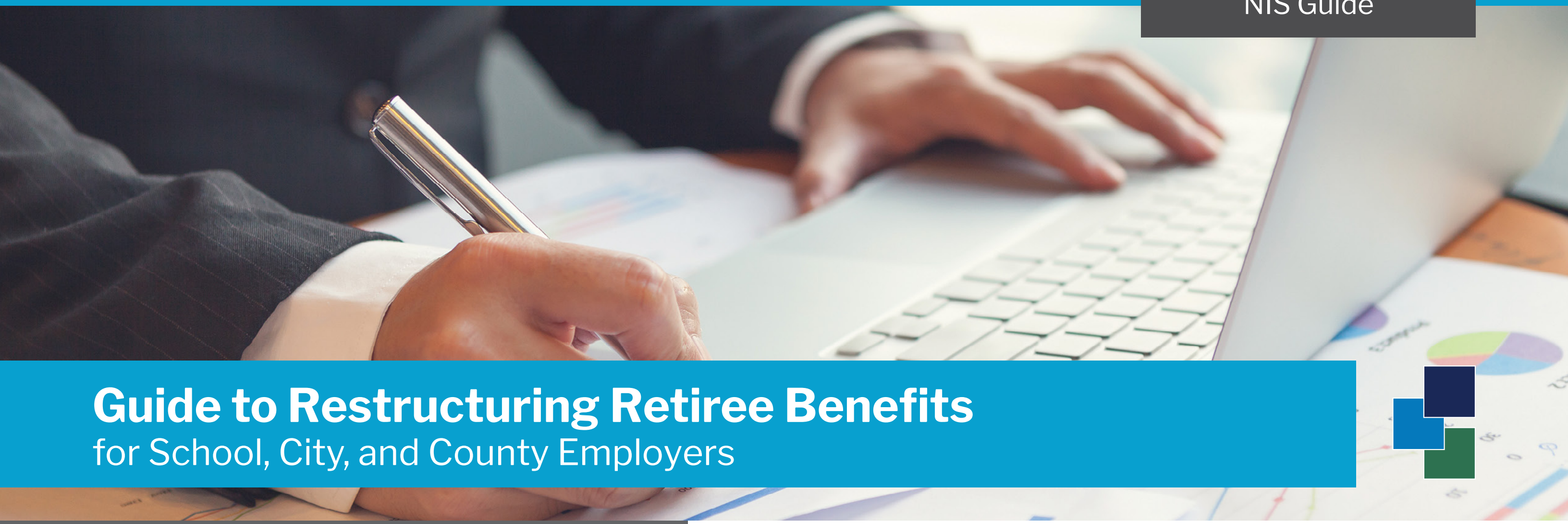
NIS National Insurance Services

NIS Guide



Guide to Restructuring Retiree Benefits

for School, City, and County Employers

Quick Reference:

	Page:
Step 1: Assess	02
Step 2: Choose a Partner	03
Step 3: Inform Stakeholders	04
Step 4: Form a Committee	05
Step 5: Benchmark	06
Step 6: Restructuring Options	07
Step 7: Evaluating the Costs	08
Step 8: Finalizing the Plan	09
Step 9: Implementation and Education	10

Why Restructure Your Retiree Benefits?

If you are reading this guide, chances are you have already identified an unfunded liability or OPEB (Other Post Employment Benefits) liability, or at least are thinking about how to save on benefits costs for your school, city, or county organization.

Because of unprecedented rate increases, the practice of providing traditional health insurance benefits to early retirees has become financially untenable and can affect an organization's financial sustainability. The good news is that restructuring your retiree benefits now can help ensure sustainability, as well as help maintain your commitment to employee satisfaction and retention.

In this guide, you will find helpful steps to identify your needs, assess costs and funding options, explore restructuring solutions, and implement your new plan.

Moving from a Defined Benefit Plan to a Defined Contribution Plan

There are two main models for retiree benefits: a defined benefit plan and a defined contribution plan. When seeking to eliminate your unfunded liability — short of eliminating the retiree benefit altogether — you will generally need to move from a defined benefit plan to a defined contribution plan.

- Defined Benefit Plan – The defined benefit approach provides retirees with a specific benefit (i.e. health insurance) over a specified time period. As health insurance costs rise, so does the cost of providing this benefit.
- Defined Contribution Plan – The defined contribution approach: Instead of receiving a specific benefit, the retiree receives a specific contribution. With this method, costs are fixed, removing the volatility of health insurance rates.

Step 1: Assess : Define the Problem

In addition, accordance with the 2004 GASB (Governmental Accounting Standards Board) requirement, public sector organizations must have an actuarial evaluation to define their unfunded liability. Certified audits depend upon this evaluation, and it should be the starting point when considering retiree benefit restructuring.

With the actuarial evaluation in hand, you have a forecast of your benefits liability. Large, unfunded benefit obligations growing exponentially may jeopardize your financial stability as an organization. It's likely that tough choices must be made.

Small changes can be made for short-term, less extreme savings or a thorough restructuring might be required. But where do you to begin, who do you include in the process and how do you decide which direction is the right one? How can you reduce or eliminate those liabilities, by what margin and where will you get the funding?

Step 2: Choose a Partner. Consider the Four Es

One of the many important decisions facing school districts, cities, and counties with ballooning unfunded liability is finding a partner who specializes in benefit restructuring. A responsible partner will make the process run smoothly and efficiently and should serve as an advisor every step of the way.

When selecting a partner, consider the Four Es:

- √ **Experience** – How long have they been assisting organizations with benefit restructuring? Do they work with public/government organizations exclusively?
- √ **Expertise** – Do they understand the specific needs of schools, cities, and counties? Are they current with the governmental landscape?
- √ **Engagement** – Will they be able to stick with you for the long term and advise you at each turn? Can they help you effectively communicate program changes to your employee pool?
- √ **Examples** – Can they provide you with success stories? What other organizations have they assisted and how?

Step 3: Inform Stakeholders

Changes of this impact can be intimidating to implement and may create a sense of unease among employees. Think of the senior level teacher who has counted on post-retirement health insurance her entire career and catches wind of a restructure to her retiree benefits, or an entry-level administrator who moved to your city because of generous retirement offerings.

How do you remain competitive enough to attract and retain talent? How do you reach an acceptable compromise between fiscal responsibility and fairness to your employee pool?

Transparency is key. The process should be inclusive so employees can feel empowered, prepared and educated. Not only will clear communication foster a sense of trust, it will help with your organization's retention efforts.

Disseminating complete information about benefit liabilities to all stakeholders will help avoid a negative turn in negotiations — or, if your organization does not have collective bargaining, it may help in successfully getting "buy-in" on the new plan.

Your benefits partner should also be able to provide you with suggestions on how best to filter down details of the necessity to restructure, whether it is through written communication or an all-hands meeting or another method catered to your structure.

Specific Suggestions:

1. **Describe the problem.** Begin by using your actuarial evaluation but simplify it. In dollars and cents, show how your current plan is unsustainable.
2. **Clarify the organization's values.** Clearly articulate the organization's values or mission and let employees know that whatever is decided will be within that framework.
3. **Emphasize inclusivity.** Let them know that you need and want their involvement in helping make the tough decisions. Feedback is not only welcome but also encouraged.
4. **Establish historical significance.** Explore the reason why the benefit was established in the first place – to assist early retirees with health coverage until Medicare-eligibility. Inform them of the desire to maintain the tradition, but that changes are imperative.

Step 4: Form a Committee

How do you get your committee involved and engaged in the discussion? One popular method, known as World Café, is to break the crowd into smaller groups, discuss and offer collective opinions, or more granular feedback, to the committee as a whole.

In addition to the World Café method, there are other established meeting styles that might be more suited to your needs. Other methods include The Circle, Open Space Technology, or Appreciative Inquiry, to name a few. Descriptions of each can be found here.

Possible Committee Members:

The Champion

This person serves as a project manager, organizes the committee, delegates work, and has a deep understanding of all aspects of the organization's employee benefits plan.

Your Consultant

Engage your partner who specializes in public sector benefit restructuring.

The Numbers Expert

This could be the Business Manager, your Treasurer, Financial Officer, Director of Finance, or someone who owns the financial side of the employee benefits plan.

Human Resources

Your HR Representative/ Personnel/Benefits Manager is crucial in choosing the right plan and the right enrollment software. S/He knows everything there is to know about which employees receive what benefits.

The Staff

We recommend at least two employee/union representatives on the team to provide input into the decision making process. They are, after all, the ones who will be enrolling on the new system you choose.

Board Member

Including a board member or other community stakeholder is always recommended.

Step 5: Benchmark

Before deciding upon any restructuring plans, you may want to consider conducting an evaluation or survey of the competitiveness of your organization's retirement benefits. That is, how does it stack up to other similar organizations? Are you poised to attract and retain talent? This step may be more important to larger organizations than smaller ones.

If you decide to move forward with benchmarking, deeply study who are the main contenders? Which organizations do your employees regularly consider when seeking employment? Equally important is where do they move to when they leave employment?

If you are competing in a non-bargained market, this is particularly crucial. While bargained regions are likely to have similar challenges and benefits (though negotiating those benefits will prove exacting enough), those without are faced with the unique task of constructing a plan that is in keeping with the times, meets or exceeds the neighboring standards, and falls within the budgetary restrictions.

Step 6: Restructuring Options

Design Sustainability While Keeping Promises

As mentioned earlier, a defined contribution plan may be a great solution that not only makes your plan sustainable but also provide retirees with flexibility in retirement. Using a defined contribution approach, you can set aside a specific amount during employment or upon retirement. The individual has access to the funds for use after retirement.

The funds the employer sets aside are placed into a tax-advantaged account. There are generally three main options for that account, and your benefits restructuring partner should be able to thoroughly assess your needs and offer informed advice on what is best suited for your organization.

Three Tax-Advantaged Account Options

As mentioned earlier, a defined contribution plan may be a great solution that not only makes your plan sustainable but also provide retirees with flexibility in retirement. Using a defined contribution approach, you can set aside a specific amount during employment or upon retirement. The individual has access to the funds for use after retirement.

The funds the employer sets aside are placed into a tax-advantaged account. There are generally three main options for that account, and your benefits restructuring partner should be able to thoroughly assess your needs and offer informed advice on what is best suited for your organization.

1. **HSA:** The Health Savings Account (HSA) is one such tax-advantaged account. There are drawbacks to the HSA, however.

   During a restructuring, a client in Wisconsin considered it among their potential restructuring options and rejected it. They found that the maximum contribution levels were too low, and contributions could not be used for health insurance premiums before the normal 65-year-old Medicare age. In addition, after age 65, HSA funds cannot be used for Medicare Supplement plans and can only be used for Medicare Part B and D.

2. **403(b)/401(a):** Another tax-advantaged account is the 403(b) for schools or the 401(a) for cities, counties, and municipalities. This option is popular with workers who would prefer a plan that allows funds to be spent on anything, not only healthcare costs or insurance premiums. Employees can make contributions while employed. However, there are restrictions on the amounts and number of years they can contribute. Retirees age 55 or older have access to the account without penalties. Note that this plan is only tax-deferred, not tax-free.

3. **Retiree HRA:** By far, the biggest advantage of using a Retiree HRA is that it can be used in retirement medical expenses and/or insurance premiums both pre- and post-Medicare age. Another benefit is that there is no limit on the number of years an employer can contribute to the fund and it's completely tax-free.

   The previously mentioned client in Wisconsin was able to reduce their OPEB liability from $50 million to $0 in 9 years with the HRA, all while maintaining their commitment to employees.

Step 7: Evaluate the Costs

Before decisions can be made about restructuring plans and implementation, your committee must first figure out how to source funding. If you can't pay for a post-employment benefits overhaul, what's the point in proposing one?

Two types of expenditures should be considered:

- **Start-up costs:** Initial contribution into the defined benefit plan.
- **Ongoing costs:** Ongoing contributions. In most cases, this will be lower under the new plan than with your current one.

Most public sector organizations will have one or more of the following resources in place that can be tapped (and "sold" to stakeholders):

- **An OPEB trust:** If one exists, these funds will no longer be necessary as your liability is reduced, short- or long-term.
- **Fund Balance:** Most public sector organizations are required to maintain a fund balance. In years of surplus, remaining capital can be reallocated.
- **Savings:** Current or predictive savings can safely be used as a source of funding as an OPEB restructure will only enhance future savings.
- **Budget:** This option requires creativity in assessing expenditures and shifting overall budget allocations.
- **Borrowing:** Your bond rating may increase because of the new plan itself. Now that you are rid of the giant tax liability, your organization should be eligible for loans to fund the start-up. With lower interest rates and future budget savings, you may be able to borrow today and use future savings to repay the initial loans.

Designing a comparison chart that includes these options and the pros and cons associated with each can be accomplished with your benefits partner and will prove to be an invaluable aid in presenting your proposal to board members and employees alike.

It is also important to remember that the restructuring itself will save thousands and likely millions of dollars over the course of its implementation and will backfill much of the initial cost.

Step 8: Finalizing the Plan

Implementation involves not only deciding upon the right restructure plan and building a budget based on your findings and employee contributions; it also concerns how the plan applies to each individual employee, each employee category/tier, and establishing a timeline for implementation.

Employee Tiers

'Grandfathering in' employees who are close to retirement and honoring legacy post-employment benefits agreements is a common and mutually satisfactory method when restructuring retiree benefits. Specific terms and qualifiers can be decided among the board, administration, union delegates, and employees themselves.

Employees are likely already grouped into categories (such as administrators, support staff, and educators) and tiers (those within five years of retirement, mid career or junior level, e.g.).

Establishing the benefit levels for new or recently hired employees will prove easier among any of the tiers as they will likely just receive the new benefit. And those closest to retirement will keep the old plan. However, the most difficult group to transition is those employees who fall between new hires and those approaching retirement.

Buyout incentives, such as providing these workers with a lump sum commensurate to accumulated benefits earnings and then moving them into the new program, have historically worked. Once more, your benefits partner should be able to advise you on the best course of action.

Step 9: Implementation and Education

Employees have already been informed of the need to restructure retirement benefits. In continuance of the spirit of transparency and collaboration, it's a good time to host a meeting to share the committee's suggestions and give employees the opportunity to ask questions and contribute.

Tips for a smooth transition:

- **Restate the problem**. Describe the issue of financial sustainability and the extent of the problem. In dollars and cents, show how your current plan is unsustainable. Lay out the consequences if nothing is done to resolve the problem.
- **Explain the change.** Explain the change in detail as if there was never any prior communication. Explain that this was an organization-wide problem and how the committee determined the solution.
- **Remember transparency.** Uneasiness is increased if employees perceive they are not being told the entire truth. Lay it all on the table. Talk openly.
- **Listen.** Major changes can trouble your employees and cause negative energy in the workplace. They may also feel worried about their future retirements and concerned about affording healthcare. Take time to listen to these concerns and validate their anxiety.
- **Engage opposition.** There will always be opposition to any change in an organization. Actively engage those who are opposed to a change. You may be able to assuage their fears and assure them they are an important part of the organization.

About National Insurance Services:

Since 1969, National Insurance Services (NIS) has worked with public sector organizations such as schools, cities, counties, municipalities, libraries, and community mental health organizations providing employee benefit consulting services, as well as brokerage services for medical, dental, life, disability, and vision insurance benefits. NIS also specializes in early retiree benefit restructuring services, tax-free options for retiree payouts, as well as, on-site and near-site medical clinics.

NIS is trusted by over 2,500 public sector organizations and 500,000 insured individuals in 29 states. We are headquartered in Brookfield, Wisconsin with regional offices in Indiana, Iowa, Michigan, Minnesota, Nebraska, and Pennsylvania.

To learn more about NIS, visit our website NISBenefits.com.

You may also be interested in the following resources:

- Why Integrated HRAs May Work Better than HSAs for Schools, Cities, and Counties
- Health Insurance Rx - 5 Remedies to Slow Escalating Costs Now

NIS National Insurance Services

250 South Executive Drive, Suite 300, Brookfield, WI 53005-4273
Offices Nationwide: 800.627.3660 **www.NISBenefits.com**