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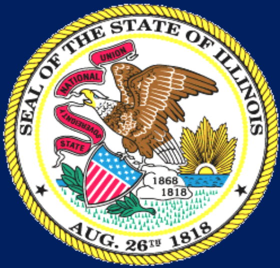

2023 Annual Review

Information Submitted by the Chicago Transit Authority's Retiree Health Care Trust

December 21, 2023

Frank J. Mautino
Auditor General

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OFFICE OF THE AUDITOR GENERAL
FRANK J. MAUTINO

To the Legislative Audit Commission, the Speaker and Minority Leader of the House of Representatives, the President and Minority Leader of the Senate, the members of the General Assembly, and the Governor:

This is our 2023 Annual Review of Information Submitted by the Chicago Transit Authority Retiree Health Care Trust.

The review was conducted pursuant to Public Act 95-708 which amended the Illinois State Auditing Act by adding a requirement for the Auditor General to annually review and report on information submitted by the Board of Trustees of the Chicago Transit Authority Retiree Health Care Trust.

The report for this review is transmitted in conformance with Section 5/22-101B(b)(3)(iv) of the Illinois Pension Code.

SIGNED ORIGINAL ON FILE

FRANK J. MAUTINO
Auditor General

Springfield, Illinois
December 2023

OFFICE OF THE AUDITOR GENERAL

December 21, 2023
Annual Review

Report Highlights

Frank J. Mautino *Auditor General*

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Annual Review of the

Information Submitted by the Chicago Transit Authority's Retiree Health Care Trust

Background:

The Illinois State Auditing Act (30 ILCS 5/3-2.3(f)) requires the Auditor General to annually examine the information on the funding level of the Retiree Health Care Trust (RHCT or Trust) submitted pursuant to Section 22-101B(b)(3)(iii) of the Illinois Pension Code.

If the Retiree Health Care Trust projects a funding shortfall, it **shall** provide a plan which may (1) increase contributions by employees, retirees, dependents, or survivors; (2) decrease benefits; (3) make other plan changes; or (4) any combination thereof to cure the shortfall within 10 years. If the Retiree Health Care Trust projects a surplus, it **may** decrease contributions, increase benefits, or make other plan changes, to the extent of the surplus.

Key Findings:

- The Retiree Health Care Trust submitted its Actuarial Valuation Report as of January 1, 2023 to the Office of the Auditor General on September 28, 2023.
- The Report concluded that the actuarial present value of projected contributions, trust income, and assets, in excess of the statutory reserve, exceeded the actuarial present value of the projected benefits. Consequently, **no change in benefits or contributions was required**.
- With the assistance of our consulting actuary, Aon, we examined the assumptions in the Retiree Health Care Trust's Actuarial Valuation Report and found that they were not unreasonable in the aggregate.

Key Recommendations:

- The investment return and inflation assumptions should continue to be monitored and justified on an annual basis.
- The latest mortality improvement scale should be considered for future valuations.

This Annual Review was conducted by OAG staff with the assistance of our consultant, Aon.

Report Digest

Statutory Requirements

The Illinois State Auditing Act (30 ILCS 5/3-2.3(f)) requires the Auditor General to annually examine the information on the funding level of the Retiree Health Care Trust (RHCT or Trust) submitted pursuant to Section 22-101B(b)(3)(iii) of the Illinois Pension Code. The Pension Code requires the Retiree Health Care Trust to prepare a report that meets the requirements delineated in the Code and to submit it to the Auditor General at least 90 days prior to the end of its fiscal year.

The Pension Code (Section 5/22-101B(b)(3)(iv)) provides the Auditor General 90 days to review the information submitted by the Retiree Health Care Trust. If the Retiree Health Care Trust projects a funding shortfall, it **shall** provide a plan which may (1) increase contributions by employees, retirees, dependents, or survivors; (2) decrease benefits; (3) make other plan changes; or (4) any combination thereof to cure the shortfall within 10 years. If the Retiree Health Care Trust projects a surplus, it **may** decrease contributions, increase benefits, or make other plan changes, to the extent of the surplus.

If the Auditor General's review determines the Retiree Health Care Trust's assumptions are *not unreasonable in the aggregate*, the Trust shall implement the plan. Otherwise, the Auditor General shall explain the basis for its determination to the Retiree Health Care Trust and may recommend an alternative plan.

The scope of the Auditor General's review, established by the Pension Code, focused on whether the actuarial assumptions used in the Trust's Actuarial Valuation were not unreasonable in the aggregate.

Report Determination

The Board of Trustees of the Chicago Transit Authority Retiree Health Care Trust submitted its Actuarial Valuation as of January 1, 2023 to the Office of the Auditor General on September 28, 2023. The Actuarial Valuation included information required by the Pension Code. As shown in Digest Exhibit 1, the Actuarial Valuation concluded that the actuarial present value of projected contributions and trust income plus assets in excess of the statutory reserve exceeded the actuarial present value of the projected benefits:

- The net actuarial present value of projected benefits was $647,253,375.
- The actuarial present value of projected active contributions, trust income, and assets was $952,127,127 (after subtracting $30,119,751 for the required statutory reserve).
- Consequently, projected income and assets exceeded projected benefits by 47.1 percent and, as such, no reduction in benefits or increase in contributions was necessary.

Digest Exhibit 1
RETIREE HEALTH CARE TRUST ANNUAL ASSESSMENT
January 1, 2023 RHCT Actuarial Valuation Report

Actuarial Present Value of Projected Benefits		**Actuarial Present Value of Projected Income and Assets**	
Actuarial present value of projected benefits prior to reduction of retiree contributions	$919,826,542	Actuarial present value of projected contributions and trust income plus assets	$982,246,878
Less: Projected current and future retiree contributions	($272,573,167)	Less: Statutory Reserve[1]	($30,119,751)[1]
Net actuarial present value of projected benefits	$647,253,375	Actuarial present value of projected contributions and trust income plus assets (net of statutory reserve)	$952,127,127

Projected income and assets exceed projected benefits by 47.1%

[1]The Statutory Reserve is net of retiree contributions.

Source: Retiree Health Care Trust Actuarial Valuation report as of January 1, 2023.

With the assistance of our consulting actuary, Aon, we examined the assumptions in the Trust's Actuarial Valuation. Overall, Aon found that the assumptions are not unreasonable in the aggregate. Aon did note that **the investment return and inflation assumptions should continue to be monitored and justified on an annual basis**. Additionally, Aon suggested the latest mortality improvement scale be considered for future valuations.

Pages 5 through 12 of our 2023 Annual Review contain observations on the specific assumptions used in the Actuarial Valuation.

Agency Review

A draft of this Review was provided to the Retirement Plan for their review.

This report does not constitute an audit as that term is defined in generally accepted government auditing standards.

This Annual Review was conducted by OAG staff with the assistance of our consultant, Aon.

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JOE BUTCHER
Division Director

This report is transmitted in accordance with Sections 3-14 of the Illinois State Auditing Act.

SIGNED ORIGINAL ON FILE

FRANK J. MAUTINO
Auditor General

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Introduction

The Board of Trustees of the Chicago Transit Authority (CTA) Retiree Health Care Trust (RHCT or Trust) is required by the Illinois Pension Code to submit a report to the Office of the Auditor General each year. The report is intended to annually assess the funding level of the Retiree Health Care Trust.

Statutory Requirements

The Illinois State Auditing Act (30 ILCS 5/3-2.3(f)) requires the Auditor General to annually examine the information on the funding level of the Retiree Health Care Trust submitted pursuant to Section 22-101B(b)(3)(iii) of the Illinois Pension Code. The Pension Code requires the Retiree Health Care Trust to prepare a report that meets the requirements delineated in the Code (see Exhibit 1) and to submit it to the Auditor General at least 90 days prior to the end of its fiscal year.

The Pension Code (Section 5/22-101B(b)(3)(iv)) provides the Auditor General 90 days to review the information submitted by the Retiree Health Care Trust. If the Retiree Health Care Trust projects a funding shortfall, it **shall** provide a plan which may (1) increase contributions by employees, retirees, dependents, or survivors; (2) decrease benefits; (3) make other plan changes; or (4) any combination thereof to cure the shortfall within 10 years. If the Retiree Health Care Trust projects a surplus, it **may** decrease contributions, increase benefits, or make other plan changes, to the extent of the surplus.

Exhibit 1
ILLINOIS PENSION CODE REQUIREMENTS

(iii) The Board of Trustees shall make an annual assessment of the funding levels of the Retiree Health Care Trust and shall submit a report to the Auditor General at least 90 days prior to the end of the fiscal year. The report shall provide the following:

(A) the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors;

(B) the actuarial present value of projected contributions and trust income plus assets;

(C) the reserve required by subsection (b)(3)(ii); and

(D) an assessment of whether the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors exceeds or is less than the actuarial present value of projected contributions and trust income plus assets in excess of the reserve required by subsection (b)(3)(ii).

Source: 40 ILCS 5/22-101B(b)(3)(iii).

If the Auditor General's review determines the Retiree Health Care Trust's assumptions are *not unreasonable in the aggregate*, the Trust shall implement the plan. Otherwise, the Auditor General shall explain the basis for its determination to the Retiree Health Care Trust and may recommend an alternative plan.

Report Determination

The Board of Trustees of the Chicago Transit Authority Retiree Health Care Trust submitted its Actuarial Valuation as of January 1, 2023 to the Office of the Auditor General on September 28, 2023. The Actuarial Valuation included information required by the Pension Code. As shown in Exhibit 2, the Actuarial Valuation concluded that the actuarial present value of projected contributions and trust income plus assets in excess of the statutory reserve exceeded the actuarial present value of the projected benefits:

- The net actuarial present value of projected benefits was $647,253,375.
- The actuarial present value of projected active contributions, trust income, and assets was $952,127,127 (after subtracting $30,119,751 for the required statutory reserve).
- Consequently, projected income and assets exceeded projected benefits by 47.1 percent and, as such, no reduction in benefits or increase in contributions was necessary.

Exhibit 2
RETIREE HEALTH CARE TRUST ANNUAL ASSESSMENT
January 1, 2023 RHCT Actuarial Valuation Report

Actuarial Present Value of Projected Benefits		**Actuarial Present Value of Projected Income and Assets**	
Actuarial present value of projected benefits prior to reduction of retiree contributions	$919,826,542	Actuarial present value of projected contributions and trust income plus assets	$982,246,878
Less: Projected current and future retiree contributions	($272,573,167)	Less: Statutory Reserve[1]	($30,119,751)[1]
Net actuarial present value of projected benefits	$647,253,375	Actuarial present value of projected contributions and trust income plus assets (net of statutory reserve)	$952,127,127

Projected income and assets exceed projected benefits by 47.1%

[1]The Statutory Reserve is net of retiree contributions.

Source: Retiree Health Care Trust Actuarial Valuation report as of January 1, 2023.

With the assistance of our consulting actuary, Aon, we examined the Retiree Health Care Trust's Actuarial Valuation and concluded that:

- The Board of Trustees of the Retiree Health Care Trust has made an assessment of the funding levels of the Retiree Health Care Trust which concluded that the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and their survivors are less than the actuarial present value of projected contributions and Trust

income plus assets in excess of the reserve required by Section 22-101B(b)(3)(ii) of the Illinois Pension Code, and

- The assumptions stated in the Actuarial Valuation submitted pursuant to Section 22-101B(b)(3)(iii) of the Pension Code are not unreasonable in the aggregate.

Calculation of the Statutory Reserve

The Pension Code requires the Retiree Health Care Trust to establish *"an appropriate funding reserve level which* ***shall not be less than the amount of incurred and unreported claims plus 12 months of expected claims and administrative expenses.****"* (40 ILCS 5/22-101B(b)(3)(ii)) [emphasis added] The Actuarial Valuation submitted by the Trust contains a calculation of the statutory reserve. The calculation includes $41.9 million for *"12 months of expected claims and administrative expenses,"* and $0.9 million for *"incurred and unreported claims,"* for a claims expense total of $42.8 million. It also subtracts $12.7 million from the claims expense for *"12 months of expected retiree and dependent contributions."* The netting or subtraction of expected contributions from the expected claims and administrative expenses is not specifically delineated in the Pension Code.

The statutory reserve is one of the figures used in the annual assessment of the Trust funding level required by Section 22-101B(b)(3)(iii) of the Pension Code. A change in the statutory reserve figure, therefore, would impact the calculation as to whether the Trust is adequately funded. As shown in Exhibit 2, when the statutory reserve is calculated by netting expected retiree contributions from expected claims (benefit payments), the actuarial present value of projected income and assets exceeds the actuarial present value of projected benefits by 47.1 percent. When expected claims are not reduced by expected retiree contributions, the statutory reserve increases from $30.1 million to $42.8 million. However, even increasing the statutory reserve to $42.8 million, the actuarial present value of projected income and assets of $939.4 million still exceeds the actuarial present value of projected benefits of $647.3 million by 45.1 percent.

As part of our 2009 Annual Review, we inquired of Trust officials why the statutory reserve was calculated by netting out expected retiree contributions. The Trust's actuary responded that they interpreted *"12 months of expected claims and administrative expenses"* to mean 12 months of **net** expenses. They noted that their understanding is that "contributions" means active contributions and "benefits" or "claims" to be net of retiree and dependent self-pay contributions. The actuary stated they used this interpretation for the initial January 1, 2008 Actuarial Valuation under Section 3-2.3(a)(7) of the Auditing Act as well as the January 1, 2009 Actuarial Valuation under Section 22-101B(b)(3) of the Pension Code. Our consulting actuary, Aon, indicated that it is not unreasonable to subtract the contributions from the anticipated benefit payments when calculating a reserve because no benefits could be paid without corresponding contributions being received.

Actuarial Assumptions

Aon examined the Retiree Health Care Trust's assumptions as disclosed in the January 1, 2023 Actuarial Valuation. Aon found that the assumptions stated in the report are not unreasonable in the aggregate. Aon did note that **the investment return and inflation assumptions should continue to be monitored and justified on an annual basis**. Additionally, Aon suggested the latest mortality improvement scale be considered for future valuations. Aon had the following observations regarding specific assumptions:

(A) **Net Investment Return.** The net investment return assumption for the plan is 6.85 percent. This assumption is unchanged from the previous valuation. In February 2023, the Trust's investment consultant prepared an analysis based on the asset allocation and found an expected ten-year return of 7.44 percent and 25th to 75th percentile range of investment returns of 9.50 percent to 5.60 percent respectively. This expected return assumes a dynamic inflation that varies across the different projected environments. The average inflation across these projected environments is 2.50 percent. The expected return assumes no alpha.

Aon calculated the investment return that could be expected based on the target asset allocation. Aon reviewed the expected return based on the Aon Expected Return Model (as of the first quarter of 2023). Based on the target asset allocation and Aon's expected return assumptions by asset class, Aon would expect a weighted average investment return of 6.41 percent. However, Aon's Expected Return Model indicates that the median return over a thirty-year time horizon based on the target asset allocation is 7.08 percent. The weighted average investment return assumes that the asset classes are one hundred percent correlated, while the median and percentile returns take into account that the asset classes are not one hundred percent correlated. Therefore, Aon believes the median is a better representation of the true expected return. Further, Aon finds that the 35th to 65th percentile range of investment returns is 7.83 percent to 6.34 percent and that the probability of achieving a return of 6.85 percent or greater over a thirty-year time horizon is 54.7 percent.

The Trust's actuary provided some information in the current valuation report related to the development of the long-term rate of return. The report includes the target allocation and long-term expected real rate of return by asset class. From this information we were able to calculate a weighted average real rate of return equal to 5.20 percent. Adding the expected inflation rate of 2.40 percent to the average real rate of return then implies the Trust's actuary's analysis supports an average net expected rate of return equal to 7.60 percent under the current target allocation. It is not uncommon for different firms to have different outlooks with respect to capital market expectations which will give rise to variances in the expected return.

The trust's inflation assumption underlying the development of the expected return assumption is 2.40 percent, which is higher than the underlying

inflation assumption used in Aon's Expected Return Model (as of the first quarter of 2023) of 2.30 percent. This assumption is increased from the 2.30 percent inflation assumption used in the prior year and was reviewed by the Trust's actuary for reasonableness along with the investment return assumption.

Actuarial Standard of Practice No. 27 (ASOP No. 27) provides guidance on the selection of economic assumptions for measuring pension obligations and is referenced as part of Actuarial Standard of Practice No. 6, Measuring Retiree Group Benefit Obligations (ASOP No. 6). ASOP No. 27 was revised and effective for plans with a measurement date on or after September 30, 2014. ASOP No. 27 states that each economic assumption should be reasonable and have no significant bias, but also recognizes that a range of reasonable assumptions may develop across actuarial practice. Further, the ASOP also states that it should not be assumed that superior returns will be achieved from an active investment management strategy (alpha) compared to a passive investment management strategy unless the actuary believes, based on relevant supporting data, that such superior or inferior returns represent a reasonable expectation over the measurement period.

Aon believes the 6.85 percent net investment return assumption is within the reasonable range despite being on the slightly lower end of the reasonable range based on the investment return analysis conducted by the Trust's actuary and investment consultant. We believe that the Trust's actuary and the Trust's investment consultant should continue performing separate analyses to support this assumption on an annual basis.

Aon reviewed the investment return assumption based on the target asset allocation. To the extent there is significant deviation from the target allocation or a lack of rebalancing to the target allocation, the 6.85 percent investment return assumption may not be reasonable.

The discount rate assumption used to measure the OPEB (other post-employment benefits) liability is equal to the long-term investment return assumption. In determining the discount rate, it was assumed active members continue to contribute 1.00 percent of payroll.

(B) **Inflation and Salary Increase.** The salary inflation and salary increase assumptions are consistent with the Retirement Plan assumptions. The underlying salary inflation assumption of 3.10 percent was last reviewed as part of the 2019 Retirement Plan experience study performed by the Plan's actuary. This assumption is higher than Aon's long-term inflation expectation of 2.30 percent and the Trust's general inflation for purposes of investment return of 2.40 percent. Aon finds this approach is not unreasonable due to multi-year negotiated salary contracts not being "subject to short-term changes in inflation rates."

Similar to the Retirement Plan, pay projections utilized 2022 earnings adjusted for the lump-sum payment. Similar one-time payments are not

expected in the future, so we believe this adjustment is reasonable for the 2023 valuation.

(C) **Disability and Withdrawal Rates.** Disability rates and withdrawal rates for full-time permanent employees match those of the Retirement Plan. Withdrawal rates for non-full-time permanent employees are assumed to be 15 percent. These assumptions were analyzed in the 2019 Retirement Plan experience study performed by the Plan's actuary, which examined five years of plan history from January 1, 2013 through December 31, 2017. These rates are unchanged from the prior year and Aon finds that the assumptions utilized are not unreasonable based on the information available/provided in the actuarial report and the 2019 experience study conducted by the Trust's actuary.

(D) **Mortality.** Pre-retirement and post-retirement mortality rates follow the Society of Actuaries (SOA) Public 2010 General Healthy Retiree Headcount-Weighted Below-Median mortality tables increased by 113 percent for females, fully generational using Scale MP-2018. Mortality rates for disabled employees are set at the SOA Public 2010 Non-Safety Disabled Retiree Headcount-Weighted mortality tables, fully generational with Scale MP-2018.

These assumptions were last reviewed and updated as part of the 2019 Retirement Plan experience study. The selected headcount-weighted mortality table is inconsistent with the Retirement Plan mortality assumption. This is not unreasonable given the differences in the plan benefits. According to the Pub-2010 report: "Per ASOP 35, the actuary should select a mortality assumption that is appropriate for the purpose of the measurement. Therefore, it would not necessarily be inappropriate – or inconsistent – to use amount-weighted tables to measure pension obligations and the corresponding headcount-weighted tables to measure most postretirement medical obligations, even when the two covered populations are identical." This mortality assumption represents the most recently published mortality table from the SOA. Overall, the mortality table assumption appears to be reasonable.

Actuarial Standard of Practice No. 35 (ASOP No. 35) provides guidance with respect to mortality improvement before and after the measurement date. After the 2014 experience study, the plan adopted generational mortality tables to account for future mortality improvements. The 2019 experience study confirmed the continued use of generational mortality tables to account for future mortality improvements. The 2014 SOA report stated that it is not inappropriate for actuaries to consider one or more of the RP-2014 tables for public plan use. The SOA has since released seven updates to MP-2014, and has further indicated their intention to provide annual updates to their mortality model. In 2022 and 2023, the SOA did not release an update to the latest MP-2021 model due to the challenges of incorporating pandemic data without adjustments into the model.

The current assumption for mortality improvement in the valuation is the MP-2018 mortality improvement scale, which reflects mortality data through 2016. This differs from the MP-2019 mortality improvement scale utilized by the Retirement Plan. More recent mortality improvement scale releases from the SOA reflect additional years of mortality data that result in slightly lower (MP-2019 and MP-2020) or slightly higher (MP-2021) mortality improvement rates relative to the preceding scale. We believe the MP-2018 mortality improvement scale could fall within the ASOP No. 35 reasonable assumption universe; however, we suggest the latest mortality improvement scale be considered for future valuations.

The mortality assumption has not been adjusted to incorporate the impact of the COVID-19 pandemic on anticipated future mortality experience. The CTA confirmed "no noticeable short-term impacts on mortality has been observed" or assumed in the long-term. We believe this is a reasonable approach based on the Retirement Plans Experience Committee of the Society of Actuaries Research Institute (RPEC) 2022 Mortality Improvement Update which states "the "MP" improvement scales are intended for use in valuing liabilities where it is assumed that past experience is already reflected in the participant or member data at the measurement date. There does not appear to be consensus within the actuarial community on the extent of the near and long-term future impacts, direct or indirect, of the pandemic on pensioner mortality." Additionally, the RPEC 2023 Mortality Improvement Update states "based on CDC information, [the data] indicates lower excess mortality in 2022 compared to 2020 and 2021 and further declining excess mortality in 2023, with no excess mortality in total for ages 65 and older." This is further supported by the SSA assuming "very little future mortality impact from COVID-19" and UK Insurers "generally assuming no COVID impact."

Aon did not otherwise perform an independent analysis of mortality improvement.

(E) **Active Retirement Rates.** Active retirement rates match those of the Retirement Plan. This assumption was last analyzed in the 2019 Retirement Plan experience study which Aon reviewed. Aon finds that this assumption is not unreasonable based on the information available/provided in the actuarial report and the 2019 experience study conducted by the Trust's actuary.

(F) **Retirement Age.** Selecting age 65 as the expected retirement age for inactive participants is not unreasonable.

(G) **Participation Rates for Retirees.** The participation assumption for future retirees is based on service at retirement. The assumed participation rates decrease as retiree contributions increase. The methodology for setting the participation rates is that the percent assumed to decline coverage is assumed to be 100 percent of the percent of full cost paid by retirees. This methodology is unchanged from the prior valuation. Participation rates for

the pre-Medicare retirees had minimal changes, reflecting the minor changes in per capita health costs. Participation rates for the MAPD (Medicare Advantage Prescription Drug) retirees decreased significantly due to a decline in the employer subsidy (retiree rates remained the same despite decreases in total cost). These changes are not unreasonable based on the changes in the per capita health cost.

Aon finds that the retiree participation assumption is not unreasonable.

(H) **Participation Rates for Dependents.** The participation assumption for dependents is based on retiree service at retirement. The assumed participation rates decrease as dependent contributions increase. The methodology for setting the dependent participation rates is that the percent assumed to decline coverage is assumed to be 100 percent of the percent of full cost paid by dependents and is unchanged from the prior valuation. Participation rates for MAPD dependents decreased significantly due to a decline in the employer subsidy. Aon finds that the dependent participation assumption is not unreasonable.

(I) **Married Assumption.** The percent married assumption of 75 percent for future retirees and a 3-year age difference is consistent with commonly used values and not unreasonable based on the information available/provided in the actuarial report and the 2019 experience study conducted by the Trust's actuary.

(J) **Plan Election.** The plan election assumption for future retirees pre-Medicare assumes 85 percent elect PPO (Preferred Provider Organization) coverage and 15 percent elect HMO (Health Maintenance Organization) coverage and assumes 95 percent of Medicare retirees elect PPO coverage and the remaining 5 percent elect HMO coverage. This assumption is unchanged from the prior valuation and is not unreasonable based on the information available/provided in the actuarial report and the 2019 experience study conducted by the Trust's actuary.

(K) **Disabled Retirees Medicare Eligibility.** The percent of disabled participants eligible for Medicare varies based on number of years on disability. It is assumed that upon retirement 40 percent of pre-65 disabled retirees are eligible for Medicare, increasing to 70 percent eligible for Medicare two years after retirement. This assumption is unchanged from the prior valuation and Aon finds that it is not unreasonable based on the information available/provided in the actuarial report and the 2019 experience study conducted by the Trust's actuary.

(L) **Missing Participant Data.** The methodology for assigning values for missing participant data is not unreasonable. Aon notes that this is unchanged from the prior year.

(M) **Per Capita Claims.** The methodology used to calculate the pre-Medicare per capita claims for the self-insured PPO medical and prescription drug benefits utilizes three years of experience (7/1/2019 – 6/30/2022) adjusted for

plan design changes and health care trend. The new experience period used differed from the 2022 valuation due to reflecting the most current claims paid at the time of developing the 2023 full cost amounts. As a result of the change in experience period, an adjustment for COVID-19 related experience was determined to be appropriate for medical claim cost development. The Trust's actuary did not see a material difference in prescription drug costs due to COVID-19, so no adjustment was made in developing the prescription drug claim costs.

Per capita claims for the pre-Medicare self-insured HMO plan are based on two years of experience (3/1/2020 – 2/28/2022) adjusted for plan design changes and health care trend. Additionally, the weighted average claims were newly adjusted for estimated HMO discounts under the new provider. These are anticipated to continue into the future, so the adjustment is not unreasonable. The experience period used differed from the 2022 valuation due to reflecting the most current claims period at the time the plan went out to bid. The difference in claims between the 2020-2021 experience year and 2021-2022 experience year is minimal, so no adjustment factors are included for COVID-19.

Per capita claims for the Medicare Advantage plan are based on the premium rates for 2023.

Per capita health costs for pre-Medicare benefits decreased for the PPO medical plan and increased for the PPO prescription drug plan and the HMO as a result of updated actuarial factors based on the Trust's actuary's review of historical claims experience. The updated actuarial factors and resulting claims presented are not unreasonable.

Per capita health costs for MAPD benefits decreased significantly as a result of premium decreases from January 1, 2022 to January 1, 2023. These decreases varied by age as a result of updated actuarial factors based on the Trust's actuary's review of historical claims experience. The changes in per capita health costs are not unreasonable based on the MAPD premium decrease and updated actuarial factors.

Overall, the methodology and resulting claims presented are not unreasonable.

(N) **Actuarial Aging Factors.** Actuarial aging factors were applied to the weighted average cost to estimate individual retiree and spouse costs by age and by gender. These same factors were applied to each plan option, except that no age grading applies to Medicare retirees under age 65. This methodology is unchanged from the prior valuation. Aon finds that the actuarial aging factors assumption and application are not unreasonable.

(O) **Health Care Cost Trends.** The Trust valuation utilizes a unique healthcare cost trend curve for pre-Medicare and post-Medicare medical and prescription drug claims. The trend rates are developed annually based on various data sources and reflect a "similar level (of trend) to other types of

Medicare coverage". As a result, MAPD trend rates were not leveraged. Aon finds this assumption is not unreasonable.

The initial (first year) health care trend rates, the period of grading down to the ultimate trend, and the ultimate trend rates of 4.5 percent assumed for HMO and PPO are not unreasonable.

The initial (first year) health care trend rate for MAPD is 7.0 percent and grades down to the ultimate trend of 4.5 percent. Based on the agreement with Humana, the health care trend rate is not unreasonable. In addition, the grading down to the ultimate rate, and the ultimate trend rate of 4.5 percent assumed for MAPD is not unreasonable.

The increase in fees and administrative expenses included in the healthcare cost trend rates are assumed to be 3.0 percent, unchanged from last year. The projected increase in fees and administrative expense assumption is not unreasonable.

Overall, Aon finds that the retiree trend curve assumption is not unreasonable.

(P) **Retiree Contribution Increase Rate.** The application of the health care trend rate to the retiree and dependent contributions is a common practice and not unreasonable. Actual contribution increases in the future should be compared against this assumption to ensure that it continues to be reasonable.

(Q) **Administrative Expense.** The administrative expense per participant added to projected incurred claims for 2023 increased 1.1 percent (from $352 per participant to $356 per participant) from the 2022 assumption. The administrative expense was developed similarly as in the past. The last valuation used historical expenses from January 1, 2017 through December 31, 2020. This year's valuation used historical expenses from January 1, 2018 through December 31, 2021. Aon finds that the administrative expense assumption is not unreasonable.

(R) **Lifetime Maximum Benefits.** The assumption of no lifetime maximum benefits in the plan is not unreasonable, as past information was not available on accumulated benefits.

(S) **Health Care Reform.** As a retiree-only plan, most aspects of the Patient Protection and Affordable Care Act (PPACA) and the Health Care and Education Reconciliation Act (HCERA) of 2010 are assumed to not apply, and any future aspects are assumed to have a de minimis effect.

Aon finds that this assumption is not unreasonable. However, it is important to note that should future aspects be released, certain assumptions in this analysis may need to be revised.

(T) **COVID-19.** Adjustments were made as deemed appropriate to reflect the impacts of the COVID-19 pandemic for various assumptions based on recent experience and forward-looking expectations. Adjustments were made to PPO medical per capita claim cost developments, but were explicitly not

made for the PPO prescription drug and HMO per capita claims cost development nor for the mortality assumption.

Overall, Aon does not find the Retiree Health Care Trust's assumptions unreasonable in the aggregate.

Limitation on Retiree Contributions

The Pension Code (40 ILCS 5/22-101B(b)(5)) requires that the *"aggregate amount of retiree, dependent and survivor contributions to the cost of their health care benefits shall not exceed more than 45% of the total cost of such benefits."* The Pension Code goes on to define *"total cost of such benefits"* as the *"total amount expended by the retiree health benefit program in the prior plan year, as calculated and certified in writing by the Retiree Health Care Trust's enrolled actuary…."*

The January 1, 2023 Actuarial Valuation prepared by the Trust's actuary contained the results of the actuary's calculation of whether the 45 percent limitation established by the Pension Code was met. The Actuarial Valuation noted that according to the preliminary December 31, 2022 balance sheet of the Retiree Health Care Trust, the aggregate amount of retiree, dependent, and survivor **contributions** for 2022 was $11.8 million. The total cost of retiree health benefits paid from the Trust in 2021 was $42.6 million. The Actuarial Valuation calculated that the retirees paid 27.8 percent of the total cost of benefits, which did not exceed the statutory limit of 45 percent. The Actuarial Valuation notes that dental benefits and contributions are excluded from this calculation, since the Fund does not provide dental benefits, but only serves as a "pass-through" for dental premiums.

Scope of Annual Review

The Office of the Auditor General has conducted this annual review of information submitted by the Board of Trustees of the Chicago Transit Authority Retiree Health Care Trust pursuant to the Illinois State Auditing Act (30 ILCS 5/3-2.3(f)): *"The Auditor General shall annually examine the information submitted pursuant to Section 22-101B(b)(3)(iii) of the Illinois Pension Code and shall prepare the determination specified in Section 22-101B(b)(3)(iv) of the Illinois Pension Code."* The scope of the Auditor General's review is established by the Pension Code and focused on whether the actuarial assumptions used in the Retiree Health Care Trust's report were not unreasonable in the aggregate.

This report does not constitute an audit as that term is defined in generally accepted government auditing standards. Consequently, while we reviewed the information provided by the CTA Retiree Health Care Trust for reasonableness and consistency, we did not conduct an audit of the accuracy of the information provided as that is the responsibility of the Trust.

The scope of our work included reviewing the Retiree Health Care Trust's Actuarial Valuation as of January 1, 2023, submitted by the Trust on September 28, 2023. Our consulting actuary, Aon, followed-up with the Trust on various questions they had based upon their review of the Valuation. Aon reviewed the reasonableness of the actuarial assumptions used by the Trust in its January 1, 2023 Actuarial Valuation.

In prior years, we reported that the Plan's Executive Director noted that the Williams case (Williams v. Retirement Plan for CTA Employees, CTA Retiree Health Care Trust, et al., No. 11 CH 15446 (Circuit Court of Cook County, Illinois)) could have a significant impact on either the Retirement Plan or the Retiree Health Care Trust in the magnitude of $100 million or more. The plaintiffs were current and former employees of the CTA who argued that after years of fully paid health care benefits for retired CTA employees, they were being asked to pay for a portion of their health care benefits and were no longer entitled to the same level of health care coverage as active CTA employees. The changes to their coverage occurred as a result of an arbitration award and related amendments to the Pension Code made by Public Act 95-708. On October 23, 2023, the Executive Director provided an update on the status of the case which was settled that day.

> The Williams settlement is a one-time, lump sum payment, which has been incorporated into the actuarial assessment and financial statements. Class members will participate in the plan going forward, if they wish, on the same basis as other participants. The settlement was approved by the Court this morning (10/23/23). Class members have 30 days to appeal, but there were no objections during the settlement this morning.

The Retiree Health Care Trust was provided a draft of this report for review and comment.

Appendix A
Statutory Authority

Illinois State Auditing Act

30 ILCS 5/3-2.3(f)

(e) The Auditor General shall annually examine the information submitted pursuant to Section 22-101B(b)(3)(iii) of the Illinois Pension Code and shall prepare the determination specified in Section 22-101B(b)(3)(iv) of the Illinois Pension Code.

(Source: P.A. 95-708, eff. 1-18-08.)

Illinois Pension Code

40 ILCS 5/22-101B

Sec. 22-101B. Health Care Benefits.

(a) The Chicago Transit Authority (hereinafter referred to in this Section as the "Authority") shall take all actions lawfully available to it to separate the funding of health care benefits for retirees and their dependents and survivors from the funding for its retirement system. The Authority shall endeavor to achieve this separation as soon as possible, and in any event no later than July 1, 2009.

(b) Effective 90 days after the effective date of this amendatory Act of the 95th General Assembly, a Retiree Health Care Trust is established for the purpose of providing health care benefits to eligible retirees and their dependents and survivors in accordance with the terms and conditions set forth in this Section 22-101B. The Retiree Health Care Trust shall be solely responsible for providing health care benefits to eligible retirees and their dependents and survivors upon the exhaustion of the account established by the Retirement Plan for Chicago Transit Authority Employees pursuant to Section 401(h) of the Internal Revenue Code of 1986, but no earlier than January 1, 2009 and no later than July 1, 2009.

(1) The Board of Trustees shall consist of 7 members appointed as follows: (i) 3 trustees shall be appointed by the Chicago Transit Board; (ii) one trustee shall be appointed by an organization representing the highest number of Chicago Transit Authority participants; (iii) one trustee shall be appointed by an organization representing the second-highest number of Chicago Transit Authority participants; (iv) one trustee shall be appointed by the recognized coalition representatives of participants who are not represented by an organization with the highest or second-highest number of Chicago Transit Authority participants; and (v) one trustee shall be selected by the Regional Transportation Authority Board of Directors, and the trustee shall be a professional fiduciary who has experience in the area of collectively bargained retiree health plans. Trustees shall serve until a

successor has been appointed and qualified, or until resignation, death, incapacity, or disqualification.

Any person appointed as a trustee of the board shall qualify by taking an oath of office that he or she will diligently and honestly administer the affairs of the system, and will not knowingly violate or willfully permit the violation of any of the provisions of law applicable to the Plan, including Sections 1-109, 1-109.1, 1-109.2, 1-110, 1-111, 1-114, and 1-115 of Article 1 of the Illinois Pension Code.

Each trustee shall cast individual votes, and a majority vote shall be final and binding upon all interested parties, provided that the Board of Trustees may require a supermajority vote with respect to the investment of the assets of the Retiree Health Care Trust, and may set forth that requirement in the trust agreement or by-laws of the Board of Trustees. Each trustee shall have the rights, privileges, authority and obligations as are usual and customary for such fiduciaries.

(2) The Board of Trustees shall establish and administer a health care benefit program for eligible retirees and their dependents and survivors. Any health care benefit program established by the Board of Trustees for eligible retirees and their dependents and survivors effective on or after July 1, 2009 shall not contain any plan which provides for more than 90% coverage for in-network services or 70% coverage for out-of-network services after any deductible has been paid, except that coverage through a health maintenance organization ("HMO") may be provided at 100%.

(2.5) The Board of Trustees may also establish and administer a health reimbursement arrangement for retirees and for former employees of the Authority or the Retirement Plan, and their survivors, who have contributed to the Retiree Health Care Trust but do not satisfy the years of service requirement of subdivision (b)(4) and the terms of the retiree health care plan; or for those who do satisfy the requirements of subdivision (b)(4) and the terms of the retiree health care plan but who decline coverage under the plan prior to retirement. Any such health reimbursement arrangement may provide that: the retirees or former employees of the Authority or the Retirement Plan, and their survivors, must have reached age 65 to be eligible to participate in the health reimbursement arrangement; contributions by the retirees or former employees of the Authority or the Retirement Plan to the Retiree Health Care Trust shall be considered assets of the Retiree Health Care Trust only; contributions shall not accrue interest for the benefit of the retiree or former employee of the Authority or the Retirement Plan or survivor; benefits shall be payable in accordance with the Internal Revenue Code of 1986; the amounts paid to or on account of the retiree or former employee of the Authority or the Retirement Plan or survivor shall not exceed the total amount which the retiree or former employee of the Authority or the Retirement Plan contributed to the Retiree Health Care Trust; the Retiree Health Care Trust may charge a reasonable administrative fee for

processing the benefits. The Board of Trustees of the Retiree Health Care Trust may establish such rules, limitations and requirements as the Board of Trustees deems appropriate.

(3) The Retiree Health Care Trust shall be administered by the Board of Trustees according to the following requirements:

(i) The Board of Trustees may cause amounts on deposit in the Retiree Health Care Trust to be invested in those investments that are permitted investments for the investment of moneys held under any one or more of the pension or retirement systems of the State, any unit of local government or school district, or any agency or instrumentality thereof. The Board, by a vote of at least two-thirds of the trustees, may transfer investment management to the Illinois State Board of Investment, which is hereby authorized to manage these investments when so requested by the Board of Trustees.

(ii) The Board of Trustees shall establish and maintain an appropriate funding reserve level which shall not be less than the amount of incurred and unreported claims plus 12 months of expected claims and administrative expenses.

(iii)The Board of Trustees shall make an annual assessment of the funding levels of the Retiree Health Care Trust and shall submit a report to the Auditor General at least 90 days prior to the end of the fiscal year. The report shall provide the following:

(A) the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors;

(B) the actuarial present value of projected contributions and trust income plus assets;

(C) the reserve required by subsection (b)(3)(ii); and

(D) an assessment of whether the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors exceeds or is less than the actuarial present value of projected contributions and trust income plus assets in excess of the reserve required by subsection (b)(3)(ii).

If the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors exceeds the actuarial present value of projected contributions and trust income plus assets in excess of the reserve required by subsection (b)(3)(ii), then the report shall provide a plan, to be implemented over a period of not more than 10 years from each valuation date, which would make the actuarial present value of projected contributions and trust income plus assets equal to or exceed the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors. The plan may consist of increases in employee, retiree, dependent, or survivor contribution levels,

decreases in benefit levels, or other plan changes or any combination thereof. If the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors is less than the actuarial present value of projected contributions and trust income plus assets in excess of the reserve required by subsection (b)(3)(ii), then the report may provide a plan of decreases in employee, retiree, dependent, or survivor contribution levels, increases in benefit levels, or other plan changes, or any combination thereof, to the extent of the surplus.

(iv) The Auditor General shall review the report and plan provided in subsection (b)(3)(iii) and issue a determination within 90 days after receiving the report and plan, with a copy of such determination provided to the General Assembly and the Regional Transportation Authority, as follows:

(A) In the event of a projected shortfall, if the Auditor General determines that the assumptions stated in the report are not unreasonable in the aggregate and that the plan of increases in employee, retiree, dependent, or survivor contribution levels, decreases in benefit levels, or other plan changes, or any combination thereof, to be implemented over a period of not more than 10 years from each valuation date, is reasonably projected to make the actuarial present value of projected contributions and trust income plus assets equal to or in excess of the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors, then the Board of Trustees shall implement the plan. If the Auditor General determines that the assumptions stated in the report are unreasonable in the aggregate, or that the plan of increases in employee, retiree, dependent, or survivor contribution levels, decreases in benefit levels, or other plan changes to be implemented over a period of not more than 10 years from each valuation date, is not reasonably projected to make the actuarial present value of projected contributions and trust income plus assets equal to or in excess of the actuarial present value of projected benefits expected to be paid to current and future retirees and their dependents and survivors, then the Board of Trustees shall not implement the plan, the Auditor General shall explain the basis for such determination to the Board of Trustees, and the Auditor General may make recommendations as to an alternative report and plan.

(B) In the event of a projected surplus, if the Auditor General determines that the assumptions stated in the report are not unreasonable in the aggregate and that the plan of decreases in employee, retiree, dependent, or survivor contribution levels, increases in benefit levels, or both, is not unreasonable in the

aggregate, then the Board of Trustees shall implement the plan. If the Auditor General determines that the assumptions stated in the report are unreasonable in the aggregate, or that the plan of decreases in employee, retiree, dependent, or survivor contribution levels, increases in benefit levels, or both, is unreasonable in the aggregate, then the Board of Trustees shall not implement the plan, the Auditor General shall explain the basis for such determination to the Board of Trustees, and the Auditor General may make recommendations as to an alternative report and plan.

(C) The Board of Trustees shall submit an alternative report and plan within 45 days after receiving a rejection determination by the Auditor General. A determination by the Auditor General on any alternative report and plan submitted by the Board of Trustees shall be made within 90 days after receiving the alternative report and plan, and shall be accepted or rejected according to the requirements of this subsection (b)(3)(iv). The Board of Trustees shall continue to submit alternative reports and plans to the Auditor General, as necessary, until a favorable determination is made by the Auditor General.

(4) For any retiree who first retires effective on or after January 18, 2008, to be eligible for retiree health care benefits upon retirement, the retiree must be at least 55 years of age, retire with 10 or more years of continuous service and satisfy the preconditions established by Public Act 95-708 in addition to any rules or regulations promulgated by the Board of Trustees. Notwithstanding the foregoing, any retiree hired on or before September 5, 2001 who retires with 25 years or more of continuous service shall be eligible for retiree health care benefits upon retirement in accordance with any rules or regulations adopted by the Board of Trustees; provided he or she retires prior to the full execution of the successor collective bargaining agreement to the collective bargaining agreement that became effective January 1, 2007 between the Authority and the organizations representing the highest and second-highest number of Chicago Transit Authority participants. This paragraph (4) shall not apply to a disability allowance.

(5) Effective January 1, 2009, the aggregate amount of retiree, dependent and survivor contributions to the cost of their health care benefits shall not exceed more than 45% of the total cost of such benefits. The Board of Trustees shall have the discretion to provide different contribution levels for retirees, dependents and survivors based on their years of service, level of coverage or Medicare eligibility, provided that the total contribution from all retirees, dependents, and survivors shall be not more than 45% of the total cost of such benefits. The term "total cost of such benefits" for purposes of this subsection shall be the total amount expended by the retiree health benefit program in the prior plan year, as calculated and certified in writing by the Retiree Health Care Trust's enrolled actuary to be appointed and paid for by the Board of Trustees.

(6) Effective January 1, 2022, all employees of the Authority shall contribute to the Retiree Health Care Trust in an amount not less than 1% of compensation.

(7) No earlier than January 1, 2009 and no later than July 1, 2009 as the Retiree Health Care Trust becomes solely responsible for providing health care benefits to eligible retirees and their dependents and survivors in accordance with subsection (b) of this Section 22-101B, the Authority shall not have any obligation to provide health care to current or future retirees and their dependents or survivors. Employees, retirees, dependents, and survivors who are required to make contributions to the Retiree Health Care Trust shall make contributions at the level set by the Board of Trustees pursuant to the requirements of this Section 22-101B.

(Source: P.A. 102-415, eff. 1-1-22.)

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