MEMORANDUM

TO: Ken Wilbur

FROM: L. Mason Neely, CFO

DATE: February 29, 2016

RE: Pension Payments

Thank you for your quick response to my February 18, 2016 memorandum. I appreciate the thoroughness by which you have responded. As I have indicated before, I believe the Pension & Benefit Study Commission has performed great services to the State of New Jersey by highlighting the problems which currently exist and detailing the fiscal cliff which confronts the tax paying public. I do believe it would be advantageous of all residents of the State to resolve the deficit funding confronting the Governor and Legislature. To this extent I wish to see change take place.

PART I

The report produced in 2016 by the Pension & Benefit Study Commission represents a snapshot in time. We all understand the New Jersey Income Tax was approved based upon the concept it would be used for property tax relief. Also you should understand, local revenues which belonged to local municipalities, such as Business, Personal Property Tax, Gross Receipt Taxes and other taxes were taken from the local property tax base by the State Legislature using the term “Reform” and “Property Tax Relief”. The State told everyone centrally collecting of those revenues and then redistributing them to the various communities, would be “Fairness”. The tax would be a uniform rate and everything would be “equal and fair”. In fact what happened was the State changed the law, collected the revenue and kept the funds past the fiscal year. Then after it was taken by the State, instead of being distributed back to municipalities. The State keeps short changing the promise. See the link to the League’s White Paper on this issue http://www.njslom.org/energy-tax-paper.html .

Subsequent payments have continuously shrunk and municipalities have not received the promised distribution of the local revenue, which was collected centrally so there would be *“Fairness” and “Equity”*. What has happened, was once the State saw the pot of money they kept taking greater portions, and did not redistribute money back to the municipalities. Had the State not ever undertaken the “Reforms” the local governments would have been collecting those revenues and they would have never flowed into the State Budget.

Therefore, when the Commission begin to talk about $16.8 Billion of the State Budget used for property tax relief it is simply a fact those revenue from the very onset were to be dedicated to local property tax. The State has continuously dipped into the growth which resulted from the promised distribution and efficiency. Because of this lack of follow-through on promises the Commission can understand local governments are skeptical when the Commission start using terms such as "*Fairness*" and "*Reform*" as our perspective is based upon having been jilted every time the State makes a promise. Look at all the empty "Trust" funds and see the per-capita debt.

New Jersey teachers may feel the same in regards to pension and health benefits. A promise was made and then funding was not realized and now the teachers have a crises, that all must solve. However, the Commission happily pointed out in their 2015 Report, it accomplishes nothing to be acrimonious as to what has gone on in the past or to try and point fingers at guilty parties. Therefore, I simply write the first section to provide amicable perspective. The State has an issue which must be addressed.

<u>PART II</u>

Thank you for clarifying the Commission believes there will be sufficient savings resulting from health benefit modification to cover all of the pension costs. The pension system will not be impacted by "Reform" at this time. If one were to really look at solving problems, one might want to look at the "Prevailing Wage Law", as it is neither the prevailing wage nor the market wage and it skews the cost of all Government Projects. This and the right to work which guarantees the Unions with a political pocket of funds further impacts problems within the State. However, none of these issues are on the table at this point so I will look only at the Health Benefit Issue.

I would suggest the Commission look beyond the gross numbers which as projected show current cost for employers. Pre and post reform the reported savings column should also show pre-capita cost. It is my suspicion the school systems have a much higher per-capita cost for health benefit coverage then the majority of local governments. Therefore, would it be possible to show per-capita cost also?

I question savings for municipal retirees. How are projected savings to be realized? How do we abrogate contractual agreement which municipalities have between their retirees in order to accomplish savings? This questions would then flow to the State of New Jersey under the State Health Benefit Systems as how to abrogate the early retirees and the other retirees agreements. How would one abrogate the contractual agreement to permit a change in the level of benefit and a cost for same?

If locals were ready to agree to the degree of change as suggested by the Commission, how would locals be protected at future date if the state decides to dip into the purported savings which may result? The wording of the law or constitutional amendment is of vital importance and locals would like this information shared with participants so we could all feel comfortable with the promises made will actually be kept, as opposed to a pending next election.

The concept of a Private Exchange is attractive, as we all understand the ACA exchanges set up under Obamacare have been failures resulting in non-qualified people being registered, wrong subsidies being provided and promises made which were unrealistic. At the same time we are seeing a proliferation of new drugs hitting the market which does not bode well for cost containment.

The following table reports the industry's top ten drugs for 2016 and the projected gross revenue associated with these drugs.

TOP TEN DRUGS BY ESTIMATE SALES IN 2016			
Estimated Cost	**Drug**	**Use**	**Generic**
$12.54 Billion	Humira	Arthrits	No
$6.4 Billion	Crestor	Cholesterol	No
$2.6 Billion	Benicar	Blood Pressure	No
$2.6 Billion	Zetia	Cholesterol	No
$1.3 Billion	Seroquel XR	Schizophrenia/Bipolar	No
$1.2 Billion	Aciphex Sprinkle	Acid Reflux	No
$1.1 Billion	Epzicom	HIV	No
$1 Billion	Kaletra	HIV	No
$962 Million	Norvir	HIV	Yes
$493 Million	Ambisome	Anti-Fungel	No

It is frightening to realize the growth of drug related cost associated with any health benefit program. For this reason we are somewhat skeptical of the projected savings which the Commission has reported. While there may be savings immediately, when one changes from the current level of coverage to what is referred to as the ACA Gold Plan. However, containment of those costs over time can be a significant problem. We have that issue now but the commission wishes to layer costs from the State onto the local tax payer.

SHBP prescription drugs via the latest audit ended the year with a negative $141.7 Million Dollar loss. Compared to the local government participating in the State Health Benefit System, which ended the fiscal year with $257.4 Million Dollar balance. If a regulated insurance company were to run a consistent negative balance of over $100 Million Dollars a year the Division of Banking and Insurance would shut them down. However, for the State of New Jersey the unthinkable has become routine. A number of reports written on the economy of the State of New Jersey have indicated the State cannot borrow its way out of debt, it cannot tax our way out of negative balances and they cannot continue the masking the ballooning liabilities that must be confronted. The reports from the Pension & Benefit Study Commission have major suggestions on how to begin the process. Who else is taking part in the review of issues?

LMN/iws

cc: Lori Buckelew, League of Municipalities
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Saved: filed saved/mydocs/benefits&payroll/pension/memorandum