**MEMORANDUM**

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| **TO:** Lori Buckelew — League of Municipalities  Mike Drulis — GFOA  John Donnadio — County  Tom Cavroll- Manager  **FROM:** L. Mason Neely, CFO, Township of East Brunswick |  |

**DATE:** February 18, 2016

**RE:** Thoughts on the Supplemental Report on Health Benefits by the New Jersey Pension & Health Benefit Study Commission" dated February 11, 2016.

The Commission has certainly formed qualified service to the public of the State of New Jersey in particular with the issuance of their three reports which have highlighted the fact the elected officials have permitted a crises to develop and seem unwilling to fully address the issues. A time bomb is ticking which will soon go off, if there is no corrective action taken.

Issues regarding the Commission's Health Benefits Report:

1. The Commission sets up a "Straw Man" called the "private sector" and then measures all of their suggested modifications against the "Straw Man". We all recognize the private sector is a generic term, which includes a broad range of situations and therefore to use it as a model against which one compares is questionable. It is a fact of need not fairness so don't pit public vs. private.
2. The Commission uses the term "reform" when in fact what they mean is to reduce the level of benefits and modify the quality of the benefits to shift the cost to employees who are now receiving those benefits. They as well plan to shift the State cost in part to the property tax base.
3. The Commission should be given high quality marks for their innovation, for the diligence by which they have addressed the subject and for coming to viable solutions to end the "Death Spiral" of Pension, Health Benefit, debt payments and Trust Fund costs, which have developed under the current and prior Governors and Legislature.
4. The Commission is recommending the pension system should be frozen, as of a certain date and a modified "Defined Benefit System" established with funding at the source level, rather than at the State level for Teachers Pension and Annuity Fund (TPAF). That suggestion remains on the table and seems to be a viable solution for partial repair of the problem.
5. The Commission clearly demonstrates the most costly sector when providing Health Benefits to active and retired employees is to the category of employee identified as "Early Retiree" (Note Exhibit 10 on Page 13 of the Report). This

**identified group is 44% more costly than "Active Employee" or and 63.5% greater than "Medicare Retiree's 65 years or older". What the commission neglects to consider is changing the retirement age for the PFRS pensions system by increasing the time one would become eligible for post-retirement benefits. This option seems to have eluded their report and there is no dialog on changing this age of retirement. *However, they do point out the vast majority of those who retire early begin a second career and have a second livelihood. Therefore, they are receiving a pension, keep working and receiving a full income from a second career while receiving free health benefits paid for by their government employer* from whom they took early retirement. Thus, they receive a full pension and they receive paid medical benefits. How does this compare to the "private sector"? "rare and getting rarer nationwide" Page 13.**

1. **The Commission recognizes the State cannot tax its way out of the situation nor can it borrow sufficient funds to bridge a period of time when solvency could reoccur. The answer is to reduce the level of benefits and require employees**

**to contribute a larger amount including those that have retired. The
  
Commission's Report clearly identifies a cap must be placed on the level of benefits provided and certain benefits cannot be preserved. As such the Commission uses the term "Fairness" because they recognize the problem is resonates with the State Government as they have not funded their pension obligation and they have provided post-retirement benefits for which there have been no reserves established. The State agreed for various political reasons to fund the Teachers' Pension Annuity and Health Benefit costs and called it "Property Tax Relief". How is that working today as the UAL grows $10 Million each day? The State has a developed a problem and the Commission uses the term "Fairness" so they can share the burden with all of the Municipalities Counties and Authorities that have paid their pension obligations timely and have managed to fund their health benefit obligations. So the term "Fairness" and "Comprehensive Reform" really mean lowering the quality of health benefit coverage and spreading the method of paying for such so the required contributions by those receiving health benefits must increase in order to resolve the State funding issue. The idea is to cast the net out over those who have not caused the problem and then use words like *"Fairness", "Comprehensive Reform", "Tax Relief'* to mask the screw-up.**

1. **The Commission adequately identifies the fact the State Pension Debt obligation is *increasing by $10 Million Dollars every day.* Footnote #29 is worth fully reading and understanding.**
2. **The Commission recognizes the current health benefit level provided broadly across all levels of Government exceeds the "Private Sector" by a significant amount. This is resulting because of collective bargaining system been permitted to develop because Legislatures have been unwilling to curb the collective bargaining process. They don't report how much Public Sector Unions have spent each election cycle to keep the system in place. Now the revenue problem is so dramatic and the potential risk so great it is believed that only quick and decisive action to modify all contractual obligations which will provide sufficient funding to stabilize pension obligations and to permit a gold level of standard under the Affordable Care Act (ACA) going forward. The**

**Commission would want one to believe that both employers and employees would see savings as a result of the two prong approach they are recommending. However, when you look at the employers premium contribution plus the increase out-of-pocket costs overlaid by the fact that the level and quality of coverage will diminish there is no misunderstanding the employees are expected to pay a major portion of the cost associated with funding the Pension and Health Benefit Plan. This appears to be a responsible expectations because without direct action both the Pension and the level of Health Benefits may be completely at risk. The question their asking is, "Do you wish to have some of the apple left or do you wish to let the whole thing rot and go away because of inaction?".**

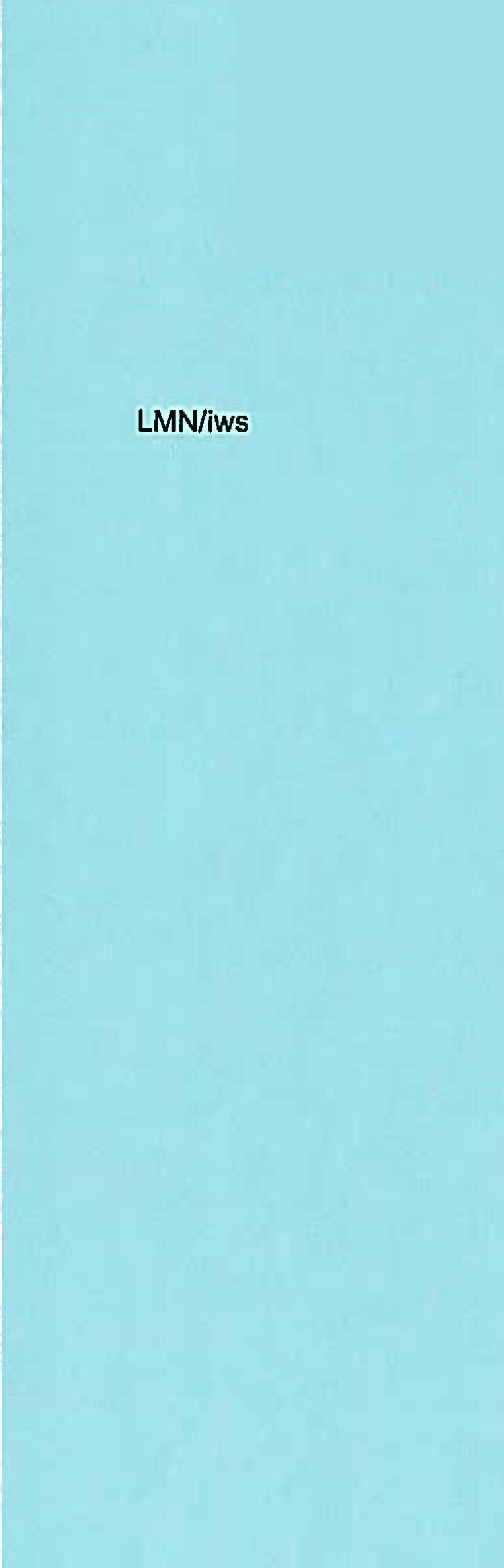
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1. **The Commission makes a valid point, modifications to the Health Benefit Program such as eliminating or modifying balance billing as well as changing the actuarial value of programs offered will happen by increased cost to the employees; however, those costs must be weighed against the protection of** a **pension system which is a lifetime annuity many are looking forward to and in fact depending upon.**
2. **The Commission's reported savings result by modifying the health benefit system rest primarily at the local level. Of the $11.8 Billion which represent expected savings. $8.1 Billion of that is local government dollars, i.e. property tax dollars. Those property tax dollars are used to fund the Pension and Benefit obligations which the State has developed. The Commission happily points out those are not new dollars, because the cost of the benefits are currently built into the property tax rate. Therefore, by lowering the level of benefit, changing assumptions, requiring modifications, the cost of Health Benefits will diminish and the delta between the newly diminished benefits and the existing tax rate could then be applied to fund the Teachers Defined Benefit Program that would be shifted from the State to the Local Level. Thus there is no question, the State is pushing its obligations onto the property tax payer, however, at this point in the crises, there appears to be little choice.**
3. **A large portion of the expected savings are speculative in the nature to say the least. The PILOT program of the Primary Care Medical Home (PCMH) Program are not known, the Program is not tested and the acceptability of the system is questionable. Coupled with that question, is the Private Exchange which is to be established. Are benefits from having a private health network exchange such potential for out years real. It depends upon how much political game playing will occur in who gets the contract for the Private Exchange and how well the Private Exchange is run. Date as of today only smaller companies are using a private exchange. Overlaying all of this is the ACA Cadillac Tax threshold, which is the cap at which government funded benefits are to be provided. If benefits cost more than the Cadillac Tax limitation then it is most likely those costs will flow to the individual employee. It seems the Commission is willing to sift all of the risk from the State to the employees.**
4. **The Commission did not have available all of the information from local governments and it recognizes that some local health programs are more efficient than others. Therefore, there will be a variation in degree of cost reductions that a municipality may see. Overall they have made the**



**assumption that the local property tax will have net zero impact, as the local portion of the tax will decrease and the portion funding education will increase.**

**They are asking the Local Governments to take the risk off the State.**

**13. The overall report may be summarized by the following quote on Page 15, which reads, "overall the proposed approach for continuing coverage to early retirees would generate $310 Million in savings of which, member costs would rise by only $90 Million". The Commission suggest that members would pay an additional $90 Million Dollars of cost while having a decreased level of coverage does not recognize the members are in fact covering the entire amount of $310 Million Dollars reduction which may result if the proposals in the report were adopted. The proposal is to shift all of the cost of the States liability onto lesser quality of coverage, lesser freedom of coverage and higher employee contribution as the local tax rate is placed at risk for out years if the suggested reductions do not materialize. It does appear all of this is necessary but it should be clear as to what is taking place.**

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