees under age 65. The increase in costs to fully fund the ADOA's annual required contribution is between \$3 million and \$12 million annually.

Arkansas

The state pays for OPEBs for uniformed state police and is qualifying its OPEB liability under GASB 45. The actuarial report is expected to be completed by the end of 2007 and reported in the fiscal 2008 audit. Initial estimates indicate a liability of about \$3.0 billion.

California

Complying with GASB's new disclosure rule, California revealed that it has an estimated unfunded OPEB actuarial liability of \$47.88 billion as of July 1, 2007 for retiree health care benefit programs. The state's OPEB valuation lies in the lower range of previous estimates of state OPEB, using rough per capita estimates based on the OPEB of other states. California is convening a special commission to consider ways to address its OPEB liability, which could result in either finding ways to lower OPEB by reducing retiree benefits, or to increase yearly funding. The commission is scheduled to release its report on Jan. 1, 2008, shortly before the release of the governor's fiscal 2009 budget proposal. The OPEB liability partially constrains California's future financial flexibility, but does not prevent it from obtaining a higher GO bond rating. The actuarially recommended annual required contribution (ARC) of the state to amortize the unfunded liability over 30 years is \$3.59 billion in fiscal 2008. This is still manageable compared to the governor's proposal for \$103.8 billion in overall fiscal 2008 general fund spending, of which \$1.1 billion would be pay-as-you-go general fund spending for OPEB, and \$1.36 billion in overall pay-as-you-go OPEB spending including all state funds. California has historically paid eligible retiree medical benefits on a pay-as-you-go basis. Using the assumptions of the state's outside actuaries, Gabriel Roeder Smith & Company, the state's OPEB was derived by assuming no change in the current programs. The OPEB calculation depends on a number of actuarial assumptions, the most critical being a 4.5% discount rate for a pay-as-you-go system, a rate consistent with the state's interest earnings on its short-term pooled money funds.

Colorado

Colorado's OPEB plan is funded through the Public Employees Retirement Association (PERA) and is a cost-sharing, multi-employer plan with a health care trust fund in place. PERA has released a report on OPEBs for state employees, some school district employees, some local districts, and judicial employees with an estimated liability of \$1.03 billion. PERA says total liability is 17% funded, using the historical difference between pay-as-you-go billed to the state, school districts, and others, and the actual pay-as-you-go costs. Colorado's share of this liability has not been calculated and it does not plan to release an estimate of the state portion of the liability in its annual financial statements.

Connecticut

In an actuarial report dated March 2007, the OPEB actuarial accrued liability for persons covered under the State Employee Retirement System (SERS) and other state retirement systems, excluding the Teachers' Retirement System, was estimated as of April 1, 2006, to range from \$11.4 billion to \$21.7 billion. The amounts depend on various assumptions, including medical cost inflation rates, establishing a trust to fund those liabilities, initial and annual amounts deposited in such a trust, and discount rates. The report used discount rates ranging from 4.5% to 8.5%. The amount of the annual required contribution under these various assumptions ranges from \$1.0 billion to \$1.6 billion for the fiscal year ending June 30, 2007. Both the governor and the state comptroller have submitted partial funding proposals to the Legislature to begin addressing the OPEB liability issue for members of the State Employee Retirement Fund in this legislative session. The State Teachers Retirement System is part of Phase 2 implementation, and under Statement 45 is not required to be reported until fiscal 2009. The retirement board has received an actuarial valuation that indicates an accrued liability of \$2.2 billion on an unfunded basis based on certain assumptions, including a 4.5% earnings assumption and a 30 year amortization period. If the plan was to be prefunded, the unfunded liability would drop to \$1.3 billion based on an 8.5% earnings assumption.

Delaware

Under Executive Order No. 67, the state conducted a comprehensive study of the potential effects of the GASB 45 other postemployment benefits (OPEB) accounting disclosure. Delaware conducted an actuarial valuation that projected a total unfunded OPEB liability of approximately \$4 billion. According to the study, the state's estimated annual required contribution (ARC) in fiscal 2008 is \$286 million, or in excess of \$180 million more than the projected pay-as-you-go amount. The state's pay-as-you-go OPEB appropriation totaled about \$85 million (3% of general fund expenditures) in fiscal 2005. The state study also included a detailed array of potential options for addressing OPEB. At this point, Delaware plans to deposit 0.3% of its payroll (equal to roughly \$5 million) in fiscal 2007 into an OPEB trust fund that the state originally established in 2000. To date, the state has accumulated about \$24 million in this OPEB trust fund. Delaware will continue to examine its various options for addressing OPEB.

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies (cont.)

Florida

Florida recently conducted a full assessment of its post retirement benefits. The state funds a health insurance subsidy (HIS) which is a cash payment directly to retirees to offset the cost of health insurance. State law permits a reduction or elimination of this payment. It is currently funded at 1% of payroll. In consultation with GASB, this will now be recorded as a pension benefit under GASB 27. The unfunded actuarial accrued liability for this benefit is estimated at \$4.5 billion as of July 1, 2006. The Florida Retirement System is well funded and had assets in excess of liabilities totaling \$6.2 billion as of July 1, 2006. State law allows retired employees to participate in the State Employees Health Insurance Program and they are required to pay a premium cost for these benefits. The premium cost is a legislated amount and is comparable to the premium for active employees. Retiree healthcare costs increase with age so the premium charged to retirees does not match the full cost of benefits. This differential will be the implicit rate subsidy for Florida. The actuarial accrued liability of this benefit after deducting for retiree contributions is estimated to range from \$2.1 billion (assuming a 7.75% investment return) and \$3.6 billion (assuming a 4% investment return) of July 1, 2005.

Georgia

Georgia provides other post employment benefits (OPEB) to its retirees through the State Health Benefit Plan, a cost-sharing, multiple employer plan for state employees, teachers and non-certificated personnel, and through the Board of Regents' plan for state employees of the higher education system. Georgia's OPEB UAAL was estimated in fiscal 2005 at \$15 billion for the state health benefit plan and \$1.7 billion for the Board of Regents. Preliminary numbers for fiscal 2006 placed the state's UAAL for the State Health Benefits Plan at \$19.18 billion with an annual required contribution of \$1.67 billion. Of this amount, the state, teachers and non-certificated UAAL amount to \$5.08 billion, \$13.17 billion and \$924 million, respectively. The accrued liability portion of the ARC is \$721 million with state and teachers accounting for \$201 million and \$486 million, respectively. These preliminary numbers reflect the use plan and coverage elections of current retirees, age-based claim data and assume increases in retiree premiums in the future. The 2006 numbers are preliminary and subject to change. The Board of Regents has not released updated numbers for fiscal 2006. The state implemented a partial funding strategy. It will continue to finance the Teachers and Non-certificated personnel's benefits on a pay-as-you go basis. While it will not contribute the full amount required to meet current costs and amortize the UAAL for the state employee portion, it will fund a percentage, currently estimated at 4% of pay, above the annual pay-as-you go cost. The 2006 valuation assumes a 4.5% discount rate for the Teachers and Non-Certificated Plans and a slightly higher discount rate of 5% was used for the state employees portion of the State Health Benefit Plan to reflect the additional contribution above the annual pay-as-you go cost. In the fiscal year 2008 budget, the 4% of pay dedicated for OPEB is expected to generate \$147 million.

Hawaii

Hawaii recently completed its OPEB valuation. The state's liabilities include benefits provided to state employees, teachers, and the voluntary employee beneficiary trust (VEBA). Assuming no prefunding (using a 5% discount rate), the state's unfunded actuarial accrued liability is \$11.1 billion and the ARC is \$841.2 million. This represents 46.9% of the state's payroll. Assuming prefunding (allowing for an 8% discount rate), the unfunded actuarial accrued liability is \$7 billion and the ARC is \$592.2 million, or 31% of payroll. Funding--done on a pay-as-you-go basis--was \$177 million in fiscal 2005.

Idaho

Idaho's liabilities relating to retiree medical, life and self-funded disability benefits are estimated to range from \$286.1 million to \$408.6 million. The actuarial valuation estimates the liability as of July 1, 2006 and the range of liabilities was calculated using a discount rate of 5% assuming no pre-funding of liabilities and 7.25% if there was pre-funding of the liabilities.

Illinois

Illinois provides health, dental, vision and life insurance benefits for retirees and their dependents but has not released an actuarial valuation estimate of its OPEB liabilities. In fiscal 2006, the cost of these benefits, which are paid on a pay-as-you-go basis, was \$577.9 million or 2.2% of state general fund expenditures.

Indiana

Indiana is under taking an actuarial OPEB study that will be included in the state's 2008 comprehensive annual financial report. Retired state employees can join the state's health plans, but they must pay the entire cost. Therefore, the state does not expect a significant liability in this area. However, there are three plans under which the state does pay part or the entire amount of the premiums for retirees: legislators, state police, and conservation officers.

Iowa

Iowa's valuation shows an OPEB cost of \$22.7 million for fiscal 2007, with a total unfunded actuarial accrued liability subsidy for OPEB of \$219.7 million. Iowa is required under Iowa Code Section 509A.13 to provide state retirees access to state health plans offered to active state employees. The state charges the retirees the same premium as active state employees pay, although the retiree pays 100% of the premium rate. This practice results in a blended premium, with the premium based upon not only the active participants but also the retirees' expected health claims. The state is required to adopt GASB 43 and 45 starting in fiscal 2008 but is choosing to voluntarily adopt the standards for fiscal 2007.

Kansas

Kansas officials have yet to determine the state's OPEB liability; it should be very low, however, because the state provides relatively few benefits.

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies (cont.)

<p>Kentucky</p> <p>Kentucky funded the postemployment medical insurance for the Kentucky Teachers Retirement System (KTRS) at just 3.0%, leaving a \$4.2 billion unfunded accrued liability, while the liability for Kentucky Employees Retirement System (KERS) retirees was \$8.1 billion. Kentucky has committed itself to taking on the pension and medical insurance benefits liabilities burden for both KTRS and KERS members, even though it is not technically required to provide OPEB benefits to KTRS members. Addressing these funding shortfalls will likely consume increasing portions of future budgets. For fiscal 2007, the state has budgeted \$500 million of general fund money for the pension and the current amount for OPEB benefits. This includes some funding for the teachers' retirement system as well. General fund surpluses are one likely source of future funding. The governor recently formed a blue ribbon tax force to explore pension and OPEB solutions. The commission has had initial meetings, with a recommendation due by Dec. 1, 2007.</p>
<p>Louisiana</p> <p>The state has not completed an actuarial valuation of its OPEB liabilities at this time.</p>
<p>Maine</p> <p>Maine provides OPEB benefits for most retired state employees and a portion of the health insurance premiums for retired teachers. GASB 45 will require the state to begin disclosing the liability for these OPEB benefits in its fiscal 2008 financial reports. Maine's initial actuarial study, issued for fiscal 2003, estimated the state's OPEB liability for current and future eligible retirees at \$1.2 billion. A second valuation for June 30, 2006, released in January 2007, estimated the liability at \$4.7 billion. The amount, which assumes no prefunding, is more than 9x the amount of direct debt the state has outstanding. The report estimated that for full amortization over a 30-year period, the required ARC for fiscal 2007 would be \$116 million. Under this estimate, the required ARC would increase to \$296 million in fiscals 2015 and 2016. In a second scenario assuming prefunding at a rate of 7.5%, the state's estimated unfunded OPEB liability would reduce to \$3.2 billion, with an ARC of \$275 million for fiscal 2007. The governor has proposed shifting the Retiree Health Trust Fund to the state retirement system, where it would yield higher investment returns, and the state is currently developing legislation to create an irrevocable OPEB trust. Given the gap between the ARC and current expenditures, the state has decided to increase its OPEB appropriations over a 10-year period to reach a level of full ARC funding. The plan calls for an initial deposit of approximately \$80 million into the Retiree Health Trust Fund in fiscal 2008 to seed the initial effort. The state plans to contribute \$101.7 million in fiscal 2008 and \$111.9 million in fiscal 2009; starting in fiscal 2010, the state will contribute 10% of the full ARC amount above the pay-as-you-go amount. This additional payment will ratchet up to 20% in fiscal 2011, ultimately reaching the full ARC payment in fiscal 2019. These estimates do not take into account the recent expansion of retiree health insurance benefits extended to local firefighters and municipal and county police, for which the state will be responsible. The state is collecting data now to account for this expanded population, for use in re-estimating the state's total OPEB liability.</p>
<p>Maryland</p> <p>In January 2007, the state received a second actuarial report addressing its OPEB liability as of July 1, 2006, which put the amount between \$9.0 billion and \$14.5 billion. Based on the assumptions within the report, the state's 2007 ARC would have ranged from an estimated \$770 million to nearly \$1.12 billion. The state's general fund has historically provided for 60% of the annual costs of current, pay-as-you-go, and OPEB benefits; in fiscal 2006, that amount was about \$140 million. In fiscal 2007, the state set aside \$100 million in general funds in its state reserve fund/dedicated purpose account to meet future OPEB obligations; an additional \$100 million in general funds is included in the fiscal 2008 budget.</p>
<p>Massachusetts</p> <p>An independent actuarial firm contracted by the commonwealth released an initial valuation report in June 2006 on the commonwealth's liability for health care and life insurance benefits. The report presented two separate calculations of the commonwealth's OPEB liability, depending on whether the commonwealth would prefund the liability in a manner meeting the requirements of GASB 45. According to the report, assuming no prefunding, the commonwealth's actuarial accrued liability for OPEB obligations earned through Jan. 1, 2006, is \$13.287 billion. Full amortization of this liability over a 30-year period using an amortization growth rate of 4.5% per year would require ARCs commencing at \$1.062 billion for fiscal 2006 and increasing to a projected \$2.758 billion in fiscal 2016. However, assuming prefunding, the commonwealth's actuarial accrued liability would reduce to \$7.562 billion; the ARC would commence at \$702.9 million for fiscal 2006, increasing to a projected \$1.205 billion for fiscal 2016. The commonwealth has not yet made any decision as to when or how it will fund the liability. The report covered only the commonwealth's OPEB obligations for commonwealth employees and their survivors.</p>
<p>Michigan</p> <p>The state provides health, dental, and vision benefits and life insurance coverage to retirees of all pension plans to which the state contributes, with the exception of the military retirement plan. Benefits are funded on a cash flow basis. The vast majority of the state's retiree benefits payments go toward retirees under the state employees' retirement system, with retirees in the state police retirement system making up most of the remainder. Under the retirement systems for state employees and the state police, retirees contribute 5%, 10%, and 10%, respectively, of the monthly premiums for health, dental, and vision coverage. Recent non-GASB 45 actuarial valuations found that the state's accrued liabilities for these benefits totaled \$6.9 billion for the state employees' system and \$467 million for the state police system.</p>
<p>Minnesota</p> <p>The state had an actuarial valuation to determine the impact of implementing GASB Statement No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions", required for fiscal year 2008. Based on this actuarial valuation, the estimated unfunded actuarial accrued liability at the beginning of the year is \$659 million, which will be amortized over 30 years. The estimated annual required contribution for the period ended June 30, 2008 is \$66 million.</p>
<p>Mississippi</p> <p>The state has not yet completed an actuarial valuation.</p>

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies (cont.)

<p>Missouri</p> <p>The state has completed an initial actuarial report released in June 2006 for the Missouri State Employees' Retirement System. The unfunded actuarial accrued liability for fiscal 2006 is \$1.267 billion (81.3% of payroll) assuming payment of the full \$103.3 million ARC. If the state does not pay the ARC, the unfunded actuarial accrued liability would be \$2.186 billion.</p>
<p>Montana</p> <p>The state's OPEB liability is \$306.2 million, with an ARC of \$29.9 million.</p>
<p>Nebraska</p> <p>The state's OPEB liability should be immaterial, primarily consisting of an implied rate subsidy for health insurance premiums for retirees.</p>
<p>Nevada</p> <p>The state has a liability for OPEB benefits that should be valued between \$1.62 billion and \$4.10 billion, compared with an annual contribution of \$114 million. The legislature will decide during the 2007 session whether to establish a trust fund to prefund the liability or continue to fund it on a current basis.</p>
<p>New Hampshire</p> <p>New Hampshire state law provides health care benefits for some retired employees. As of May 2007, New Hampshire had received a draft actuarial OPEB liability estimated at \$1.5 billion-\$2.9 billion, depending on whether the liability is prefunded. Most of the state's employees who were hired on or before June 30, 2004, may become eligible for these benefits if they reach normal retirement age while working for the state and receive their pensions on a periodic basis rather than a lump sum. These and similar benefits for active employees are provided through the Employee Benefit Risk Management Fund, which finances the state's self-funded employee and retiree health benefit program. Payments from the state of actuarially determined working rates finance the fund, which the state established in October 2003. The state paid approximately \$30.7 million to fund health care benefits for about 9,375 state retirees (and their covered dependents) receiving a periodic pension benefit for fiscal 2006 (ended June 30). Of the amount paid, \$14.8 million was received from self-supporting state agencies. An additional major source of funding for retiree benefits was the New Hampshire Retirement System's medical subsidy program for certain employees, which totaled approximately \$13.5 million for fiscal 2006.</p>
<p>New Jersey</p> <p>The state funds its OPEB benefits on a pay-as-you-go basis. For fiscal 2007, the state expended \$1.03 billion to pay for postretirement medical benefits; the adopted fiscal 2008 budget has that cost growing to about \$1.13 billion. Based on an initial valuation submitted to the State Health Benefits Commission by AON Consulting on July 26, 2007, the fiscal 2007 accrued PRM liability was \$58.1 billion. The discount rate used to determine the retiree health care liabilities was 4.5%, which is the maximum discount rate permitted when employers do not prefund that liability. At this time, the state has not indicated any plans to change from its current practice of funding postretirement medical benefits on a pay-as-you-go basis. However, the state has begun to address the consistent growth in expenditures each year with reforms put in place earlier this year.</p>
<p>New Mexico</p> <p>In August 2007, New Mexico completed a revised actuarial valuation and review of OPEB for the New Mexico Retiree Health Care Authority. The study estimated the state's total long-term unfunded liability at \$4.1 billion, as of June 30, 2006, assuming a discount rate of 5% and the payment of benefits from arrangements similar to a qualified trust. The ARC would be \$383 million for fiscal 2007. A legislative committee formed to review funding options for the liability has not yet published its findings.</p>
<p>New York</p> <p>New York State has completed a preliminary valuation for the state's OPEB disclosure. The state's actuarial accrued unfunded OPEB liability is approximately \$47 billion using a level percent of projected payroll under the frozen entry age actuarial method. The assumed discount rate is 4.1%, which would equate to a rate closer to pay-as-you-go funding. The actuarially determined ARC totals \$3.7 billion, or about \$2.7 billion more than the fiscal 2007-2008 budget's assumed pay-as-you-go OPEB expense of \$1.0 billion. The state's financial plan does not presently reflect the assumption of prefunding the unfunded OPEB liability. However, the New York State Health Insurance Council is reviewing and weighing potential options that would address the state's OPEB liability. It is possible that the state's approach to addressing GASB 45 could be formulated in conjunction with the fiscal 2009 budget process. New York State's pay-as-you-go OPEB appropriation totaled about \$858 million, or roughly 2% of general fund expenditures, in fiscal 2006.</p>
<p>North Carolina</p> <p>North Carolina has regularly evaluated its OPEB costs. An updated actuarial valuation of retiree health care benefits (OPEB) liability was calculated in 2006. The accrued liability for benefits earned as of Dec. 31, 2005, is an estimated \$23.9 billion. The actuarial assumptions reflect a short-term discount rate of 4.25%, which is lower than previous studies. The ARC is \$2.4 billion. Employers included in the retiree health care benefit plan include state agencies, local education agencies, the University of North Carolina, community colleges, and some local governments. State law requires that health care benefits for retirees be consistent with benefits for full-time employees. The state legislature made many statutory changes in 2006 relating to vesting periods and benefit levels for new employees that will begin to mitigate future liabilities. There is no formal funding plan in place for OPEBs at this time. The state's moderate debt burden and well-funded pension system, however, would offset cost pressures relating to this liability.</p>

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies (cont.)

<p>North Dakota</p> <p>The state recently completed an actuarial valuation of the retiree health plans for the North Dakota public employees' retirement system in conjunction with required GASB 45 OPEB determinations. The state's total accrued liability as of 2006 was approximately \$82.8 million; the unfunded liability was assessed at \$51.9 million. This is considered a very manageable number for the state. There are a total of 29,000 participants in the program.</p>
<p>Ohio</p> <p>Ohio's pension plans fund retiree health insurance, and the state will be complying with GASB 43 in fiscal 2008. Ohio has assessed its OPEB liabilities regularly and has been one of the few states to begin to manage this liability and accumulate assets to fund the liability. For Ohio's Public Employees' Retirement System, the state's unfunded actuarial liability is \$18.7 billion; the state had accumulated assets of \$12.0 billion as of Dec. 31, 2006 (39.1% funded ratio). For the State Teachers' Retirement System plan, assets available for future retiree health care benefits are \$3.5 billion. This plan is funded on a pay-as-you-go basis. In 2005, the Ohio Police and Fire Pension had an unfunded actuarial accrued liability of \$2.99 billion (10.3% funded ratio). The Highway Patrol Retirement System had an unfunded actuarial accrued liability of \$185 million (34.1% funded ratio).</p>
<p>Oklahoma</p> <p>Oklahoma's pension funds support the state's OPEB obligations. The combined liability of pension and OPEB for all of the state's pension plans is greater than \$9 billion, significantly larger than the state's total tax-supported debt. The amount attributable to OPEB alone has not been quantified but represents a small portion of the total liability. OPEB benefits are limited to \$105 monthly for retirees who maintain their employer-provided health insurance.</p>
<p>Oregon</p> <p>The unfunded actuarial liability for the state's share of OPEB benefits for state employees is currently an estimated \$415 million.</p>
<p>Pennsylvania</p> <p>The commonwealth provides health care plans to its retirees and their qualifying dependents under two plans. The Retired Pennsylvania State Police Program offers collectively bargained benefits to retired state enlisted members and their dependents. The Retired Employee Health Program provides commonwealth-determined benefits to other retired state employees and their dependents. The commonwealth currently funds its OPEB benefits on a pay-as-you-go basis, totaling \$521 million in fiscal 2007. Commonwealth officials estimate the commonwealth's fiscal 2008 cost at \$600 million. Officials have established a restricted receipts account in order to accumulate funds to pay for retiree health care and from which the commonwealth could pay future OPEB costs. At fiscal year-end 2007, the commonwealth's ending combined fund balances for the two plans was \$288 million; it should increase to \$366 million by the end of fiscal 2008. The commonwealth plans to establish an irrevocable trust fund or equivalent arrangement before June 30, 2008. Pennsylvania's unfunded actuarial accrued liability decreased to \$9.388 billion from the \$13.8 billion previously reported. The commonwealth's estimated ARC for fiscal 2008 was reduced to \$772 million from \$1.125 billion. While these updated figures are still preliminary and subject to material change, they represent changes made under recently completed bargaining unit agreements, as well as revisions to the medical and prescription drug plans.</p>
<p>Rhode Island</p> <p>The state has updated its OPEB study, which now estimates an unfunded OPEB liability of \$479.8 million as of June 30, 2005. The largest portions of this unfunded liability are due to state employees (\$427.3 million) and state police (\$32.2 million). This estimate was calculated using an estimated investment rate of return of 8.25%. The actuarial analysis also calculated unfunded OPEB liability estimates using alternative rates of return. The assumption of a 7% rate of return resulted in an unfunded liability estimate of \$549.7 million; an assumed 5% rate of return resulted in an unfunded liability estimate of \$696.2 million. Although officials had considered beginning the amortization of the unfunded OPEB liability in the fiscal 2008 budget, the enacted 2008 budget only provides funding for pay-as-you-go OPEB costs.</p>
<p>South Carolina</p> <p>South Carolina provides and administers OPEB benefits through the state's Employee Insurance Program on a pay-as-you-go basis. The state provides funded health insurance to retirees of state agencies and public school districts meeting specified requirements, which generally are 10 years of qualified service for 100% of benefits equal to active employees. The state engaged an actuary in 2006 to study its liability and to comply with GASB 45 reporting requirements. The state's benefits are presently unfunded and there is no separate trust fund for OPEB. If the state does not set up a separate trust fund, its unfunded liability is \$10 billion with a net OPEB obligation of \$536 million in fiscal 2007, or a potential impact of \$418 million on the general fund. However, if the state sets up a trust fund, the funding assumptions change and the total liability would decrease to a still significant, but more manageable \$6.5 billion, with a potential impact on the general fund of \$240 million. The 2008 Appropriation Act included funding for the OPEB trust fund with \$47.4 million in recurring funds from the general fund and \$16 million in nonrecurring funds. The state has not yet set up the trust fund as it is working through the legal ramifications of the irrevocable trust; under South Carolina law, the funding of the trust ties back to a specific formula, which would limit the state's ability to manage funding of the trust in a down year. The state is also exploring changes to the benefit structure for new employees so that employees would receive 50% of the benefits after 12.5 years of service and 100% after 25 years.</p>
<p>South Dakota</p> <p>South Dakota allows eligible pre-Medicare retirees to buy into the active employees' health care plans with an implicit contribution from the state. According to a 2006 preliminary actuarial report, the state's unfunded actuarial accrued liability was \$87.16 million for fiscal 2007. The ARC for 2007 was \$11.18 million, which was substantially higher than the state's \$3.82 million current pay-as-you-go contribution. All numbers are based on a 3% discount rate.</p>

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies (cont.)

<p>Tennessee</p> <p>The state has also completed its OPEB actuarial, which has identified a preliminary liability of \$3.2 billion, including the teachers' and state employees' funds. Officials are likely to use pay-as-you-go financing to fund the ARC in the short term while the state performs additional actuarial analysis. The state has authorized the creation of trust funds in order to accumulate assets for OPEB under the Other Post Employment Benefit Investment Trust Act of 2006 (Chapter 771 of the Public Acts of 2006).</p>
<p>Texas</p> <p>Texas has elected not to adopt GASB 45 based on recently approved state legislation. The state does contribute to retiree health care and determines its contribution as part of the budget process. It has not entered into any collective bargaining agreements which impose postemployment healthcare benefits. Standard & Poor's will continue to request information regarding the state's OPEB obligations, number of eligible retirees, and annual cost. This information will be used to evaluate the effect that these obligations may have on the state's ability to meet its debt service obligations.</p>
<p>Utah</p> <p>Utah recently established through an actuarial study that its actuarial accrued liability as of 2004 was \$487.8 million. The 2005 legislature reduced this liability by eliminating and capping certain benefits and funding the state's full ARC of \$46.8 million in fiscals 2007 and 2008. This ARC payment is greater than the cash amount paid out for benefit costs in those years, which is \$21 million-\$22 million. The state will deposit the difference in a newly created irrevocable trust fund to pay for OPEB benefits. The state does not intend to issue bonds to fund either its pension or OPEB liabilities.</p>
<p>Vermont</p> <p>The state's third annual other postretirement employment benefits (OPEB) liability for both the state employees' and teachers' systems has recently been estimated at approximately \$1.4 billion (assuming no prefunding) or roughly \$2,500 per capita. Like most states, Vermont currently funds such benefits with pay-as-you-go financing rather than prefunding these benefits in the same manner as a traditional pension. Assuming no prefunding, the employee system's OPEB liability was estimated at \$604.4 million as of June 30, 2007. To fully amortize that amount over 30 years would require officials to make a \$47 million annual required contribution in fiscal 2008, which is significantly higher than the current fiscal 2008 contribution of \$16 million. The ARC under this scenario would increase to \$198 million in fiscal 2037. The liability for the teachers' system OPEB costs is higher: Assuming no prefunding, the accrued OPEB liability was \$820.2 million; this would require a \$60.2 million annual contribution in fiscal 2008, almost four times the system's current OPEB expenditure. Under the prefunding scenario, the unfunded actuarial liability for both systems is lower at \$690.4 million. Vermont officials have yet to make a decision on when or how they will fund the full annual required contribution. However, management has already taken several steps, including establishing an irrevocable trust in fiscal 2007 in which the state treasurer will manage OPEB specific assets. The treasurer hired an independent expert to review pension and retiree health plan design.</p>
<p>Virginia</p> <p>The commonwealth estimates its OPEB liability under GASB 45 at \$2.3 billion with an ARC of \$324.4 million. Funding scenarios are currently being evaluated. Two of the state's five OPEB plans are funding the ARC.</p>
<p>Washington</p> <p>In its intention to comply with GASB 43 and 45 reporting requirements (for fiscal 2008) relating to OPEB, Washington recently completed its actuarial valuation study. This report indicates the state has a liability of \$7.495 billion, which it funds on a pay-as-you-go basis. This approach to funding the state's liability results in annual costs of \$138 million, of which \$51 million is in the form of an implicit rate subsidy (allowing retirees to purchase health insurance coverage in the same pool as current employees) and is therefore not easily delineated cash outlays. The explicit benefit subsidizes retired members' monthly premiums for enrollment in Medicare parts A and B. If the state funded the ARC (thereby paying for the benefit on an actuarial basis), the annual cost would increase to \$635 million. While this approach would dampen the annual growth of the actuarial accrued liability, it would also formalize the benefit liability; the nature of the state's obligation to provide this benefit is currently ambiguous.</p>
<p>West Virginia</p> <p>West Virginia's OPEB plan is a cost-sharing multiple employer plan that covers state government and its agencies, state-related colleges and universities, county boards of education, county and municipal governments, and other employers allowed under statute. The Public Employees' Insurance Agency (PEIA) funds retiree health benefits. West Virginia completed an initial actuarial valuation in 2006 and updated it in fiscal 2007. The baseline unfunded actuarial accrued liability is an estimated \$7.8 billion, using a 4.5% investment rate assumption. For fiscal 2008, the pay-as-you-go cost to fund benefits is \$133 million while the ARC is \$824 million. In fiscal 2007, PEIA accepted a bid from Coventry Health Care to implement its Advantra Freedom plan for Medicare eligible retirees. This is a Medicare Advantage Prescription Drug plan licensed by the federal government through the Centers for Medicare and Medicaid Services. This shift, along with increased retiree co-pays, should substantially reduce the total unfunded liability and ARC. Assuming the conversion occurs, the actuary reports that the state's liability would be a lower \$3.4 billion with a pay-as-you-go cost of \$60 million and an ARC of \$398 million. These liabilities include all covered employees and retirees and do not represent the amounts due directly from the state's general fund. The West Virginia legislature created the West Virginia Retiree Health Benefits Trust Fund in 2006, which PEIA will administer. The balance in the trust fund is an estimated \$104 million, with an additional appropriation expected for fiscal 2008.</p>
<p>Wisconsin</p> <p>Wisconsin does not fund retiree health care, but allows retirees to participate in the state health care plan. An actuarial study is underway to determine the liability associated with the implicit rate subsidy. Retirees may use unused sick leave benefits to fund the cost of health care; the state has fully funded this sick leave conversion benefit.</p>

Table 1

U.S. States' OPEB Liability Assessments And Funding Strategies (cont.)

Wyoming

The state has not completed an actuarial valuation of its OPEB liabilities.

Table 2

State OPEB Liabilities

State	Rating	OPEB Liability (\$ Mil.)	Analyst
Alabama	AA	17,800	Sussan Corson
Alaska	AA	Reported with pension	Ian Carroll
Arizona	AA (ICR)	1,100-1,200	Sussan Corson
Arkansas	AA	3,000	Paul Jasin
California	A+	47,900	Dave Hitchcock
Colorado	AA (ICR)	Reported with pension	Rob Williams
Connecticut	AA	12,700-23,900	Karl Jacob
Delaware	AAA	4,000	Eden Perry
Florida	AAA	2,100-3,600	Robin Prunty
Georgia	AAA	19,180	John Sugden
Hawaii	AA	7,200-12,500	Rob Williams
Idaho	AA (ICR)	286-409	Rob Williams
Illinois	AA	N.A.	John Kenward
Indiana	AA+ (ICR)	N.A.	Eden Perry
Iowa	AA+ (ICR)	220	John Kenward
Kansas	AA+ (ICR)	N.A.	James Breeding
Kentucky	AA- (ICR)	12,300	Helen Samuelson
Louisiana	A	N.A.	Peter Murphy
Maine	AA	3,200-4,760	Colin MacNaught
Maryland	AAA	9,000-14,500	Richard Marino
Massachusetts	AA	7,600-13,300	Karl Jacob
Michigan	AA-	7,360	James Wiemken
Minnesota	AAA	659	Jane Ridley
Mississippi	AA	N.A.	Paul Jasin
Missouri	AAA	1,267-2,186	Peter Block
Montana	AA	306	Ian Carroll
Nebraska	AA+ (ICR)	N.A.	Peter Block
Nevada	AA+	1,620-4,100	Ian Carroll
New Hampshire	AA	1,500-2,900	Colin MacNaught
New Jersey	AA	58,100	Richard Marino
New Mexico	AA+	4,100	Sussan Corson
New York	AA	47,000	Colleen Woodell
North Carolina	AAA	23,900	Eden Perry
North Dakota	AA (ICR)	52	Jane Ridley
Ohio	AA+	21,700	Robin Prunty
Oklahoma	AA	Reported with pension	James Breeding

Table 2

State OPEB Liabilities(cont.)			
Oregon	AA	415	Rob Williams
Pennsylvania	AA	9,388	John Sugden
Rhode Island	AA	480-696	Richard Marino
South Carolina	AA+	10,000	Eden Perry
South Dakota	AA (ICR)	87	John Kenward
Tennessee	AA+	3,200	Ted Chapman
Texas	AA	N.A.	Horacio Aldrete
Utah	AAA	488	Gabe Petek
Vermont	AA+	690-1,400	Colin MacNaught
Virginia	AAA	2,300	Karl Jacob
Washington	AA	7,495	Gabe Petek
West Virginia	AA-	7,761	John Sugden
Wisconsin	AA-	N.A.	Peter Block
Wyoming	AA (ICR)	N.A.	Paul Jasin
Total Liabilities		357,476-394,210	
Median Liability		3,200-4,100	
Average Liability		9,166-10,108	

N.A. - Not available.

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