



Deloitte Consulting LLP
50 South Sixth Street
Suite 2800
Minneapolis, MN 55402-1538
USA

Tel: +1 612 397 4000
Fax: +1 612 692 4681
www.deloitte.com

Memo

Date: September 12, 2012
To: Sparb Collins
From: Pat Pechacek and Michael de Leon
Subject: Review of Proposed Bill No. 13.0102.01000

At the request of the Public Employees Retirement System, Deloitte was asked to provide a review of the effect on healthcare premiums and retiree health liability of proposed Bill No. 13.0102.01000 relating to amending insurance benefit coverage and health benefit credits for retired employees not eligible for Medicare.

Essentially, the North Dakota Century Code as amended by this bill will permit retired employees to use the health benefit credits to purchase insurance coverage outside of the uniform group insurance program. Currently, the health benefit credits must be used to purchase coverage from the uniform group insurance program.

The intended result of this amendment is that the affected group will be able to purchase health insurance coverage, beginning at the effective date of this bill, from a State Health Insurance Exchange (HIX) for similar coverage at rates more attractive than those offered by the uniform group insurance program.

Effect on Active Employee Premium Rates

Retirees not eligible for Medicare are currently blended with active employees when determining premium rates under the uniform group insurance program. This amendment will eventually eliminate all retirees from the uniform group insurance program. Since these retirees are expected to have higher claims on average than the active employees, removing them from the program will decrease the premiums for the remaining population.

We estimate that the active premium rates currently charged for the uniform group insurance program will decrease by approximately 0.9% (not withstanding other medical trend factors) as a result of all non-Medicare retirees leaving the program. This full effect of this decrease would be worth approximately \$120,000 in reduced premiums for one year based on Fiscal Year 2013 rates and data.

The effect on active premiums of this amendment may not be fully realized in the year after the effective date of this bill. This is due to the fact that current non-Medicare retirees will be permitted to



Official Professional Services Sponsor

Professional Services means audit, tax, consulting and financial advisory services.

Solely for the information and use of North Dakota PERS and not to be relied upon by any other person or entity

Member of Deloitte Touche Tohmatsu Limited

To: Sparb Collins
Subject: Review of Proposed Bill No. 13.0102.01000
Date: September 12, 2012
Page 2

stay within the plan. However, given that a HIX will likely offer less expensive options to these retirees, we would expect almost all of the savings to be realized within the first few years.

Our analysis of the effect of the amendment on active employee premium rates was based on claims and membership data for non-Medicare retirees and State active employees for the period July 2009 through April 2012. We also used normative data from national sources and proprietary data from the States of Wisconsin, Minnesota, and Iowa. Finally, we used summary information provided in the North Dakota Retiree Health Insurance Credit Fund Actuarial Valuation Report as of July 1, 2011.

Effect on Retiree Health Liability (Implicit Subsidy)

The fact that non-Medicare retirees are blended with active employees to set premiums in the uniform group insurance program creates a liability that has to be valued under GASB Statement No. 45 (GASB 45). Since these non-Medicare retirees are paying a premium rate that is on average lower than their expected health claims, they are receiving an implicit subsidy. GASB 45 requires that the liability associated with this implicit subsidy for current and future retirees be valued and reported as a footnote in the State's financial statements.

The values shown in the rest of this memo are based on the report titled "*July 1, 2011 Actuarial Valuation of Retiree Health Plans under GASB Statement No. 45 for Fiscal Years Ending 2012 and 2013*" prepared by Van Iwaarden Associates. We have not reviewed the report; therefore, we can make no comment on the reasonableness of the results contained in the report and restated in this memo.

According to the most recent actuarial valuation report, the present value of all implicit subsidy benefits expected to be paid for the current active and retiree population is \$122 million as of July 1, 2011. Of this, \$4 million is due to current retirees and \$118 million is due to actives. For the active population, \$61 million is attributable to services already provided and \$57 million is attributable to future service. The retiree portion plus the active portion attributable to past service totals \$65 million. This is considered the Actuarial Accrued Liability and is what is disclosed in the State's financial statements. Only a portion of this liability currently appears on the State's balance sheet; however, new GASB Statements being considered will likely require that the full unfunded liability be reported on the balance sheet at some point in the near future (similar to the new pension requirements under GASB 67/68).

This amendment will eventually eliminate all of this implicit subsidy liability. When this amendment is passed, the liability associated with the active population will be eliminated. The remaining liability associated with the retirees (currently \$4 million) will decrease as individuals opt to leave the uniform group insurance program in favor of an HIX plan or as they reach age 65. The majority of the remaining retiree liability will be eliminated within a few years after the effective date of the amendment.

To: Sparb Collins
Subject: Review of Proposed Bill No. 13.0102.01000
Date: September 12, 2012
Page 3

Effective Date of Amendment

The current bill contains an effective date for the amendment of January 1, 2014, which is the date when HIX plans should be implemented according to federal legislation. The State may want to consider delaying the effective date of the amendment to allow time for the Health Insurance Exchanges to be fully implemented. It is possible that there could be administrative problems at the initial implementation date that would create an undue hardship on retirees.

The effect on GASB liability can be recognized as soon as the legislation is passed regardless of the effective date of the amendment.