Retiree Health Benefit Program Consultation

CUCSA

September 7, 2017

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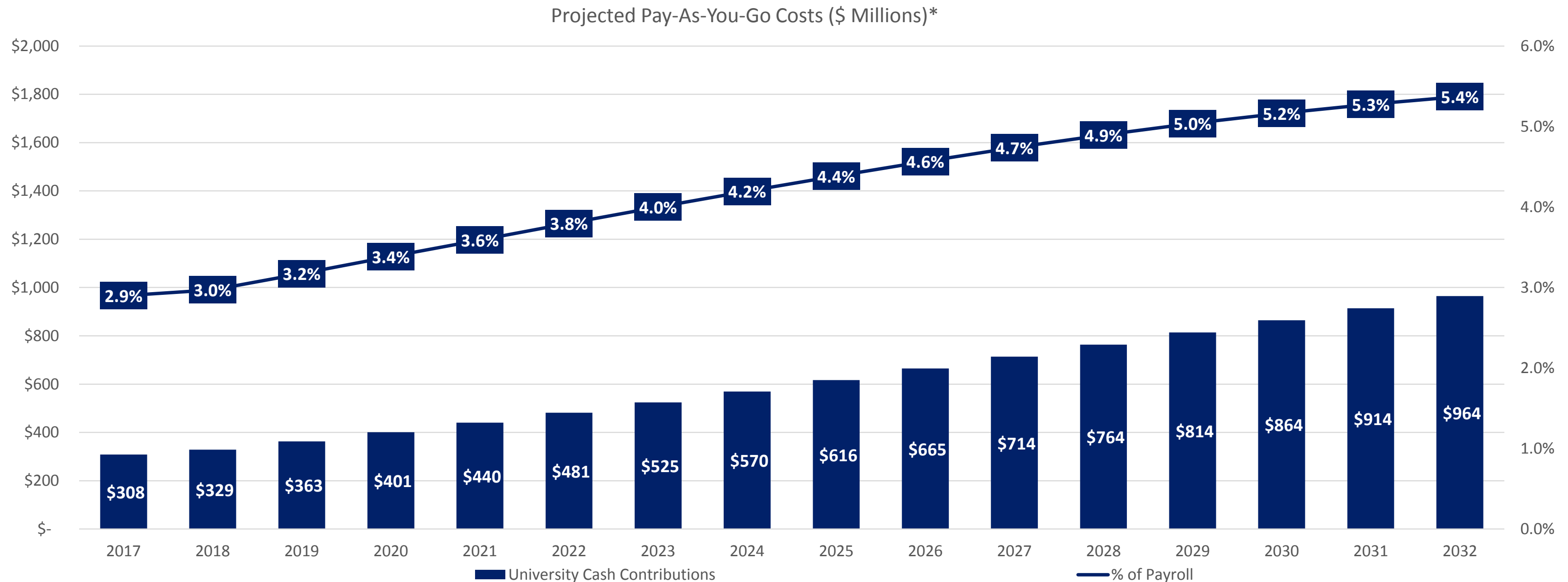
Executive Summary

- The University currently spends approximately $300 million per year on retiree health benefits for 43,000 UC retirees and survivors. The Retiree Health Benefit Program has a $21.2 billion unfunded liability as of July 1, 2016.
- For 2018, the UC contribution will increase by 7.2%, or $19.6 million dollars
- The current and projected cost increases are greater than inflation and are growing faster than the University's budget
- The Regents policy implemented in 2010 helped slow anticipated growth of University pay-as-you-go costs, which have been held nearly flat for the past five years; however, a new policy is needed to address future UC cost growth
- The current policy steadily reduced the University's contribution to 70% of aggregate premiums. The 70% level for the University's share was reached for pre-Medicare in 2015 and will be reached for Medicare retirees in 2018.
- A budget target for University contributions to the Retiree Health Benefit Program will provide cost predictability for the University's operating budget. There is currently a budget target for the University contributions for the active health and welfare program.
- A budget target, combined with programmatic changes, could slow the growth in operating costs and would significantly reduce the unfunded liability, thus helping sustain the program well into the future
- While a budget target and adjustment to the floor will provide cost certainty to the University, we realize that this will result in greater cost uncertainty for our retirees, with greater year to year fluctuations.
- We know how important health benefits are to our retirees, and although UC retiree health benefits are not a vested or guaranteed benefit, we are sensitive to the potential impacts on retirees as a result of cost and plan changes. UC Human Resources, in partnership with UC Health, will continue to manage the program and plan design to keep costs down and to deliver a choice of quality benefits that are also affordable.

The University "Pay-As-You-Go" cash contributions are expected to increase as a percent of payroll

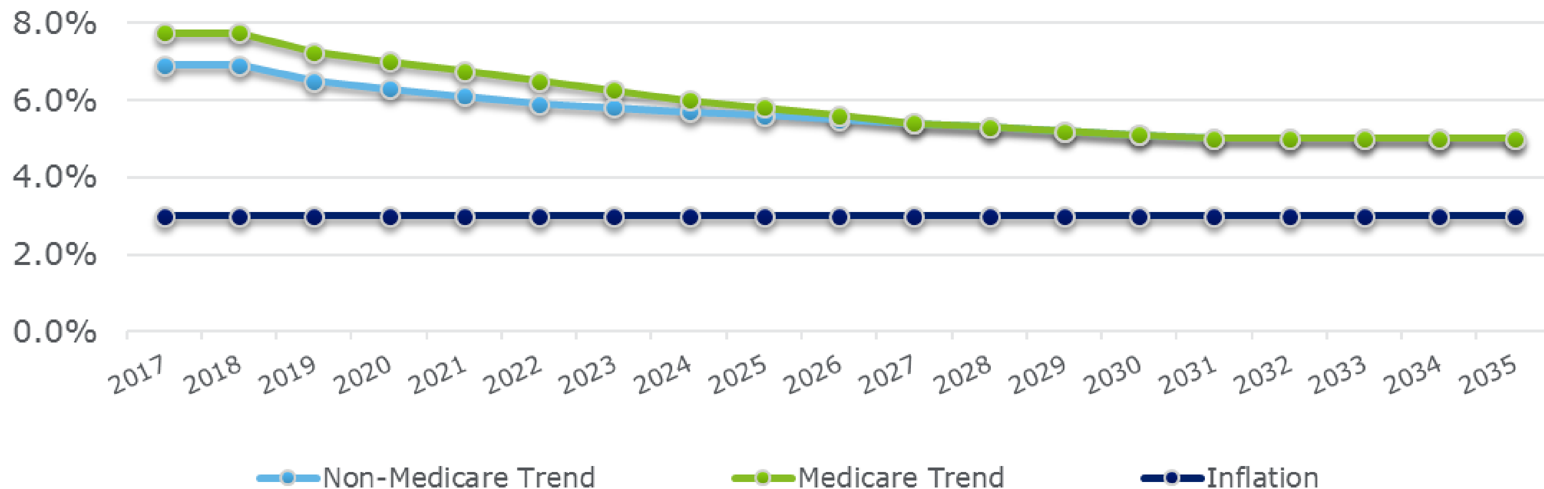
- The University **"Pay-As-You-Go" cash contribution** requirements are expected to escalate more quickly than price inflation
  - Increase is driven by UC's retiree health costs, which are projected to grow at the **medical trend rate (currently at ~7%)**
  - Increase is also driven by our **growing retiree population**
  - Combined impact of these two drivers could cause a greater portion of annual budget growth to be **diverted to fund retiree health costs rather** than to fulfill the mission of the University



**Based on total payroll projections provided by Segal (includes 0.7% employee headcount growth)*

Medical trend is expected to be notably higher than price inflation

- Plan costs are expected to increase over time due to **growing retiree health population** and **expected future medical inflation (trend)**
  - Medical trend is a significant driver of future pay-as-you-go costs
  - Medical trend is expected to be notably higher than price inflation
- The chart below illustrates the current assumption for medical trend compared to price inflation



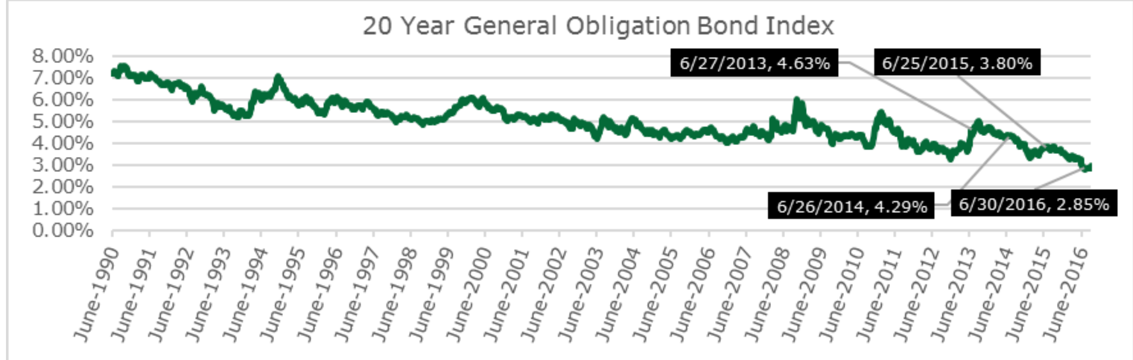
- Since medical trend is higher than the anticipated growth of revenue, the retiree health program could divert monies from other operational needs if additional efforts are not made to manage costs

New accounting standards have highlighted the long-term costs of retiree health benefits

Changes in how Retiree Healthcare (OPEB) liabilities need to be reported on financial statements has highlighted the size of the unfunded obligation.

GASB Changes – Reporting Benefit Liabilities

- Effective FYE June 30, 2017, the University will report retiree health liability under GASB 75
- Similar to recent accounting changes for pensions, under GASB 75 the entire net OPEB liability must be reported on the face of the financial statements rather than in the footnotes
- The new GASB 75 standard requires the discount rate for pay-as-you-go plans to be determined based on the index rates for a 20-year General Obligation Bond, which were at historically low levels at 6/30/2016
- The index rate at 6/30/2016 was 165 basis points lower than the assumed return on the University's assets, which was the basis for discounting liabilities under the prior accounting standard
- The decrease in discount rate increased the GASB liability by $5.0B*
- The liability is highly sensitive to the index rate; as noted in the table below, the index has increased 73 basis points as of 6/30/2017, which would have reduced the 6/30/2016 GASB 75 liability by $2.4B
- GASB changes have ***no impact on the University "Pay-As-You-Go" cash contribution requirements***



Discount Rate	*2.85%*	*3.58%*	*4.50%*
Basis	Index Rate – 6/30/16	Index Rate – 6/30/17	STIP/TRIP return
6/30/16 Liability	***$21.2B***	***$18.8B***	***$16.0B***

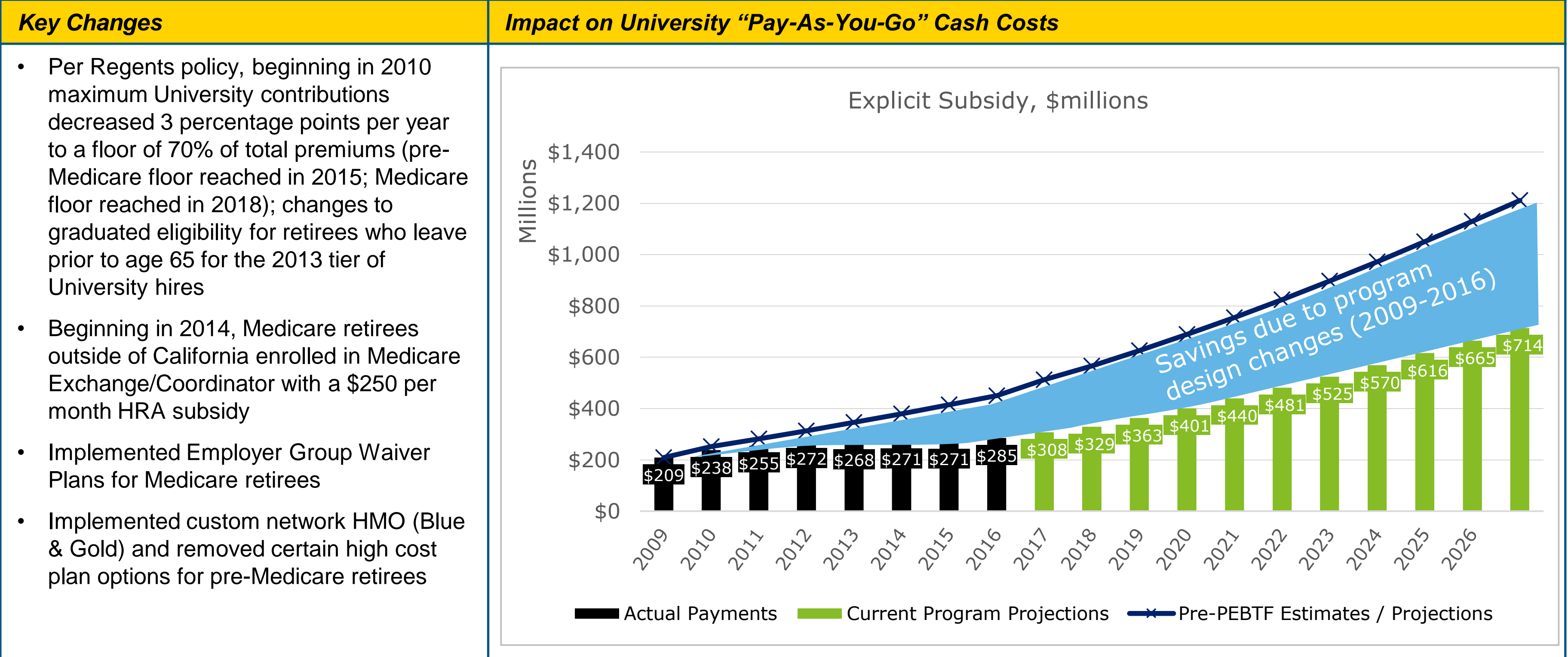
1% increase in discount rate decreases liability ***$3.3B***

Liability reflects Campus, Medical Centers, Hastings and Other (CMCHO)

Regents policy implemented in 2010 and recent program changes have slowed growth in costs

- Recent program changes have helped slow anticipated growth of pay-as-you-go costs which have been held nearly flat for the past five years

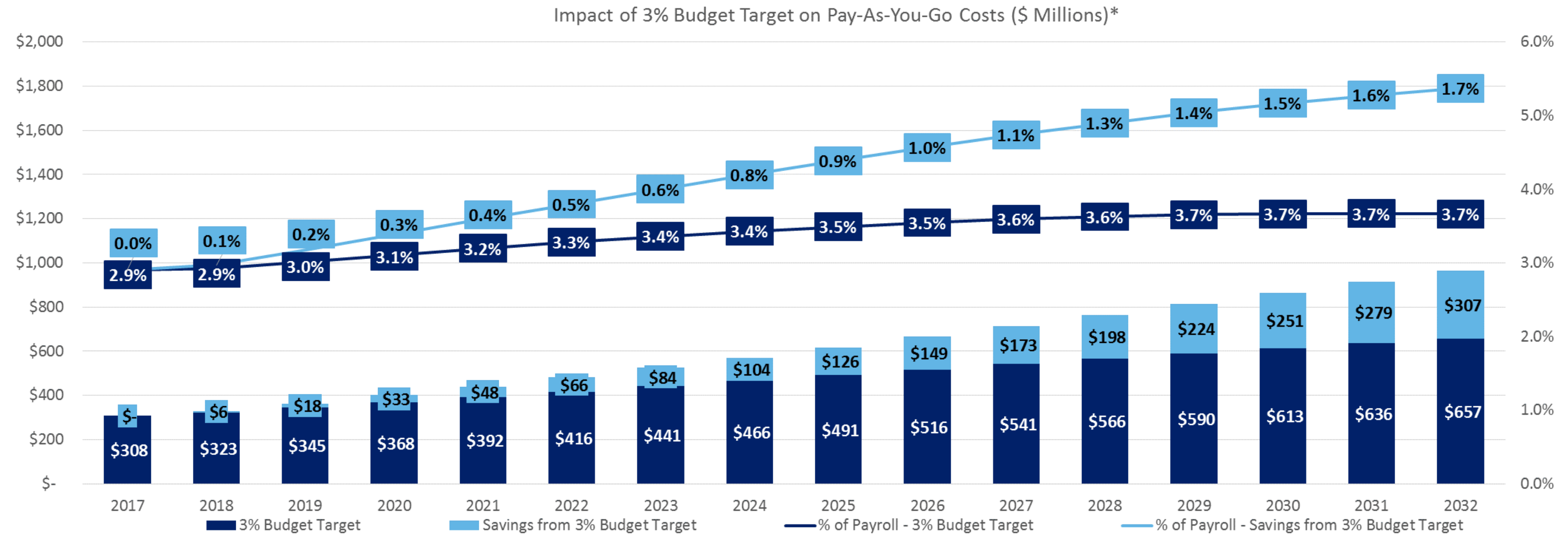
- Below is a graph comparing ongoing University “pay-as-you-go” cash costs to the projected costs of the program as it existed before the 2010 PEB Task Force Recommendations



Despite recent changes, there is still a long tail for the future cash requirements of the program driven primarily by the Medicare eligible population.

Implementing a 3% budget target is consistent with the University's long-term price inflation assumption

- Baseline University "Pay-As-You-Go" cash contribution is expected to grow more quickly than payroll
  - Medical trend and retiree headcount growth is expected to outpace wage and employee headcount growth
  - In 2032, cash contributions are projected to be 5.4% of projected payroll (~85% higher than current % of payroll)
- Implementing a 3% budget target is projected to keep University cash contributions closer to current levels as a percent of payroll
  - In 2032, cash contributions are projected to be 3.7% of projected payroll (~30% higher than current % of payroll)



*Based on total payroll projections provided by Segal (includes 0.7% employee headcount growth)

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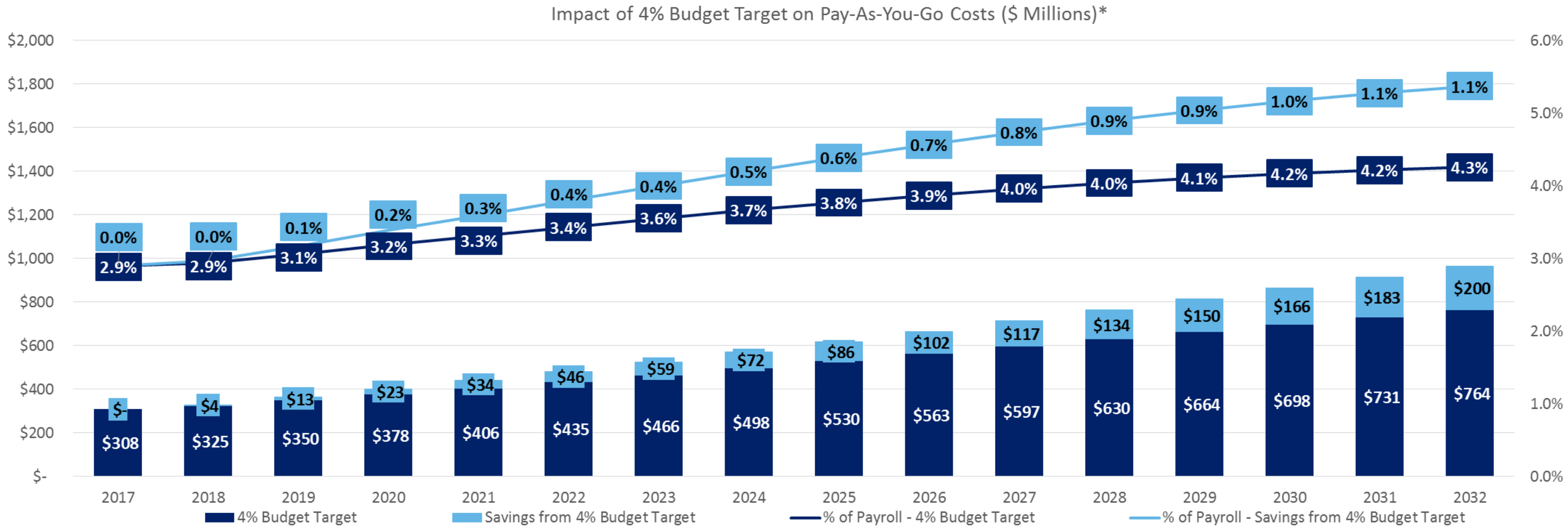
Projected University "Pay-As-You-Go" Cash Contributions – Impact of 4% Budget Target

- Baseline University "Pay-As-You-Go" cash contributions are expected to grow more quickly than payroll
  - Medical trend and retiree headcount growth is expected to outpace wage and employee headcount growth
  - In 2032, cash contributions are projected to be 5.4% of projected payroll (~85% higher than current % of payroll)
- Implementing a 4% budget target is projected to steadily increase University cash contributions as a percent of payroll
  - In 2032, cash contributions are projected to be 4.3% of projected payroll (~50% higher than current % of payroll)



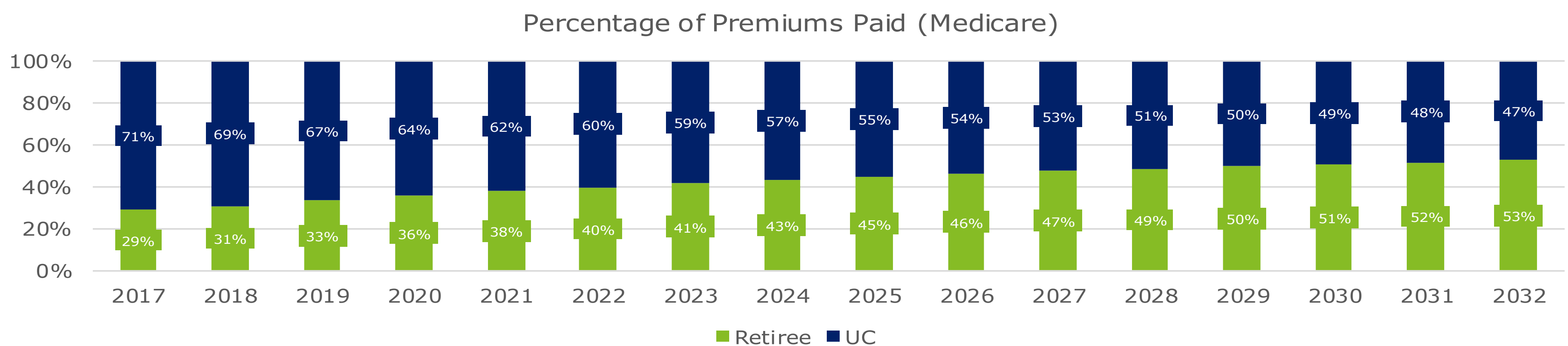
*Based on total payroll projections provided by Segal (includes 0.7% employee headcount growth)

A budget target will provide cost predictability for UC and shift costs above the target to retirees

- A 3% or 4% annual budget target of per capita University contributions is a means of controlling cash contribution requirements and obligations by directly addressing the rising costs associated with medical trend.

How a 3% or 4% Budget Target Would Work

- The University will share in the payment of rate increases up to the 3%/4% budget target. Rate increases above the budget target will be borne by the retirees.
- In years where medical trend is greater than the budget target, and barring other plan changes, retirees would pay an increasing portion of plan costs.
- HR would be responsible for implementing plan changes designed to achieve the budget target while mitigating the adverse impact on retirees.
- The University would need to determine if there would be any exceptions to those impacted by the budget target (e.g., retirees over 65 not eligible for Medicare)
- The graph below provides an illustrative projection of the share of Medicare premiums paid by UC and retirees assuming a 3% budget target is implemented in 2018 without any plan changes and medical trend grows at the rates previously noted.



This chart projects the aggregate portion of premiums paid by Medicare retirees receiving the full University contribution (i.e. 100% graduated eligibility).

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Pre-Medicare Retiree Contributions with 3% or 4% Budget Target

Pre-Medicare Retiree Impact

The table illustrates how a 3% or 4% budget target could impact pre-Medicare retirees five years after implementation (2022) under a range of rate increase environments. This example compares monthly rates for pre-Medicare retirees with and without a budget target for the most affordable (Kaiser) and most expensive (UC Care) plans.

Key Assumptions

The following assumptions were made in projecting costs for this illustration:

- Premiums applicable for Calendar Year 2017
- Participant has single coverage
- Eligible for 100% of the maximum University contribution
- Medical trend is projected at ~~a~~ low (3.5%), medium (6.0%) and high (8.5%) annual increase levels

Active vs. Pre-Medicare Retiree (Monthly Rates - Single Coverage)		**2017**			**2022 Low - 3.5%**			**2022 Medium – 6.0%**			**2022 High – 8.5%**		
		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions	
Medical Plan	Budget Target		University	Member		University	Member		University	Member		University	Member
UCCare	No Budget Target	$ 754	$ 476	$ 278	$ 895	$ 566	$ 329	$ 1,009	$ 638	$ 371	$ 1,134	$ 715	$ 419
	4% Budget Target					$ 566	$ 329		$ 579	$ 430		$ 579	$ 555
	3% Budget Target					$ 551	$ 344		$ 551	$ 458		$ 551	$ 583
Kaiser	No Budget Target	$ 604	$ 476	$ 128	$ 717	$ 566	$ 151	$ 808	$ 638	$ 170	$ 908	$ 715	$ 193
	4% Budget Target					$ 566	$ 151		$ 579	$ 229		$ 579	$ 329
	3% Budget Target					$ 551	$ 166		$ 551	$ 257		$ 551	$ 357

Medicare Retiree Contributions with 3% or 4% Budget Target

Medicare Retiree Impact

The table illustrates how a 3% or 4% budget target could impact Medicare retirees five years after implementation (2022) under a range of rate increase environments. This example compares monthly rates for Medicare retirees with and without a budget target for the most affordable (Kaiser) and most expensive (High Option) plans.

Key Assumptions
The following assumptions were made in projecting costs for this illustration: • Premiums applicable for Calendar Year 2017 with standard Part B premium ($121.80) • Participant has single coverage • Eligible for 100% of the maximum University contribution • Medical trend is projected at a low (3.5%), medium (6.0%) and high (8.5%) annual increase levels

Active vs. Medicare Retiree (Monthly Rates - Single Coverage)		**2017**			**2022 Low - 3.5%**			**2022 Medium – 6.0%**			**2022 High – 8.5%**		
		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions	
Medical Plan	Budget Target		University	Member		University	Member		University	Member		University	Member
High Option	No Budget Target	$ 539	$ 328	$ 211	$ 640	$ 389	$ 251	$ 721	$ 439	$ 282	$ 811	$ 493	$ 318
	4% Budget Target					$ 389	$ 251		$ 399	$ 322		$ 399	$ 412
	3% Budget Target					$ 380	$ 260		$ 380	$ 341		$ 380	$ 431
Kaiser	No Budget Target	$ 374	$ 328	$ 46	$ 444	$ 389	$ 55	$ 500	$ 439	$ 61	$ 563	$ 493	$ 70
	4% Budget Target					$ 389	$ 55		$ 399	$ 101		$ 399	$ 164
	3% Budget Target					$ 380	$ 64		$ 380	$ 120		$ 380	$ 183