



DEPARTMENT OF DEFENSE
MEDICARE-ELIGIBLE RETIREE HEALTH CARE BOARD OF ACTUARIES
4800 MARK CENTER DRIVE, SUITE 03E25
ALEXANDRIA, VA 22350

September 28, 2023

MEMORANDUM FOR THE RECORD

SUBJECT: Minutes of the July 28, 2023, Meeting of the DoD Medicare-Eligible Retiree Health Care Board of Actuaries

These are the minutes of the July 28, 2023, meeting of the DoD Medicare-Eligible Retiree Health Care Board of Actuaries (Board). The Board advises on the actuarial valuation of the Medicare-Eligible Retiree Health Care Fund (MERHCF or Fund).

List of Attachments:

- 1 – Meeting agenda
- 2 – List of attendees
- 3 – DoD Office of the Actuary handout
- 4 – Meeting transcript

We have reviewed and agree with the meeting minutes. Responsibility for the accuracy of each attachment resides with the organization creating it.

A handwritten signature in cursive script, reading "David H. Osterndorf".

David Osterndorf, Chairperson
DoD Medicare-Eligible Retiree
Health Care Board of Actuaries

A handwritten signature in cursive script, reading "Inger M. Pettygrove".

Inger M. Pettygrove
Designated Federal Officer

**MEDICARE-ELIGIBLE RETIREE HEALTH CARE
BOARD OF ACTUARIES
MEETING MINUTES**

**July 28, 2023
10:00 a.m.
*Virtual Meeting***

HIGHLIGHTS/KEY BOARD DECISIONS

Introduction:

- Transcript Pages 2-3: Chairperson David Osterndorf opened the 2023 Board Meeting. Mr. Osterndorf outlined several agenda items and the objectives for the meeting. He also expressed the Board's appreciation for efforts undertaken by the DoD Office of the Actuary (OACT) staff.

Agenda Item 2: September 30, 2021, Actuarial Valuation Results

- Transcript Pages 3-4: OACT presented the MERHCF valuation history and gains/losses to the Fund. MERHCF per capita normal costs for FY 2024 are \$6,405 and \$2,553 for active duty and reserve, respectively. The actuarial liability as of September 30, 2021, was \$519.2 billion and the unfunded liability was \$207.4 billion. The Treasury payment for October 1, 2022, was \$10 billion.
- Transcript Pages 4-5: In FY 2021, there was an experience gain of \$13.1 billion and an assumption loss of \$36.8 billion, leading to a total valuation loss of \$23.8 billion. In FY 2022, there was an experience gain of \$12.1 billion attributable to asset performance with returns in excess of the valuation assumption.

Agenda Item 3: September 30, 2022, Actuarial Valuation Proposals

- Transcript Pages 6-7: Effective fund yield and balance for each fiscal year from 2017 to 2022 were presented. In FY 2022, we had a beginning balance of \$312.1 billion and an ending balance of \$345.1 billion. The annual effective yield was 8.4%. It was noted that the fund has benefitted from the high inflation environment. The investment income was \$27.1 billion due to a majority of the Fund being invested in TIPS.
- Transcript Pages 7-8: Active service member counts for FYs 21-22 were presented, showing a decrease across the board compared to last year, mainly due to the services facing recruiting challenges. The decrease was somewhat offset by increased retention. This is the first year the Fund includes Public Health Service reserves, with a count of 64.

- Transcript Pages 8-9: Mr. Alden inquired if we should expect to have National Oceanic and Atmospheric Administration reserve members in the future, and it was confirmed. Mr. Osterndorf asked if there was a change in the average age of the population given that there is an increase in retention of existing service members. OACT confirmed that there is a slight increase in average age from 29.49 last year to 29.64 this year.
- Transcript Pages 10-12: Counts of retired beneficiaries and dependents were presented for FY21 and FY22. Across the categories, there was a slight increase in the number of Medicare-eligible beneficiaries. OACT presented the incurred outlays for FY21 and FY22. It was noted that there is a continuation of the prior trend post-COVID of spending moving from direct care to purchased care. OACT confirmed that there are no new entrants into the USFHP plan as it is a closed plan.
- Transcript Pages 12-13: OACT proposed no change to the discount rate assumption of 4.50%, and no change in the Ultimate Medical Trend of 4.75%. Similar to other boards such as Social Security, OPM, and CMS, OACT proposed to keep the assumptions the same. OACT confirmed that there has been a change in the investment policy: a smaller percentage of the Fund is invested in TIPS (60-70%, vs. 75-85%). The target average duration shifted from 20 to 15 years.
- Transcript Pages 14-21: Mr. Osterndorf expressed the Board's view that the investment policy should be very closely tied to a strong asset liability matching approach as well as setting an appropriate discount rate. Lt Col Keough from IAC provided background information on changes to investment policy as well as the reason for the changes to acquire more leverage to make broader decisions in investments.
- Transcript Pages 22-27: Lt Col Keough and Lt Col Pagoaga discussed the unusual yield curve in treasuries being a factor for modification in investment policy. The US Treasury yield curve was presented and it was noted that the upward shift of the inverted yield curve was the driving factor for investment recommendations. The IAC members confirmed that asset liability matching was a very important element of their deliberations in setting investment policy and expressed their willingness to be involved in the asset liability study requested by the Board.
- Transcript Pages 27-29: OACT presented the medical trend assumptions for direct care (DC), purchased care (PC), and USFHP. Proposed trends reflect the most recent experience with short-term expectations to return to pre-pandemic levels. OACT noted a continued shift to PC from DC along with a consideration for the emerging blockbuster drugs, such as Ozempic and Wegovy.
- Pages 29-31: Mr. Osterndorf commented how our experience showed a significant drop-off in terms of services due to the pandemic, and how the expectation to return

to normalcy is still a year or two away. He added that the care patterns for both pre- and post-Medicare are relatively consistent.

- Transcript Pages 31-34: OACT proposed the use of weights for 2021 and 2022 mortality experience period, an update to survivor long-term rate of improvement, and an update to spouse-per-sponsor rates using 2022 experience. It was noted that the Society of Actuaries did not publish a new projection scale in 2022.
- Transcript Pages 34-38: OACT proposed a reserve rate update to adjust projection of reserve retirees with an emphasis on gray area. Rates based on experience in FY17 and FY19 will be used to model individuals either age 63 or 41 years of service. There was a discussion regarding why individuals eligible for retirement with age 59 and 41 years of service were not retiring. OACT confirmed with advisors that members would need to apply for retirement to become eligible for health benefits. Since there is limited interaction with former service members who have not yet applied for retirement, there is insufficient information to understand the rationale behind the deferred retirement dates.
- Transcript Pages 38-39: OACT proposed a 10% increase in disability retirement rates to reflect the Promise to Address Comprehensive Toxics (PACT) Act. It was noted that the 10% increase is a moderate reflection of PACT Act and does not speculate on what services will do in the future in terms of members leaving service prior to the passage of the PACT Act who might ultimately be entitled to benefits even if they had not met standard retirement eligibility, due to the potential for retrospective review of any disability retirement entitlement.
- Transcript Page 39: OACT proposed assumptions related to administrative cost loads and decrement rates. The IP and OP admin load decreased from 2.00% to 1.50%, and the Retail Pharmacy admin load was unchanged.
- Transcript Pages 39-43: The average claims level was updated for FY2022 experience, and no changes were proposed for valuation claims cost age grading. Mr. Osterndorf stated concerns regarding the discrepancy between mortality improvement assumptions for MRF and MHS. He described the self-correcting phenomenon associated with greater improvement: members would be receiving benefits longer but would be receiving less benefits due to improving health conditions.
- Transcript Pages 43-44: The Board approved OACT's proposed methods and assumptions for calculating the FY 2025 per capita normal costs, the September 30, 2022, unfunded liability (UFL), and the October 1, 2023, Treasury UFL amortization and normal cost payments.
- Transcript Pages 44-48: OACT gave a brief presentation on the transition to ADVANA, a new method of accessing and storing data from the Defense

Manpower Data Center (DMDC). OACT addressed concerns regarding the comparison of valuation results from both methods and data security concerns associated with the new system.

- Transcript 48-52: Mr. Osterndorf expressed the Board's appreciation for Bob Moss, a close friend and trusted advisor with comprehensive knowledge of healthcare within the military. Bob Moss will retire in the Fall 2023.

ATTACHMENT 1

MEDICARE-ELIGIBLE RETIREE HEALTH CARE BOARD OF ACTUARIES MEETING AGENDA

July 28, 2023
10:00 AM – 1:00 PM EDT
Virtual Meeting (MS Teams)

MS Teams Link:

https://dod.teams.microsoft.us/l/meetup-join/19%3adod%3ameeting_8c6365637e0a4f34920c827944587d1f%40thread.v2/0?context=%7b%22Tid%22%3a%22102d0191-eeae-4761-b1cb-1a83e86ef445%22%2c%22Oid%22%3a%22244081cb-d4dd-4158-8c6f-2048b5cf15bb%22%7d

Call-In (for audio only): Dial: 410-874-6749 Conference ID: 248 496 215#

- ** Please ensure your audio is muted when not speaking or actively participating.**
- ** Please leave your camera off unless you are speaking.**
- ** Please identify yourself before asking a question.**
- ** If you are calling in to the meeting, please email Inger Pettygrove (Inger.M.Pettygrove.civ@mail.mil) with your name and organization as a record of your participation.**

1. Meeting Objective (Board)

Review and approve actuarial assumptions and methods needed for calculating*:

- a. FY 2025 per capita full-time and part-time normal costs
- b. September 30, 2022 unfunded liability (UFL)
- c. October 1, 2023 Treasury UFL amortization and normal cost payments

2. September 30, 2021 Actuarial Valuation Results

(Chelsea Chu, DoD Office of the Actuary)

3. September 30, 2022 Actuarial Valuation Proposals

(Drew May, Phil Davis, Jonathan Wong, DoD Office of the Actuary)

4. Transition to ADVANA

(Phil Davis)

*Board approval required

ATTACHMENT 2

MEDICARE-ELIGIBLE RETIREE HEALTH CARE BOARD OF ACTUARIES MEETING ATTENDEE LIST

July 28, 2023

	NAME	POSITION or OFFICE
1	Dave Osterndorf	Chairperson
2	Stuart Alden	Board Member
3	Jian Yu	Board Member
4	Pete Zouras	DoD Chief Actuary
5	Inger Pettygrove	DoD OACT
6	Chelsea Chu	DoD OACT
7	Phil Davis	DoD OACT
8	Drew May	DoD OACT
9	Qian Magee	DoD OACT
10	Jonathan Wong	DoD OACT
11	Ethan Field	Guest
12	Austin Keib	Guest
13	Paul Bley	General Counsel
14	Chris Borcik	CCRC Actuaries
15	Matt Schmidt	CBO
16	Edith Smith	Capitol Crusader
17	James Fasano	OSD OUSD C
18	Daniel Lee	OSD OUSD C
19	Karen Ruedisueli	MOAA
20	Debra Wade	USFHP
21	Lt Col David Barker	OSD OUSD C
22	Brad Paulis	CCRC Actuaries
23	Bryan Nelms	Kearney
24	Molly Byrnes	OSD OUSD C
25	Chris Music	OMB
26	Lori Haines	DFAS
27	Jason Merriweather	NOAA CPC
28	Karen Noah	Guest
29	LaNita Cousin	USPHS
30	Alicia Litts	OUSD (C)
31	Tom Liuzzo	OSD OUSD P-R
32	Lt Col Steve Pagoaga	IAC

33	Lt Col Keough	IAC
34	Michael McCarthy	NOAA
35	Robert J. Moss	DHA
36	Tyler Zentz	Guest
37	Richard Virgile	USCG

ATTACHMENT 3

**MEDICARE-ELIGIBLE RETIREE HEALTH CARE
BOARD OF ACTUARIES
DOD OFFICE OF THE ACTUARY HANDOUT**

July 28, 2023

Medicare-Eligible Retiree Health Care Fund

Board of Actuaries Meeting



Department of Defense
Office of the Actuary
July 28, 2023

Medicare-Eligible Retiree Health Care Fund (MERHCF) Valuation History

<u>Board Meeting</u>	Per-Capita Normal Costs			Liability (\$B)				UFL Payment (\$B)	
	<u>for</u>	<u>Full-time</u>	<u>Part-time</u>	<u>as of</u>	<u>AL</u>	<u>Fund</u>	<u>UFL</u>	<u>on</u>	<u>amount</u>
Summer 2016	FY18	\$4,890	\$1,955	9/30/15	\$427.3	\$232.8	\$194.4	10/1/16	\$5.7
Summer 2017	FY19	\$4,632	\$1,844	9/30/16	\$409.4	\$239.3	\$170.1	10/1/17	\$6.6
Summer 2018	FY19R	\$4,471	\$1,760						
Summer 2018	FY20	\$4,621	\$1,847	9/30/17	\$406.4	\$250.2	\$156.2	10/1/18	\$5.7
Summer 2019	FY21	\$4,911	\$1,952	9/30/18	\$436.3	\$265.7	\$170.6	10/1/19	\$6.6
Summer 2020	FY22	\$5,506	\$2,138	9/30/19	\$452.8	\$277.8	\$175.0	10/1/20	\$7.0
Summer 2021	FY23	\$5,795	\$2,279	9/30/20	\$472.4	\$289.7	\$182.7	10/1/21	\$7.5
Summer 2022	FY24	\$6,405	\$2,553	9/30/21	\$519.2	\$311.8	\$207.4	10/1/22	\$10.0
Summer 2023	FY25	?	?	9/30/22	?	?	?	10/1/23	?

Valuation (Gains)/Losses (\$B)

<u>Val Date</u>	<u>Experience</u>			<u>Assumptions</u>				<u>Plan Changes</u>	<u>TOTAL</u>
	<u>Asset*</u>	<u>Other</u>	<u>Total</u>	<u>Trend</u>	<u>Admin</u>	<u>Other</u>	<u>Total</u>		
9/30/17	\$4.7	(\$6.8)	(\$2.2)	\$0.9	(\$0.5)	(\$1.0)	(\$0.6)	(\$14.1)	(\$16.9)
9/30/18	\$1.4	(\$5.9)	(\$4.4)	(\$4.5)	(\$0.2)	\$22.3	\$17.6	\$0.0	\$13.2
9/30/19	\$4.4	(\$6.1)	(\$1.7)	(\$21.8)	\$0.3	\$25.0	\$3.5	\$0.0	\$1.8
9/30/20	\$6.5	(\$22.4)	(\$15.9)	\$2.6	(\$0.3)	\$20.0	\$22.3	\$0.0	\$6.4
9/30/21	(\$3.1)	(\$9.9)	(\$13.1)	\$33.6	\$0.2	\$3.1	\$36.8	\$0.0	\$23.8
9/30/22	(\$12.1)								

* Includes yield as well as budget lead time effect.

Effective Yield During the Fiscal Year
Medicare-Eligible Retiree Health Care Fund
(\$ in billions)

Fiscal <u>Year</u>	Fund Balance <u>Beginning of Year</u>	<u>Contributions Received</u>			<u>Benefit Payments</u>			Fund Balance <u>End of Year</u>	Effective <u>Annual Yield</u>
		From Uniformed Services, for <u>Normal Costs</u>	From Treasury, for Unfunded <u>Accrued Liability</u>	Investment <u>Income</u>	Direct <u>Care</u>	Purchased <u>Care</u>	<u>Total</u>		
2017	\$240.0	\$7.2	\$5.7	\$7.9	\$2.1	\$7.8	\$9.9	\$250.8	3.2%
2018	\$250.8	\$8.4	\$6.6	\$10.7	\$2.2	\$7.9	\$10.1	\$266.4	4.1%
2019	\$266.4	\$7.8	\$5.7	\$9.1	\$2.3	\$8.1	\$10.5	\$278.5	3.3%
2020	\$278.5	\$8.1	\$6.6	\$7.7	\$2.4	\$8.2	\$10.6	\$290.3	2.7%
2021	\$290.3	\$8.6	\$7.0	\$17.4	\$2.6	\$8.6	\$11.2	\$312.1	5.8%
2022	\$312.1	\$9.6	\$7.5	\$27.1	\$2.4	\$8.8	\$11.2	\$345.1	8.4%

Note: Fund balances are book values.

Benefit payments are on a paid (not incurred) basis.

Active Service Members

	<u>9/30/21</u>	<u>9/30/22</u>	<u>% Change from End of FY21 to FY22</u>
<u>DoD</u>			
Active duty	1,425,014	1,393,696	-2.2%
Reserve	702,629	675,807	-3.8%
 <u>Coast Guard</u>			
Active duty	40,449	39,471	-2.4%
Reserve	5,882	6,164	4.8%
 PHS Active duty	6,013	5,814	-3.3%
PHS Reserve		64	
 NOAA Active duty	329	334	1.6%
NOAA Reserve		0	
 <u>TOTAL</u>			
Active duty	1,471,805	1,439,315	-2.2%
Reserve	708,511	682,035	-3.7%

Note: These are end of FY counts.

Retired Beneficiaries and Dependents (all Uniformed Services)

	<u>9/30/21</u>	<u>9/30/22</u>	<u>% Change from End of FY21 to FY22</u>
<u>Retirees</u>			
Sponsors			
Non-Medicare-eligible	1,026,216	1,031,402	0.5%
Medicare-eligible	<u>1,204,853</u>	<u>1,211,196</u>	<u>0.5%</u>
Total	2,231,069	2,242,598	0.5%
Spouses			
Non-Medicare-eligible	909,647	909,228	0.0%
Medicare-eligible	<u>736,374</u>	<u>735,249</u>	<u>-0.2%</u>
Total	1,646,021	1,644,477	-0.1%
Others			
Non-Medicare-eligible	861,167	878,359	2.0%
Medicare-eligible	<u>13,482</u>	<u>13,339</u>	<u>-1.1%</u>
Total	874,649	891,698	1.9%
<u>Survivors</u>			
Spouses			
Non-Medicare-eligible	76,713	76,235	-0.6%
Medicare-eligible	<u>522,312</u>	<u>522,773</u>	<u>0.1%</u>
Total	599,025	599,008	0.0%
Others			
Non-Medicare-eligible	30,909	31,093	0.6%
Medicare-eligible	<u>8,322</u>	<u>8,406</u>	<u>1.0%</u>
Total	39,231	39,499	0.7%
<u>Retirees and Survivors</u>			
Non-Medicare-eligible	2,904,652	2,926,317	0.7%
Medicare-eligible	<u>2,485,343</u>	<u>2,490,963</u>	<u>0.2%</u>
Total	5,389,995	5,417,280	0.5%

MERHCF Incurred Outlays

	<u>FY 2021</u>	<u>FY 2022</u>	<u>% Change from FY21 to FY22</u>
Aggregate (\$ in millions)			
Purchased Care			
IP	\$787	\$818	4.0%
OP	\$3,065	\$3,210	4.7%
Rx	\$3,556	\$3,696	4.0%
Other	<u>\$125</u>	<u>\$135</u>	<u>7.3%</u>
TOTAL	\$7,533	\$7,859	4.3%
Direct Care			
IP	\$637	\$599	-6.0%
OP	\$771	\$785	1.8%
Rx	<u>\$862</u>	<u>\$850</u>	<u>-1.4%</u>
TOTAL	\$2,271	\$2,234	-1.6%
US Family Health Plan			
Capitation Rates	\$810	\$833	2.8%
Other	<u>\$3.3</u>	<u>\$3.7</u>	<u>10.3%</u>
TOTAL	\$814	\$837	2.8%
Grand Total	\$10,617	\$10,930	2.9%
	<u>FY 2021</u>	<u>FY 2022</u>	<u>% Change from FY21 to FY22</u>
Per Capita			
Purchased Care	\$2,951	\$3,211	8.8%
Direct Care	<u>\$920</u>	<u>\$915</u>	<u>-0.6%</u>
TOTAL	\$3,871	\$4,126	6.6%
US Family Health Plan	\$17,654	\$18,622	5.5%

Notes:

1. PC Retail Rx incurred amounts are net of incurred Rx rebates.
Incurred Rx rebates in FY 2021 / FY 2022 were \$550m / \$610m.
2. Medicare is primary payer in most cases with PC IP and PC OP.
3. TRICARE is primary payer in most cases with PC mail order Rx, DC (IP, OP, Rx) and USFHP.
4. Purchased care "other" includes: admin costs and certain claim adjustments or payments not already included in claims; some admin costs are included in the claims line.
5. Average USFHP capitation rate is influenced by various factors, including changes in plan (among six plans), demographic mix (age / gender), and utilization experience.
In addition, Rx rebates are applied to experience period on a paid (not incurred) basis in the development of the USFHP rates.
6. Effective FY 2016, PC mail order Rx ingredient cost is the amount Defense Health Agency (DHA) pays to replenish inventory at the mail order warehouse.

MERHCF Valuation Key Economic Assumptions

Discount Rate and Ultimate Medical Trend

	<u>September 30, 2021 Val</u>	<u>September 30, 2022 Val (Proposed)</u>
Discount Rate	4.50%	4.50%
Ultimate Medical Trend	4.75%	4.75%
MERHCF Ultimate Medical Trend		
Real Per Capita GDP	1.50%	1.50%
Inflation	2.75%	2.75%
<u>Margin or Excess Medical Cost Growth</u>	<u>0.50%</u>	<u>0.50%</u>
Total	4.75%	4.75%
MERHCF Discount Rate		
Real Yield/Real Interest	1.75%	1.75%
CPI	<u>2.75%</u>	<u>2.75%</u>
Total	4.50%	4.50%

September 30, 2022 Val (Proposed)

[illegible]

MERHCF Valuation Assumptions Decrements and Administrative Load

September 30, 2021 Val

September 30, 2022 Val (Proposed)

Decrements

Consistent w/Sept-20 Val, except:

- (1) One more year of MI,
- (2) Update MI Scale (based on MIL MI),
- (3) Updated Retiree Mortality Rates,
- (4) Updated Reserve New Entrant Assumption

Consistent w/Sept-21 Val, except:

- (1) One more year of MI,
- (2) Update MI Scale (based on MIL MI),
- (3) Updated Former Spouse Survivor
Allocation and Spouse per Sponser Rates,
- (4) Updated Reserve Rates,
- (5) PACT Act

Admin Load

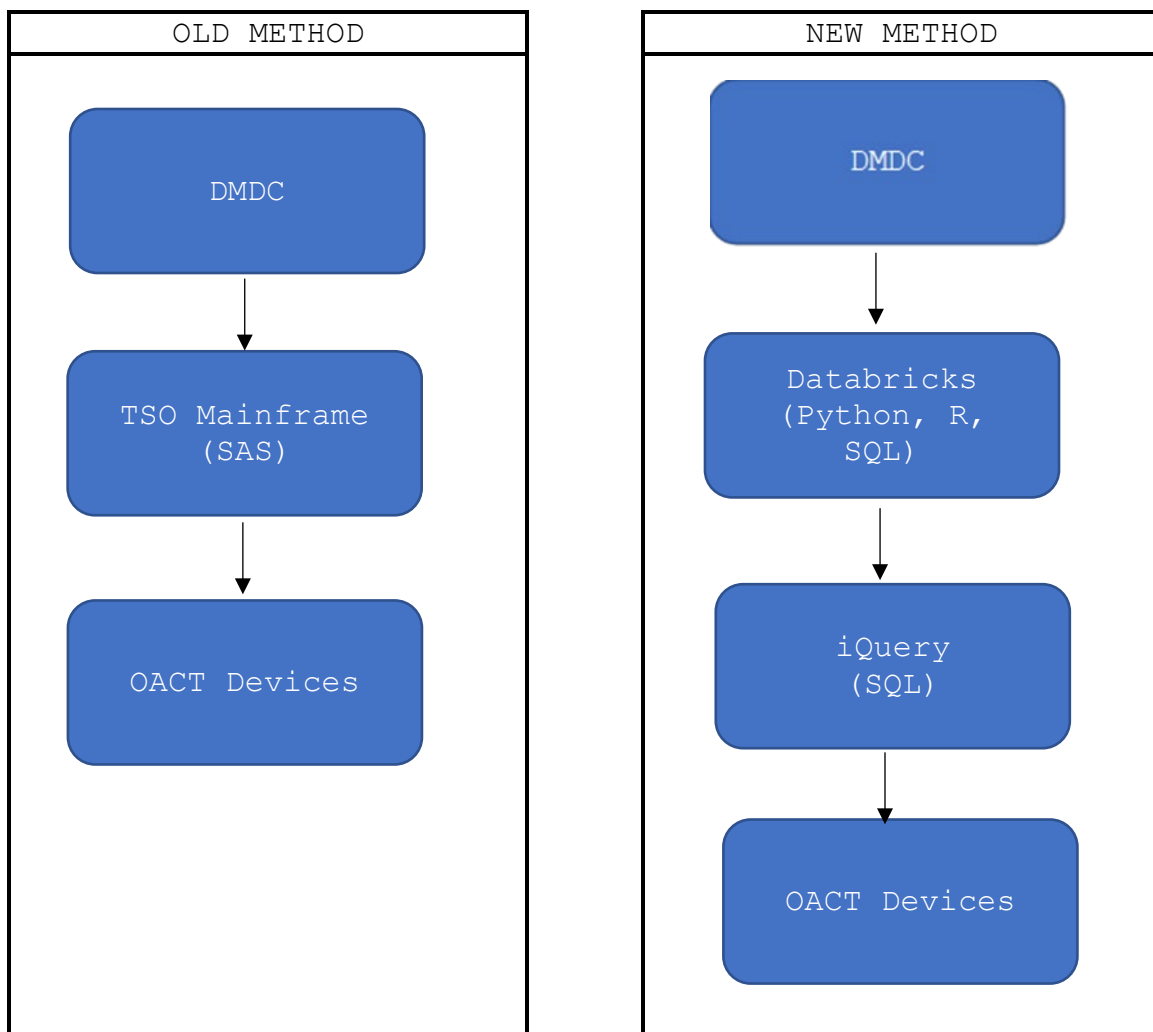
IP & OP	2.00%	1.50%
Rx	1.70%	1.70%
USFHP	0.40%	0.40%

MERHCF Valuation Assumptions
Claim Costs Development

	<u>September 30, 2021 Val</u>	<u>September 30, 2022 Val (Proposed)</u>
Average Claims Level	FY 2021 experience	FY 2022 experience
Claims Age Grading		
Direct Care	Blend of FY 2015 - 2017 experience	Blend of FY 2015 - 2017 experience
Purchased Care	Blend of FY 2015 - 2017 experience (2017 for Rx)	Blend of FY 2015 - 2017 experience (2017 for Rx)
USFHP	Blend of FY 2015 - 2017 rates by gender	Blend of FY 2015 - 2017 rates by gender

Converting to ADVANA for Data Extraction

The Census data used for valuation purposes is extracted from files maintained by the Defense Manpower Data Center (DMDC). In the past, OACT has accessed this data through the TSO Mainframe utilizing programs written in SAS. DoD has introduced a cloud computing system called ADVANA (a portmanteau of “Advancing” and “Analytics”) where DoD is able to combine 1,200 systems into one central platform for data and analytics, simplifying more than 3,000 business systems and tracking everything from finance to infrastructure. This comes with the decommissioning of the TSO Mainframe in the coming months. The ADVANA platform is accessed through internet browsers allowing streamlined access, especially compared to the TSO Mainframe. ADVANA has several “Data Tools” available to users, two of which are being used by OACT. “Databricks” allows users to access the files maintained by DMDC and perform operations using three different programming languages: Python, R, and SQL. “iQuery” allows users to access and export the files maintained by DMDC as well as user-created files using SQL. OACT extracts and manipulates files in Databricks and then exports them using iQuery. Several OACT staff members plan to undertake the monumental task of converting all of the TSO Mainframe SAS programs to Databricks and iQuery and perform parallel runs for the 2021 and 2022 valuation.



ATTACHMENT 4

**MEDICARE-ELIGIBLE RETIREE HEALTH CARE
BOARD OF ACTUARIES
MEETING TRANSCRIPT**

July 28, 2023

UNITED STATES DEPARTMENT OF DEFENSE
OFFICE OF THE ACTUARY

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BOARD OF ACTUARIES MEETING

+ + + + +

FRIDAY
JULY 28, 2023

+ + + + +

The Department of Defense Board of
Actuaries met via Videoconference, at 10:00 a.m.
EDT, Dave Osterndorf, Chair, presiding.

PRESENT

DAVE OSTERNDORF, Chair
STU ALDEN, Board Member
JIAN YU, Board Member

1 P-R-O-C-E-E-D-I-N-G-S

2 10:01 a.m.

3 CHAIR OSTERNDORF: I am going to open
4 up the 2023 Medicare-Eligible Retiree Healthcare
5 Fund Board of Actuaries meeting.

6 We have the agenda on screen, everyone
7 should be able to see it at this point. This
8 meeting is intended to provide the ability for
9 the Board to review and approve the actual
10 assumptions methods needed for calculating the
11 fiscal 25 per capita full-time and part-time
12 normal cost, the September 30, 2022 unfunded
13 liability of the fund, and the October 1, 2023
14 treasury unfunded liability amortization and
15 normal cost payments from the services.

16 We'll go through a number of agenda
17 items. We'll have the information led by the
18 staff of the DoD Office of the Actuary. The OACT
19 staff have been obviously working very hard on
20 this process as we go through. And the Board
21 would like to express its appreciation for the
22 efforts that were made in doing that.

1 So that is the intended agenda for
2 today. We'll touch on a couple things once we've
3 gotten Board approval of the actual assumptions.
4 But let's start out by reviewing previous year's
5 evaluation results. I'm going to turn it over to
6 Chelsea Chu from OACT to walk us through that.
7 Chelsea.

8 MS. CHU: Thank you, Dave.

9 Good morning, I'm Chelsea Chu from DoD
10 Office of the Actuary. I'm going to talk about
11 agenda number two, MERHCF valuation result for
12 September 30, 2021.

13 Here we are showing board handout on
14 the screen. Is the size good for everybody?

15 CHAIR OSTERNDORF: Chelsea, could you
16 increase it just a little bit, especially for us
17 old folks with bad eyes? Thank you.

18 MS. CHU: Thank you. For people on
19 the phone, please refer to the PDF file we sent
20 out yesterday named MERHCF report handout 2023.

21 Okay, page one. Page one shows
22 valuation result starting from summer 2016 Board

1 meeting. If you go to the summer 2022 line, they
2 are valuation results based on assumption
3 approved by the board members last year. First,
4 per capita normal cost.

5 Per capita normal cost under amount
6 that is attributed to the fund for each full-time
7 or part-time member every year to pay for future
8 MERHCF benefits. Last year the Board approve of
9 FY 24 per capita normal cost of 6,405 for full-
10 time and the 2,553 for part-time.

11 Let's move to the middle box. As of
12 September 30, 21, the actuarial liability is
13 519.2 billion. The fund balance is about 312
14 billion. And the fund liability is 207.4
15 billion.

16 To the right box it shows unfunded
17 liability payment of 10 billion was made by
18 Treasury on October 1, 2022.

19 Any question before we move to the
20 valuation gains and losses?

21 CHAIR OSTERNDORF: Any questions from
22 the Board or from the audience?

1 MEMBER ALDEN: Not here, Dave.

2 MEMBER YU: Yeah, I have no questions.

3 MS. CHU: Okay, let's move to
4 valuation gains and the losses. Here we are
5 showing the valuation gains and the losses by
6 experience, assumptions, and the claim changes.
7 If you go to the valuation date of September 30,
8 2021, it shows total loss about 24 billion. This
9 is mainly due to the trend of the catchup of
10 delay. The medical service was not as fast as we
11 expected.

12 If you move to the next slide,
13 September 30, 22, the asset gain is about 12
14 billion. This gain is mainly due to high
15 interaction, which increased the TIPS returned.
16 Any questions?

17 CHAIR OSTERNDORF: Hearing none, let's
18 keep going.

19 MS. CHU: Okay. Dave, we can move to
20 agenda number three.

21 CHAIR OSTERNDORF: All right, so let's
22 move to agenda item three, the actual valuation

1 assumption proposal from OACT. And I believe
2 we're going to start with Drew, Drew May.

3 MR. DAVIS: It's actually me, Phil
4 Davis.

5 CHAIR OSTERNDORF: Okay, thanks.

6 MR. DAVIS: So on this page we are
7 showing the affected fund yield during each
8 fiscal year from 2017 to 2022, the most recent
9 year we had available. And looking at the 2022,
10 we have a beginning of the year fund balance of
11 312.1 billion.

12 We received contributions of 9.6
13 billion from the services and 7.5 billion from
14 Treasury. We had investment income of 27.1
15 billion. We paid out in benefit payments 2.4
16 billion in direct care and 8.8 in purchased care,
17 for a total of 11.2 billion.

18 And that gives us an end of the year
19 fund balance of 345.1 billion and an affected
20 annual yield of 8.4%.

21 Just want to point out that these
22 numbers are as of values as the investment

1 strategy is to purchase maturities and then -- or
2 purchase assets and then hold them til maturity.

3
4 And additionally, the fund has
5 benefitted fairly well from this high inflation
6 environment we've been in. You can see, as
7 Chelsea mentioned, this high investment income of
8 27.1 billion. It's much higher than any previous
9 years. And this is because the majority of the
10 fund is in TIPS.

11 Any questions or comments for this
12 page?

13 CHAIR OSTERNDORF: Let's keep going.

14 MR. DAVIS: Okay. So now moving to
15 the next page, page three, we list the counts of
16 active service members for last year and this
17 year. And some things to point out. This is the
18 first year where we have PHS reserves, or public
19 health services, at 64. So you can see there's
20 no percentile comparison here as we didn't have
21 those last year.

22 And generally you can see that there

1 are decreases in the counts compared to last
2 year. And this is mainly due to the services
3 facing recruiting struggles. And this has been
4 offset somewhat by increased retention, however
5 you can see the effect the recruiting struggles
6 are having in the counts.

7 Are there any questions for this page?

8 CHAIR OSTERNDORF: Go ahead, Stu.

9 MEMBER ALDEN: Oh I'm sorry. Phil, this
10 is Stu Alden. I was just curious about the NOAA
11 reserve of zero. Is that -- that's like a
12 placeholder so we will have NOAA reserve people
13 in the future or we expect to but none right now?

14 MR. DAVIS: Yes, sir.

15 MEMBER ALDEN: Okay, thanks.

16 CHAIR OSTERNDORF: And given that
17 we've got a -- some challenges on bringing in new
18 recruits but are doing a better job of retaining
19 existing service members, are we starting to see
20 any change in the average age of the active
21 population?

22 MR. DAVIS: Yes, sir, a slight

1 increase in the average age from 29.49 last year
2 to 29.64 this year.

3 CHAIR OSTERNDORF: Good, thank you.

4 MR. DAVIS: Anything else regarding
5 this page?

6 MR. VIRGILE: Sorry, this is Rick
7 Virgile with the Coast Guard. Quick question on
8 COVID, more of a general question. We were
9 seeing, when it first came out, a drop in medical
10 claims, which was a little surprising til we
11 understood, well, people are not going to the
12 doctor and that's -- not having elective
13 surgeries.

14 But would you say that the current
15 claims are pretty much that's done and we've
16 caught up and can expect this to continue into
17 the future?

18 CHAIR OSTERNDORF: Can we hold on that
19 question for a bit? Because we're going to get
20 into actually some of the claims costs, and I
21 think that'll be better answered there. But it's
22 a --

1 MR. VIRGILE: Oh, sure.

2 CHAIR OSTERNDORF: A good question.

3 So I appreciate your asking it and I think we'll
4 probably get some input from OACT on exactly that
5 issue.

6 MR. DAVIS: Now moving on to the next
7 page, we have the counts of the retired
8 beneficiaries and dependents. We've broken that
9 out by retirees for sponsors, their spouses, and
10 other kind of dependents then survivors for
11 spouses as well as other kinds of survivors. And
12 then totals here.

13 And we've further broken out each
14 category into non-Medicare-eligible and Medicare-
15 eligible. And you can see across the board
16 generally there is a slight increase in the
17 number of people.

18 And just want to point out that in the
19 past, we've had Medicare increasing slower than
20 historically. And historically it's been
21 increasing slower than non-Medicare, excuse me.
22 And this hasn't happened in the past, but we are

1 seeing due to excess death as a factor that's
2 appearing.

3 Any questions or comments for this
4 page? Okay, hearing none, I will go now to the
5 next. We are outlining the incurred outlays for
6 last year and this year. And we've broken this
7 up into aggregate numbers of purchase care,
8 direct care, USFHP, and then a grand total here.
9 And then we have the per capita numbers below
10 that.

11 And at a high level, I just want to
12 point out that we all have seen a continuation of
13 a trend that we've seen post-COVID of spending
14 moving from direct care to purchased care. And
15 additionally, for USFHP, the rate is increasing,
16 and this is primarily driven by an aging
17 population. And for example the 65 plus
18 population increase in age from 75.5 to 75.9.

19 And additionally I just want to point
20 out looking at the per capita numbers for
21 purchase care, you can't do a simple calculation
22 of dividing this by the population numbers we

1 just looked at as these net of rebates.

2 CHAIR OSTERNDORF: Phil, just a quick
3 question there. Reminded, in USFHP, that's a
4 closed group, right. We're not getting new
5 entrants into the USFHP plan?

6 MR. DAVIS: Yes, I believe that's
7 correct.

8 Chelsea, correct me if I'm wrong.

9 MS. CHU: Correct. Yes, it is
10 correct. The USPP for the Medicare-eligible
11 people, we don't receive any new member any more.
12 Thank you.

13 MR. DAVIS: Are there any other
14 questions or things the Board would like me to
15 address for this page? Hearing none, we'll move
16 on to the next page, where we list the key
17 economic assumptions for last year, as well as
18 the proposed assumptions for this year.

19 So looking at the two economic
20 assumptions, the first being the ultimate medical
21 trend of 4-3/4%. That is broken down by 1-1/2%
22 real per capita GDP, 2-3/4% inflation, and a 1/2%

1 in March in our excess medical cost growth.

2 And looking at the 4-1/2% discount
3 rate, that is broken down by 1-3/4% real yield
4 and 2-3/4% CPI. And going on to our proposals,
5 despite the short-term volatility that we've been
6 seeing in the economic environment in the last
7 couple years, we don't yet see a compelling
8 reason to change our assumptions.

9 And so similar to other boards like
10 Social Security, OPM, and CMS, we are proposing
11 to keep our assumptions the same.

12 Any questions for this page?

13 CHAIR OSTERNDORF: Phil, a question on
14 the discount rate assumption. Is that
15 essentially a proxy for return on the fund? And
16 has there been any change in investment policy in
17 management of the assets? I know we're in a sort
18 of volatile time and the fund is obviously a, you
19 know, very long tail fund, given that we're, you
20 know, projecting payments off for essentially a
21 100 years.

22 What has happened in terms of any

1 investment policy or any investment adjustments?

2 MR. DAVIS: Yes, sir, so there has
3 been a change in the investment policy of going
4 down to a further or a smaller percentage of the
5 fund being made up in TIPS now to I believe 60-
6 70% from previously 75-85%.

7 And additionally, the target average
8 duration has now been shifted down from 20 years
9 to 15. And the way this has -- the justification
10 we received from DFAS is their goal is in order
11 to maximize yield of the fund.

12 CHAIR OSTERNDORF: So I guess I want
13 to make sure that we get on record the Board's
14 view around some of the investment policy
15 decisions. And I think we understand that
16 especially in a high-yield investment environment
17 like we're in right now, there is a desire to
18 grab the short-term earnings that are available
19 with investing at the shorter durations.

20 There is an, and I think we have
21 stated previously in other Board meetings, there
22 is a very strong view from this board that the

1 investment policy should be very closely tied to
2 a strong asset liability matching kind of
3 approach, given that we really are financing, as
4 in I noted earlier, very long tail liability.

5 And therefore our preference is to
6 have longer rather than shorter durations,
7 knowing that the duration of our liability is
8 very long.

9 So given that I think we've now given
10 this input in prior meetings and in prior venues,
11 I think, you know, one of the things that the
12 Board is going to ask of OACT and DFAS and work
13 through the channels is to try to put together a
14 relatively strong asset liability study to inform
15 some of our decision-making as we go forward,
16 especially around setting appropriate discount
17 rates, given that we have the potential for an
18 asset liability mismatch here.

19 And for purposes of preserving the
20 integrity of the fund, rather than simply going
21 to a more conservative discount rate to offset
22 the potential mismatch there, I think we'd like

1 to have that much better informed with data.

2 So one of the follow-up steps from
3 this meeting from our perspective on the Board
4 will be to request something in the asset
5 liability matching review to have that
6 information able to inform our further decisions.

7 So appreciate your input, and Pete
8 Zouras and others will circle back to you on
9 trying to make that asset liability study happen.

10 MR. DAVIS: Yes, sir. There's nothing
11 else for this --

12 MR. ZOURAS: I noticed members from
13 the investments advisory committee are on the
14 call. Did you want to respond?

15 MR. KEOUGH: Hello. We are, there's
16 a couple of us of on, so we're more than happy to
17 answer any question. The one thing that I'll
18 start off with, with a word that was used just a
19 second ago, which was target. We are not
20 targeting anything. If anything, we are
21 targeting duration over 20 years.

22 The changes to the investment policy

1 statement were put forward to simply give the
2 investment advisory committee the ability to
3 recommend different durations to take advantage
4 of a situation similar to what we just had
5 recently, which is an inverted yield curve,
6 ridiculously high interest rates with very little
7 risk on the short end.

8 And again, duration is a measure of
9 risk, by the way. It's not just a way to match
10 liabilities. The less duration you have in
11 portfolio, technically the less risk you. Now, I
12 realize that doesn't match the long duration of
13 the liabilities.

14 However, you can always roll those
15 over as the yield curve normalizes in future
16 years, which it will. I don't know where it'll
17 normalize, but it will normalize. You can then
18 roll those maturities that have just matured, the
19 shorter end stuff, out.

20 And that's really what we're trying to
21 do is give us the opportunity to take advantage
22 of better yields down the road. And in the

1 meantime take advantage of the current yields.
2 We are absolutely not targeting a lower duration
3 fund. We are simply giving ourselves more
4 opportunity to take advantage of shorter and
5 shorter yielding instruments.

6 On the TIPS versus -- on the TIPS
7 versus nominal side, TIPS have done very well for
8 us lately. In fact, there's no doubt about it,
9 and it's hard to argue with the return that we've
10 received from TIPS. That may not always be the
11 case.

12 TIPS are an instrument that, you know,
13 the way -- when we look at and we analyze TIPS,
14 there's a thing called the break-even rate of
15 return, which is the proxy for the expected rate
16 of inflation for each maturity level. So there's
17 a break-even rate of return for, say, a five-year
18 TIP, a ten-year TIP, a 20-year TIP, a 30-year
19 TIP.

20 And that -- and if that, let's say
21 that's 1.9%, which is kind of the general average
22 right now. If the break-even rate of return is

1 1.9% for a 20-year TIP, if we, the investment
2 advisory committee, and you all, the actuaries,
3 if you believe that inflation will be higher than
4 1.9% for the next -- on average for the next 20
5 years, you would want to buy TIPS. If you
6 believe that the average inflation rate will be
7 lower than 1.9% for the next 20 years, you would
8 buy nominals, right.

9 So what we've done a long time ago is
10 we've said we want to overweight TIPS in the
11 portfolio. And again, that's worked out very
12 well for us. If conditions change, we really
13 want to be able to recommend more nominals.

14 In other words, if the expected
15 inflation rate on a break-even TIPS on the
16 October 1 timeline that we make the investments,
17 let's say 4%, we don't want to necessarily buy
18 TIPS. Because we believe the long-term inflation
19 rate will be closer to 3%, which is the historic
20 rate of inflation.

21 And I know you all may even think it
22 might be lower. Why? Because let's say it's a

1 target of 2%.

2 So the only reason we're making an
3 adjustment to the investment policy statement is
4 to get us more leverage to make a little bit
5 broader decisions in investments to the
6 investment committee. We are certainly not
7 targeting lower duration for less TIPS.

8 And if we want to do a duration-
9 matching liability study, I'd be happy to help.
10 Because that's important, that's something that's
11 important to us. And it's actually one of our
12 absolute -- that is one of our priorities, to
13 match liabilities. We always match, we always
14 look at that in matched liabilities.

15 And if you were to actually look at
16 our portfolio right now -- I don't have it up
17 right now. But I think it's 2032-ish, I believe.
18 Very few assets held in that area, that timeline.
19 Why? Because there were no assets, Treasury
20 didn't issue any assets that we could cover those
21 with.

22 Which we're now within ten years of

1 that, we can now use ten-year treasuries to go
2 out and tap into those things. So we're buying
3 more of those to raise the assets to 2032.

4 We were very, very conscious of asset-
5 matching liabilities policies. But we're also
6 conscious of maximizing returns because at the
7 end of the day that's what really, really matters
8 on our side of the street.

9 So I'll be happy to -- and we've got
10 a few folks on the call. I know Steve Pagoaga's
11 on the call. Colonel is. I'd be happy to answer
12 any questions, and he would, if you guys have any
13 questions about why we've asked for that change
14 in the investment policy statement.

15 CHAIR OSTERNDORF: That's helpful,
16 appreciate it. Just for the sake of the record,
17 could you identify yourself just so we have your
18 name.

19 MR. KEOUGH: Oh, I'm sorry, you did
20 say to do that. I apologize. This is Lieutenant
21 Colonel Lee Keough, Rudy Keough. I'm on the IAC.
22 I'm one of the senior members. I'm not the

1 ranking senior member, but I've been on the
2 committee for now I guess 12 years or something
3 like that.

4 And this is my last go-round,
5 actually, I retire in October. So the August-
6 September's meetings that we will have will be
7 the last one for me.

8 CHAIR OSTERNDORF: Thank you for that
9 input and congratulations on your retirement.

10 MR. PAGOAGA: This is Lieutenant
11 Colonel Steve Pagoaga. The only additional
12 comment I'd make is, one, emphasizing Rudy's
13 point that, yes, we are primarily concerned with
14 matching assets and liabilities. So we do pay
15 attention to that first and foremost.

16 The second point would be on the
17 duration matter, and it really has to do with the
18 shape of the yield curve. When we get beyond ten
19 years, the shape of the yield curve in treasuries
20 right now is a little unusual. So building that
21 flexibility to grab a year or two earlier in
22 maturity is what we're looking for in the

1 modification to the investment policy statement.

2 But it's certainly not a intent or
3 plan to bring maturity, average maturity or
4 duration down deliberately. It's really an
5 opportunistic move.

6 MR. KEOUGH: Matter of fact, if I can
7 -- am I allowed to share a screen with you on my
8 end here? I don't know if I have that capability
9 from --

10 MS. PETTYGROVE: I think you should be
11 able to. Give it a shot.

12 MR. KEOUGH: Okay, hang on I'm trying.
13 It's not -- I don't know that it's letting me.
14 Usually I see a button that pops up for me and I
15 -- I can tell you, so there's a website, and you
16 guys have access to this obviously. I'm not
17 trying to insult your intelligence.

18 But there's a very good website you
19 can look at called ustreasuryyieldcurve.com. All
20 one word, ustreasuryyieldcurve.com. And it pops,
21 immediately pops up to the yield curve. This is
22 the treasury yield curve. And you can pin that

1 one, there's a pin up there.

2 Pin it, it changes colors, or it has
3 a red -- and then you can change the date. Like
4 I can go back and say okay, what was it a year
5 ago. And you'll see the dramatic change in the
6 yield curve.

7 And if you actually do this for
8 September, that's when we had to make the
9 decision on what recommendations to make. And
10 this drove a lot of what -- of how we made those
11 recommendations.

12 So one thing I will tell you about the
13 inverted yield curve, though, and this is good
14 for us to some extent, all of us, is that it did
15 shift up. The whole thing shifted up, which is
16 good. So going out and taking some long yields
17 didn't hurt us, it just didn't help us as much as
18 taking the short yield from a return standpoint.

19 What we expect is that over time the
20 short end will come back down. And we're hoping
21 the long end stays above 4%, that would be nice.
22 Then it makes bond investing very simple and very

1 logical. We build in a ladder, we make sure the
2 duration's over 20 years, and we meet everybody's
3 requirements, including ours. But the inverted
4 yield curves really, really mess things up, so.

5 I really apologize I can't share that
6 with you. Oh, here we go -- no, that's open.

7 CHAIR OSTERNDORF: That's fine, I
8 think your description was very useful. And I
9 appreciate the input. So it is -- it helps us in
10 kind of finalizing our decision as to our
11 assumption setting here. So that's valuable, and
12 I appreciate your -- there we go. Yeah, so.

13 MR. KEOUGH: If you back three years,
14 you can kind of see what we're dealing with here.
15 I mean, a few years -- if you look at the blue
16 line on the bottom, which is interesting, I
17 remember -- this is 2020, okay.

18 Not that long ago, but if you look at
19 your return assumptions, the investment
20 assumption from the actuarial point of view back
21 in 2020, I still think we were assuming that we
22 would be able to get a pretty high rate of return

1 from treasuries.

2 And what we were dealing was we were
3 forced to only invest in like 1.25% at best way
4 back then. Even though TIPS weren't paying us a
5 lot, we felt like the break-even rate of return
6 was so low, it was down to like 1.2 or something,
7 there was just no reason not to buy TIPS at that
8 point.

9 And you see it did work out for us.
10 I can't say that I was a genius or we were a
11 genius or anything like that. But through our
12 discussions we came up with that conclusion on
13 purchases way back in 2020. There's the yield
14 curve movement since then, so.

15 Anyway, I don't want to take up too
16 much of your time, but that is something I think
17 is important to understand from where we're
18 coming from. Stop sharing, there you go.

19 CHAIR OSTERNDORF: Good input, so
20 appreciate that. And that will help us in our
21 consideration. And appreciate the fact that, you
22 know, you folks are all willing to be engaged in,

1 you know, a bit of a more complete study around
2 this. I think there's a real opportunity to have
3 greater information as we go forward. So
4 appreciate your work on that.

5 Board, are there other questions on
6 this page before we go on?

7 MEMBER YU: No more questions,
8 appreciate the additional context. I think even
9 at the minimum, acknowledging that there is focus
10 on lining the duration between asset liability is
11 important to know that the risk is being
12 monitored and evaluated before a decision is
13 made.

14 MEMBER ALDEN: No questions from me,
15 Dave.

16 MR. DAVIS: So now I believe I'm
17 turning it over to Drew May.

18 MR. MAY: Thank you. The next page is
19 the MERHCF Valuation Medical Trend Assumptions.
20 And can everyone see it okay?

21 MR. DAVIS: Can you make it a little
22 larger, Drew? Thank you.

1 MR. MAY: Thank you, Phil.

2 On the left, we have the trend
3 assumptions set by the Board at last year's
4 meeting. And on the right we have the proposed
5 trends. There are direct care inpatient, direct
6 care outpatient, direct care drug, purchased care
7 inpatient, purchased care outpatient, and
8 purchased care drug. As well as USFHP.

9 Each row corresponds to a fiscal year,
10 and we reach the ultimate medical trend after 25
11 years.

12 The proposed trends are taking the
13 most recent experience and information into
14 consideration, specifically, first we're
15 considering a continued bounce-back to pre-COVID
16 levels. Recent experience has shown this to be
17 more gradual, with as mentioned earlier, the
18 actual 2021 to 2022 trends being lower than last
19 year's expected.

20 And this is reflected in the proposed
21 trends, and they also anticipate a moderate level
22 of returned deferred care.

1 Second, we are considering a continued
2 shift to purchased care from direct care.

3 Speaking to advisors, we've been told that direct
4 care admissions have been decreasing since 2017,
5 and for reasons such as convenience or generally
6 little incentive to use direct care, retirees are
7 not returning to the medical treatment facilities
8 and are instead using purchased care.

9 Lastly, we are considering the impact
10 of known emerging blockbuster drugs, such as
11 Ozempic and Wegovy. And we will also be
12 continuing to pay attention to other drug
13 introductions that will impact the fund.

14 Are there any questions or comments on
15 this page?

16 CHAIR OSTERNDORF: I want to circle
17 back to the question that was asked earlier I
18 believe from the gentleman at Coast Guard I
19 think. What I'm hearing you say, Drew, is we
20 were -- certainly our experience showed that
21 there was a significant drop-off due to the
22 pandemic in terms of services.

1 As we see that ability to address some
2 of the deferred care areas, we are still a year
3 or two away from having an expectation that we
4 have fully returned to what was a pre-COVID
5 steady state. Is that fair?

6 MR. MAY: Yes.

7 CHAIR OSTERNDORF: And to the earlier
8 question, did that address the individual's
9 question that was asked previously?

10 MR. VIRGILE: Sorry, I was muted.
11 Yeah, pretty much. I, you know, our concern is
12 more with the MHS benefits than the MERHCF
13 benefits. But they're, you know, the same
14 benefits pretty much. They just, one starts at
15 65 and the other stops at 65.

16 But you know, I don't expect you to
17 address things specific to MHS here. You know, I
18 think, you know, the same answer probably applies
19 to both.

20 CHAIR OSTERNDORF: And I think we
21 would agree with that. We're generally seeing
22 care patterns both pre- and post-Medicare act

1 relatively consistently.

2 And you know, those of you who have
3 seen past quadrennial reports and other areas of
4 inputs from the Board, we have suggested that
5 this board really over time should be looking at
6 both the pre-Medicare and Medicare-eligible
7 retirees. So from that standpoint we do keep an
8 eye on it as well.

9 So we would agree with your basic
10 statement.

11 MR. VIRGILE: Okay, thank you.

12 CHAIR OSTERNDORF: Any other questions
13 about the trend assumptions? Jian, Stu?

14 MEMBER YU: No, I'm good, thank you.

15 MEMBER ALDEN: I'm good.

16 CHAIR OSTERNDORF: Okay, you can keep
17 going.

18 MR. MAY: On this page we have the
19 decrements and administrative load. To start
20 with the proposed decrements, we have an
21 additional year of mortality improvement and an
22 update to the mortality improvement scales, which

1 Jonathan Wong will speak to.

2 MR. WONG LAU: Thank you, Drew.

3 On to our next decrement update and
4 our time improvement --

5 MS. PETTYGROVE: Hey, Jon, it's Inger.
6 We kind of forgot to prompt you that you're a
7 relatively new hire for the OACT crew. Would you
8 just give us a quick introduction?

9 MR. WONG LAU: Yeah, sure. So you
10 guys haven't see me from last year, but this is
11 my first year and being part of OACT. So I'll
12 introduce myself. My name is Jonathan Wong. I
13 graduated UCSB just like about a year ago. And
14 UCSB is UC-Santa Barbara.

15 And yeah, so it's been about a year,
16 and a milestone year. I hope to learn as much as
17 possible and work closely with everyone here.
18 Thank you.

19 CHAIR OSTERNDORF: Glad to have you.

20 MR. WONG LAU: Okay, so for mortality
21 improvement, for step one, as Drew mentioned,
22 mortality scales are updated each year to reflect

1 another year of mortality improvement. And a
2 second step to -- or incorporation of the 2021
3 and 2022 mortality data into the experience
4 period, with weights of 0% for 2021 and 25% for
5 2022.

6 And it's worth noting that this
7 experience period is using actual experience of
8 military retirees. And on another note, it's
9 worth mentioning that the Society of Actuaries,
10 also known as SOA, did not produce a new
11 projection scale in 2022, as they believed that
12 COVID-impacted data was certain -- uncertain to
13 be predictive of future mortality.

14 As such, we are following CMI, or the
15 continuous mortality investigations approach, for
16 handling 2022.

17 And another note is that we're only
18 projecting improvements to the valuation date but
19 not projecting future improvement after the
20 valuation date.

21 And secondly we also have a update to
22 the survivor's long-term rate of improvement.

1 And this is using data from the military retiree
2 to -- in replacement of the Society of Actuaries.

3 And third, we also have the spouse per
4 sponsor rate update, and that is using the 2022
5 experience.

6 Is there any questions or comments on
7 this topic?

8 CHAIR OSTERNDORF: So just to make
9 sure I'm tracking the one-year of mortality
10 improvement to the population statistic. The
11 other two are specific to the military retirement
12 fund experience. Is that correct?

13 MR. WONG LAU: That sounds right,
14 yeah.

15 If there's any other questions, I'll
16 be turning it over to Drew for the reserve rates
17 update.

18 MR. MAY: Thank you, Jon.

19 The next proposal is an update to the
20 reserve rates. The purpose of the reserve rate
21 update is to adjust our projection of reserve
22 retirees. Most reserve retirees come from the

1 gray area, which means that they have 20 good
2 years of service and are inactive waiting for
3 retirement eligibility, which usually occurs at
4 age 60.

5 However, in our data there are about
6 2,700 gray area reserves at or over age 63 who
7 are not retiring. And this is contrary to our
8 current assumption that at our over either age 63
9 or 41 years of service, there is a 100%
10 retirement rate.

11 To address this, we are proposing
12 using a rate based on experience in fiscal years
13 2017 to 2019 for those ages and year of service.

14 There is one exception, which is age
15 59 and 41 years of service, where we believe it
16 is reasonable to still assume that anyone turning
17 60 would then claim their benefits.

18 To verify that this proposal is
19 appropriate, we reached out to advisors as to why
20 these reservists are on --

21 MS. PETTYGROVE: Hey Drew, sorry to
22 interrupt. Matt Schmit has a hand up. Matt.

1 MR. SCHMIT: Yeah, Matt Schmit from
2 CBO. I think you're about to answer my question.
3 My question is why, why are they not retiring.

4 MR. MAY: Yeah, to verify we reached
5 out to advisors as to why they are on file, and
6 we were told that they're inactive
7 servicemembers. And beyond the initial queries
8 for retirement application at age 59, there is
9 not much management of the records.

10 Therefore, they may remain on file if
11 there's no response from the reservist for
12 several possible reasons, including they're
13 deceased or otherwise physically unable to reply,
14 they know that they're ineligible for reasons
15 such as living overseas, or perhaps they're
16 receiving a better benefit in place of reserve
17 retirement, such as retirement through a
18 different service or a benefit through Veterans
19 Affairs or VA.

20 Does that answer your question?

21 MR. SCHMIT: Yes, thank you very much.

22 MR. VIRGILE: I just have a follow-up

1 based on some discussion we've had on this at the
2 Retirement Board meeting. There's no -- and I
3 don't know if --

4 MS. PETTYGROVE: Rick, Rick -- Rick,
5 that's you, right, that's Rick Virgile?

6 MR. VIRGILE: Yes, it is.

7 MS. PETTYGROVE: Yeah, I just wanted
8 to make sure that was identified for the court
9 reporter.

10 MR. VIRGILE: Yeah, I'll make sure I
11 mentioned my name if I have anything to say, and
12 I usually do. There is, unlike the private
13 sector, when somebody is eligible to retire and
14 doesn't, there's no outreach on the pension side
15 to contact them and say hey, we're trying to find
16 you, do you want your benefits.

17 And I'd expect that same approach
18 applies on the medical side, that if the member
19 doesn't contact you, he never gets the benefits.

20 MR. MAY: From what we have heard from
21 the advisors, there is a bit more nuance to the
22 process. But in general, it would be apply for a

1 retirement benefits to become eligible for the
2 health benefits.

3 CHAIR OSTERNDORF: And just
4 logistically, Drew, I'm assuming that if someone
5 doesn't apply for retirement benefits, they're
6 literally not going to have, you know, the
7 medical, you know, card that says when I go into
8 a, you know, doctor's office, private sector,
9 here's my card.

10 I'm not going to have that unless I
11 actually apply for retirement, is that true?

12 MR. MAY: Yes, that is what we have
13 been told.

14 CHAIR OSTERNDORF: Okay.

15 MR. MAY: Continuing, the last
16 proposed decrement is a 10% increase of
17 disability retirement rates to reflect
18 anticipated changes due to the PACT Act, which
19 passed on August 10, 2022. It increased
20 criteria, which can lead to VA healthcare and
21 benefits, and this 10% is a moderate reflection
22 of the PACT Act as it is currently understood.

1 This means the proposal is not
2 speculating on what services will or could do in
3 the future. We will continue to monitor the
4 impact of PACT Act and look for any resulting
5 policy changes that would affect this valuation.

6 Are there any questions or comments
7 before we move on? Still have one more item on
8 that page.

9 Below the decrements we have
10 administrative load. As you can see, there's a
11 large change in medical admin load, going from 2%
12 to 1.5%. Reaching out to the Defense Health
13 Agency, we were told that this is due to a
14 contract of current change in April 2022.

15 Any questions or comments here? Next
16 page, please.

17 On this page we have the claims cost
18 development. We are changing the average claims
19 levels to use fiscal year 2022 experience and
20 continuing to use fiscal 2015 to 2017 for claims
21 age grading or claim vectors. And I'll also note
22 that our population is large enough that one year

1 of experience is sufficient for a credible
2 average claims level.

3 We looked at updating the claim vector
4 experience and bringing it to a raw state. It
5 did not produce much shape -- change in the
6 shape, therefore, updating them did not have much
7 impact.

8 And furthermore, with our current
9 methodology, to update them would use fiscal
10 years 2020 to 2022. And while it appears that
11 there's minimal change, we are still wary of
12 using entirely COVID-impacted years to model the
13 future.

14 Are there any questions or comments on
15 this page? Okay. I believe this concludes item
16 three of the agenda.

17 CHAIR OSTERNDORF: So at this point I
18 think the Board has received the full proposal
19 from OACT in terms of the assumptions that are
20 being proposed for this year's valuation. Let me
21 make sure there aren't any other questions on the
22 assumptions that have been proposed.

1 Stu, Jian, do you have any other
2 questions?

3 MEMBER ALDEN: Not here, Dave.

4 MR. VIRGILE: Rick Virgile again. My
5 last question, which I ask a lot, is I always
6 compare what the MRS Board does to the MHS Board.
7 And in general if an assumption has changed for
8 one, it's changed for the other. You know, they
9 tend to run in tandem.

10 The one big exception that I see is on
11 mortality improvements in the future. Whereas
12 the pension side assumes future improvements and
13 the medical side doesn't, and I just at this
14 point think maybe it's time to put that on the
15 table.

16 It's not a big difference to me for my
17 numbers, but I don't like the inconsistency
18 between the two. And I know there's two separate
19 boards making two separate sets of decisions. So
20 it's more of a comment than a question.

21 CHAIR OSTERNDORF: So it's a fair
22 comment. It is something that we have discussed

1 in the past. One of the interesting elements for
2 us on the healthcare side is if we assume greater
3 mortality improvement and therefore greater
4 longevity, likely it would also come along with
5 improvement in health status.

6 And so while people would be receiving
7 benefits for longer, they would likely be
8 receiving less benefits because they are
9 generally healthier. That is of course
10 speculative. But it is a likely outcome.

11 So we have a little bit of a self-
12 correcting element within the MERHCF that is not
13 that is not true on the retirement fund side,
14 where if you live longer, then you simply receive
15 benefits for longer and it's the same benefit.

16 Here obviously the benefit level
17 itself is dependent on the health status of the
18 members. And if longer life is attributable to
19 improvements in the morbidity of the population,
20 then those two will be somewhat offsetting.

21 So that has been part of our decision
22 making around not reflecting all of these

1 improvements in future years. And will be
2 something I think that we continue to look at. I
3 think that's where our thinking has been to date.
4 So it's a fair comment, it is something that we
5 have discussed.

6 MR. VIRGILE: Great, thank you.

7 CHAIR OSTERNDORF: Are there any other
8 questions or comments from the audience? Then at
9 this point in time I'll look for a motion to
10 adopt the proposals from OACT.

11 MEMBER ALDEN: Yes, Dave, Stu here.
12 I move that the Board adopt the assumptions
13 presented here by OACT for the 9/30/22 valuation.

14 MEMBER YU: And this is Jian, I
15 second.

16 CHAIR OSTERNDORF: All right, then
17 let's go ahead and vote on that. Stu, how do you
18 vote?

19 MEMBER ALDEN: Aye.

20 CHAIR OSTERNDORF: Jian?

21 MEMBER YU: Aye.

22 CHAIR OSTERNDORF: And I also vote

1 aye. So we have approved these assumptions for
2 the current valuation. And we look forward to
3 seeing the results as the group from OACT puts
4 together the final numbers.

5 At this point I know we have at least
6 a couple other minor items that we want to touch
7 on. I think they are more on the informative
8 side. Phil Davis, I think you have a update for
9 us on the data management side of some changes
10 that are happening within the -- within the OACT
11 area.

12 MR. DAVIS: Yes, sir. So I'll be
13 covering a project that three OACTers have been
14 working on for the last several months. And it
15 essentially boils down to a change in the method
16 in which we receive data from the Defense
17 Manpower Data Center, or DMDC, that we use to
18 construct our census that we use for valuation
19 purposes.

20 So the method that we've been using
21 and have used in the past is essentially outlined
22 here in this crude graphic where DMDC produces

1 and maintains the data files. We use a platform
2 that we call the Mainframe to access these files,
3 perform whatever manipulations and calculations
4 we need to, primarily through SAS programs.

5 And then we transfer these quote
6 unquote new files to our devices. And this
7 system has been somewhat cumbersome in the past,
8 as for example several OACTers have to have
9 complete separate laptops purely dedicated to
10 accessing the Mainframe. And then we transfer
11 those through a platform like DoD Safe Transfer
12 to our day-to-day devices.

13 And the Mainframe is being
14 decommissioned, and in the coming months. And
15 with that comes the introduction of a new
16 platform called ADVANA, which is a portmanteau of
17 advancing and analytics. This platform's owned
18 by the comptroller and it is a cloud computing
19 platform.

20 And there are several data tools
21 available in ADVANA, and OACT primarily has used
22 two so far. And I'll outline this new method

1 that we will be using for next year's valuation,
2 where DMDC still produces and maintains the data
3 files.

4 We will access these data files and
5 perform whatever calculations and manipulations
6 we previously did in the Mainframe, and a data
7 tool called Databricks, where we will perform
8 these in a variety of Python, R, and SQL
9 programs. And then we will upload these new
10 files to our cluster, which is essentially our
11 office's digital workspace.

12 And then we will download these files
13 through another data tool called iQuery using SQL
14 programs, and we can download those directly to
15 our devices as ADVANA's accessed through the
16 internet browser. So it's much more streamlined
17 access, which is very convenient and nice for us.

18 And additionally there are built-in
19 machine learning and predictive analytics
20 capabilities with ADVANA. And we haven't had a
21 full chance to explore those yet. However, we're
22 very excited to be able to do so.

1 And we are planning on running
2 parallel runs for the 2021 and 2022 valuation to
3 make sure everything is going smoothly, and so
4 far it is. And then we will be using ADVANA
5 exclusively for the 2023 valuation.

6 Any questions or comments regarding
7 this?

8 MEMBER ALDEN: Yes, Phil, Stu here.
9 Can you give us a feel for what kinds of
10 comparisons you've done between the old and new
11 data gathering, just to ensure we've got
12 consistency and we aren't opening up any new --
13 any new unforeseen problems?

14 MR. DAVIS: Yes, sir. So we have
15 performed these parallel runs on the retirement
16 side already, and while the censuses and the data
17 won't exactly be the same, there are some
18 similarities. And on the retirement side, for
19 instance, the 2022 parallel run, there was a
20 headcount difference of three people and a
21 liability difference of .004%.

22 MEMBER ALDEN: Okay.

1 MR. DAVIS: So we're very good there,
2 and hopefully that'll carry on to health. And we
3 expect it to do so.

4 MEMBER ALDEN: Very good, thank you.

5 MR. DAVIS: Any other questions or
6 comments?

7 CHAIR OSTERNDORF: Phil, I'm assuming
8 the same level of data security, data integrity
9 that was resident in the old system is in this
10 process as well so that we're not opening up any
11 kind of, you know, potential data challenges.

12 MR. DAVIS: Yes, sir. As several
13 OACTers can speak to from personal experience,
14 it's an extensive and thorough review process to
15 get access to ADVANA. So it assures us
16 everything is the same security as Mainframe.

17 CHAIR OSTERNDORF: Thank you.
18 Appreciate the input. And then just one final
19 topic for the meeting, I would be remiss if we
20 didn't take the opportunity that this is the
21 final valuation process where we are getting
22 input from one of our favorite advisors, Bob

1 Moss.

2 Bob is someone who has been, after a
3 30-year career in the Air Force side, moved over
4 into the private sector and now comes back as the
5 Chief of Budget and Resource Management Division.
6 Bob has been one of those individuals who has
7 comprehensive knowledge of healthcare within the
8 military.

9 He is one of those resources that we
10 have relied on who is always there to provide
11 insight and input in a way that is very
12 digestible for all of those of us who only see
13 this on a periodic basis. And has been, you
14 know, both a trusted advisor and friend to many
15 of us for a number of years.

16 Bob's work with all this, you know,
17 predates my, beginning of my term 11 years ago on
18 the OACT Board and is someone who has just, I
19 think has provided, you know, a ton of value.

20 And we very much appreciate his
21 counsel and input. We wish him the best on his
22 retirement as he goes out and explores other

1 things in life after a very long career dedicated
2 to military service.

3 So Bob, very much appreciate what you
4 have done for us. I want to express both the
5 Board's appreciation and my personal appreciation
6 for the efforts and for the good counsel you've
7 given us. So thank you for that, and best wishes
8 on your retirement.

9 MR. MOSS: Thank you, sir, I
10 appreciate those very kind words. And I wish all
11 of you the very best. And I am sure the trust
12 fund will continue to prosper and do very well
13 under your guidance and the guidance of senior
14 leadership both in DoD and the DHA. Appreciate
15 it, thank you very much.

16 MEMBER ALDEN: Thanks, Bob.

17 MEMBER YU: Thank you.

18 CHAIR OSTERNDORF: Before I end the
19 meeting, are there any other issues that should
20 be raised from -- first, anything from Board
21 members that we didn't touch on?

22 MEMBER YU: No.

1 MEMBER ALDEN: Not here, Dave, no.

2 CHAIR OSTERNDORF: Anything from the
3 OACT side, Pete? Any of your group, anything
4 else we needed to look at?

5 MR. ZOURAS: None here.

6 CHAIR OSTERNDORF: And anything from
7 the attendees?

8 MR. VIRGILE: Rick Virgile, final
9 question. And I missed the first few minutes, so
10 you may have touched on this already. But the
11 fiscal year 24 letters I assume will go out mid
12 to late September, making the, you know, the
13 numbers final so we can make our payments by
14 October 1 into the fund.

15 CHAIR OSTERNDORF: Yeah, I believe we
16 usually shoot for getting those numbers our
17 during August, so that would be our expectation.

18 MR. VIRGILE: All right. And the 25
19 numbers are question marks. Does that mean
20 they're still a work in progress? Just on the
21 chart showing history of the contribution rates
22 full-time and part-time?

1 CHAIR OSTERNDORF: Yeah, so those are
2 the numbers that are dependent on the valuation
3 that's being done now with the new assumptions.

4 MR. VIRGILE: Okay, that's it for me.
5 Thank you.

6 CHAIR OSTERNDORF: Thank you, Rick.
7 Any other questions or comments? All right,
8 well, then hearing none, I will formally adjourn
9 this meeting. Thank you all on the OACT staff
10 for all of your hard work. Thank the attendees
11 for your time today. And appreciate all parties
12 involved in this.

13 So thank you, and all of you have a
14 good rest of the day and a good weekend.

15 (Whereupon, the above-entitled matter
16 went off the record at 10:57 a.m.)
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In the matter of: Board Meeting

Before: US DOD Office of the Actuary

Date: 07-28-23

Place: teleconference

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