TESTIMONY OF SPARB COLLINS ON

HOUSE BILL 1058

Mr. Chairman, members of the committee, good morning my name is Sparb Collins and I am the Executive Director of the North Dakota Public Employees Retirement System (PERS). Today I appear before you in support of HB1058. This bill relates to retirees, in particular pre-Medicare retirees. Specifically, it does the following:

1. Closes the PERS health plan to pre-Medicare retirees on July 1, 2015 (Section 1)
2. Makes the retiree health credit portable (Section 2 & 3).

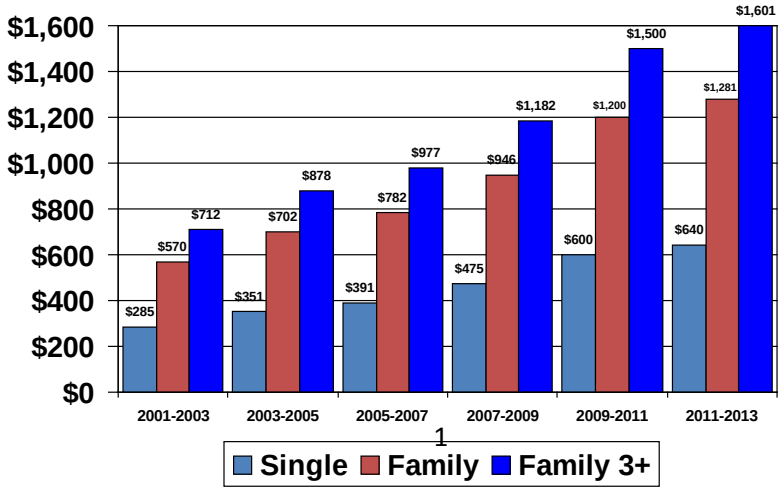
Let me discuss the reasons and details of the proposed changes listed above.

SECTION 1 - CLOSES THE PERS HEALTH PLAN TO PRE-MEDICARE RETIREES

Section 54-52.1-02 (1) authorizes retired employees not eligible for Medicare the option to participate in the PERS Health Plan. Historically, it is my understanding that this option was available to insure that retiring employees would be able to find health coverage when they retired without having to be exposed to medical underwriting requirements or pre-existing condition provisions. The rate for this coverage is also set in statute as:

- the rate for a non-Medicare retiree single plan is one hundred fifty percent of the active member single plan rate,
- the rate for a non-Medicare retiree family plan of two people is twice the non-Medicare retiree single plan rate, and
- the rate for a non-Medicare retiree family plan of three or more persons is two and one-half times the non-Medicare retiree single plan rate.

The following is a history of the premium for that coverage:



Since the above rate is set by a state statute and is not based upon the actuarial requirements of the group, the above rates while high, do not reflect the full cost of that coverage. If the rate was set based upon the actuarial requirement for the pre-Medicare group, it would be even higher. This difference between the statutory rate and the actuarial rate is called an implicit subsidy of the plan.

Relating to financial reporting of this implicit subsidy, the Governmental Accounting Standards Board (GASB) finalized Statements No. 43 (GASB 43 for funded OPEB plans) and 45 (GASB 45 for employers) in 2004. The statements' objectives are to establish uniform standards of financial reporting by state and local governmental entities for post-employment benefit plans other than pension benefits (OPEB plans). This includes post-employment health care benefits such as the one provided to North Dakota pre-Medicare retirees. Pursuant to these statements the State must report the present value of this implicit subsidy as a footnote on the State's financial reports. The most recent valuation put this amount at $65.2 million. If this bill is adopted, PERS would no longer offer this coverage. Consequently, this liability would be substantially eliminated and, therefore, would not appear on the financial statements.

The second aspect of the implicit subsidy is that in the near term (the cost for one year) the actuarial difference in the cost is applied to the active contracts in the plan. The estimated cost of this to the active contracts in the plan is about $2.46 per contract per month on premiums for 2013-15. Again, if the provisions of this bill are approved, this cost would no longer be applied to the active contracts in the plan. In the fiscal note, we assumed that this would reduce the active health insurance coverage by about half of this amount in 2015-17. We would expect that by 2018 nearly all pre-Medicare members would be off the health plan and this entire savings would then be reflected in the active premiums.

While the provisions of this bill would result in the above two savings for the employer (no longer having to report the present value of the subsidy on the states financial statements and the subsidy being reflected on the active rates), what about the effect on retirees? First, as mentioned at the beginning, this coverage was offered to pre-Medicare retirees to insure they had access to coverage when they retired. Due to the passage of the Affordable Care Act (ACA), there are provisions in the bill that provide access to insurance without having to be concerned with being medically underwritten or having pre-existing condition provisions. Consequently, the primary reason that PERS offers this coverage to this group may no longer apply. Additional advantages for the pre-Medicare retirees to access coverage through the new health care exchanges may be:

- Possible subsidies for coverage
- More selection of plans

The primary disadvantage to our pre-Medicare retirees is that at this time the PERS Retiree Health Insurance Credit is not portable, so they would lose that benefit by going to the health care exchange. That is why Sections 2 & 3 of this bill are proposed. You

will note, however, that the effective date of this act is not until July 1, 2015 (Section 4, page 7). The reason for this is to allow us enough time to confirm our understanding when the Affordable Care Act provisions are implemented in 2014. If our understanding proves to be incorrect, then corrective provisions can be proposed to the 2015 legislative session before we stop offering non-Medicare coverage. The advantage of passing the bill at this time is that we will see the present value cost on the financial statement's reduced.

SECTIONS 2 & 3 – RETIREE HEALTH CREDIT PORTABILITY

In 1989, the North Dakota Legislature started the Retiree Health Insurance Credit Program (RHIC). The purpose of this program was to help retirees offset the cost of health insurance. It was recognized at the time that the cost of health insurance was becoming increasingly unaffordable. The monthly benefit formula and benefit paid information is:

BENEFIT FORMULA:

$5 for each year of credited service

Example: $*5 x 25 years = $125*

During the last year, the program paid out the following benefits:

BENEFITS PAID

Average benefit: $118 per month to 4,442 members

This program is presently funded by a 1.14% contribution from payroll.

Presently, this benefit can only be used to purchase PERS retiree health insurance coverage.

If the provision in Section 1 of this bill alone was passed, it would mean that pre-Medicare retirees would not be able to participate in the PERS health plan and would lose this benefit. Consequently, the proposal in Sections 2 & 3 would make this coverage portable for any health insurance coverage and also allow it to be used for the PERS dental, vision, prescription and long term care coverage. This provision adds the portability feature for not only pre-Medicare retirees but also Medicare retirees.

During the interim study of this bill by the Legislative Employee Benefits Committee, it was noted that the cost of making this coverage "portable" would be .19% of payroll, and the cost of the existing program is .90% of payroll. Adding the cost of existing coverage and the portability provision would result in a total cost of 1.09%. The existing contribution is 1.14% which means that the portability provision could be added without the need to increase contributions.

Summary

As noted in the beginning of this testimony, this bill does two basic things:

1. Closes the PERS Health Plan to pre-Medicare retirees on July 1, 2015 (Section 1). As discussed above, this will eliminate the implicit subsidy associated with offering this coverage, which consists of a present value of about $65 million, thus reducing that amount on the state's financial statements. In addition, this change will reduce the active rates in the future by the annual implicit subsidy cost of about $2.46 per contract per month.

2. Makes the retiree health insurance credit portable. While this will increase the cost of this program based upon the most recent actuarial valuation, the additional cost can be paid within the existing contribution.

Both the employer and retired employees benefit from the provisions of this bill. The employer gets rid of the implicit subsidy costs. The retiree gets more flexibility for using the health credit.

This bill was reviewed during the interim by the Legislative Employee Benefits Committee and received a favorable recommendation. In addition, the PERS Board requests your favorable consideration of the bill.

Mr. Chairman, this concludes my testimony and thank you.