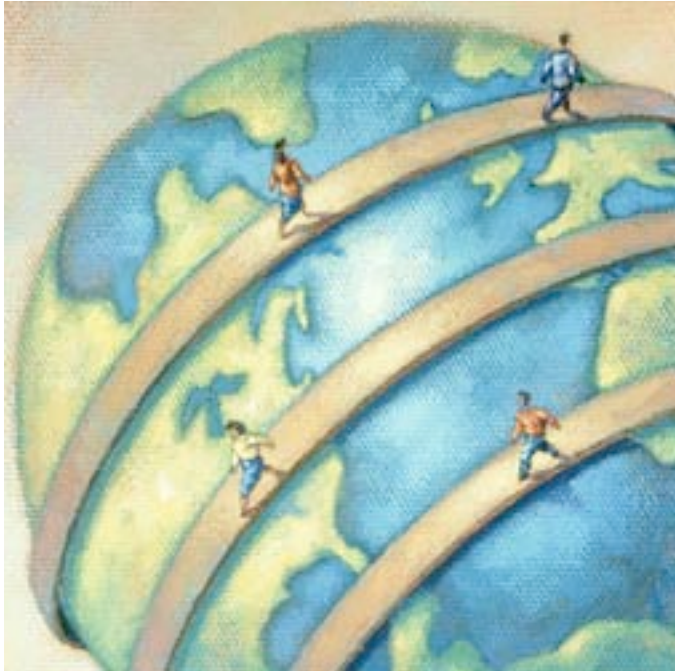


# MERCER

Health & Benefits



December 13, 2006

## **Vassar College**

Retiree Medical Discussion for  
Faculty & Administration



Marsh & McLennan Companies



# Retiree Medical Discussion Agenda

- The Situation Today
- Profile of Current Costs
- What If We Do Nothing
- What Can We Do to Address Costs
- Which Groups Could Be Affected -- Grandfathering Strategies
- Developments in Retiree Health Care Products



## The Situation Today

- Vassar today:
  - Extends the active employee medical plan to eligible retirees
  - Offers coverage to retirees who are at least 55 with 10 years of service at retirement
  - Provides free retiree health benefits for roughly 200 retirees age 65 and older
    - And covers roughly 60 retiree spouses and pre-65 retirees who pay the full cost of coverage
  - Will spend roughly \$1 million in 2006 on retiree health insurance
    - Average cost per retiree is about \$5,000
  - Has a liability of \$30 million for future retiree health benefit payments
  - Sees both cash costs and liability costs growing each year



## The Situation Today

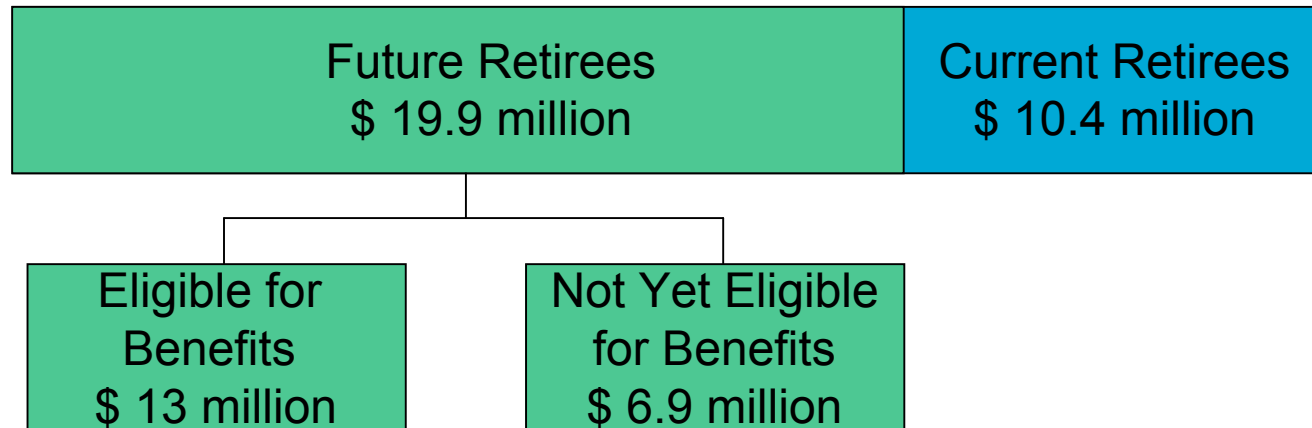
- Nationally, employers continue to drop retiree medical benefit programs
  - In 2006, only 19% of employers offer programs covering current and future Medicare-eligible retirees
- Most of Vassar's peer academic institutions do have retiree medical plans
- Retiree—and employee—health care costs continue to rise at near double-digit rates if no plan changes are made
- Employers are increasingly looking to modify retiree programs with new approaches available today
- Vassar faces concern over the size and increase in cash cost and accounting cost for this program



# The Situation Today

## Costs for Fiscal Year Ending June 30, 2006

I. The Accounting Cost of Future Benefit Payments: \$30.3 million unfunded liability



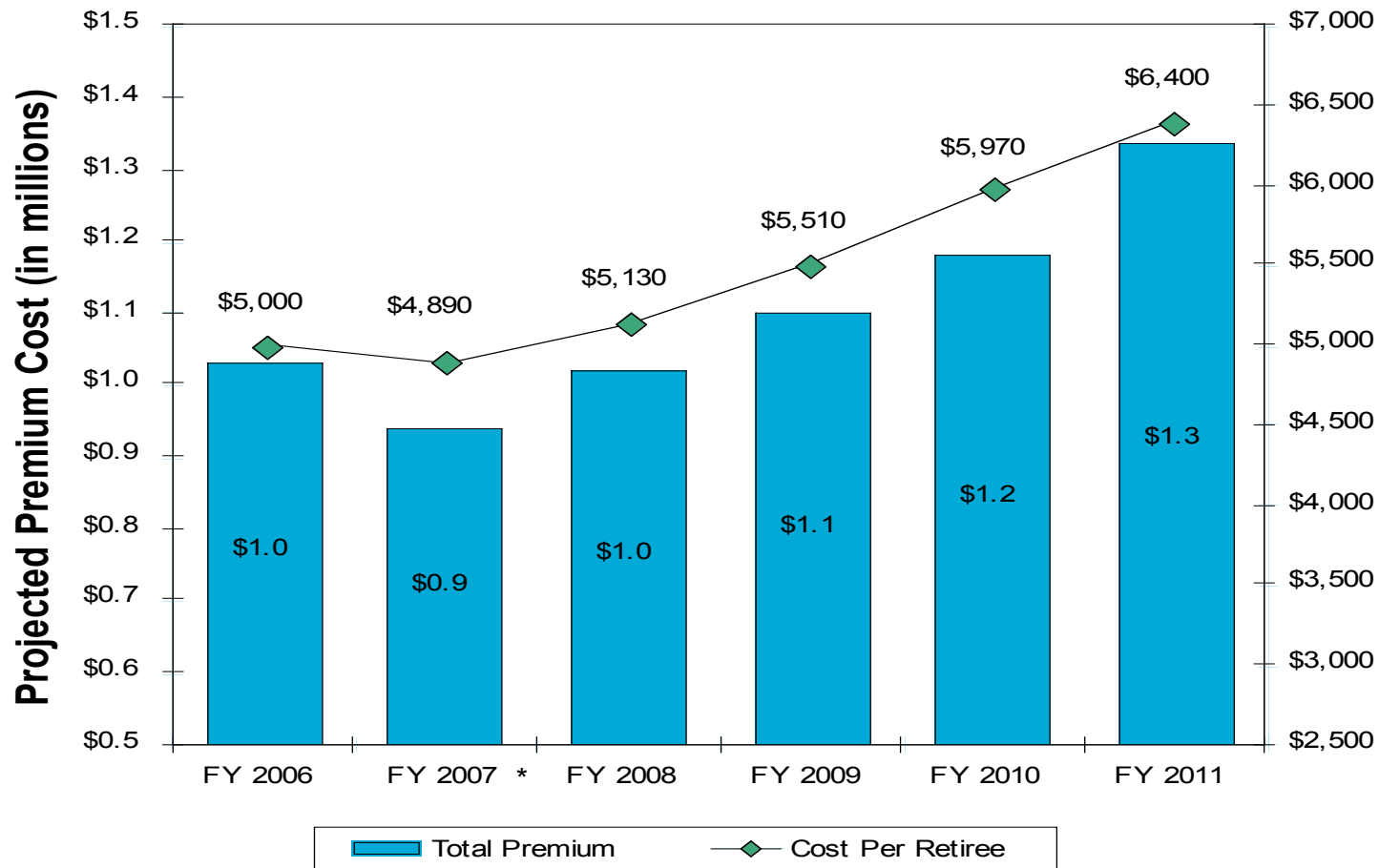
II. Annual Expense

	<u>Future Retirees</u>	<u>Current Retirees</u>
A. Cash	\$ 0	\$1,000,000
B. Annual growth in unfunded liability	\$2,400,000	\$ 700,000
- with no changes, the \$30.3 million unfunded liability will grow each year as employees accrue more benefits and interest is credited to the liability		



# What If We Do Nothing?

## Projected Cash Costs Rise Each Year



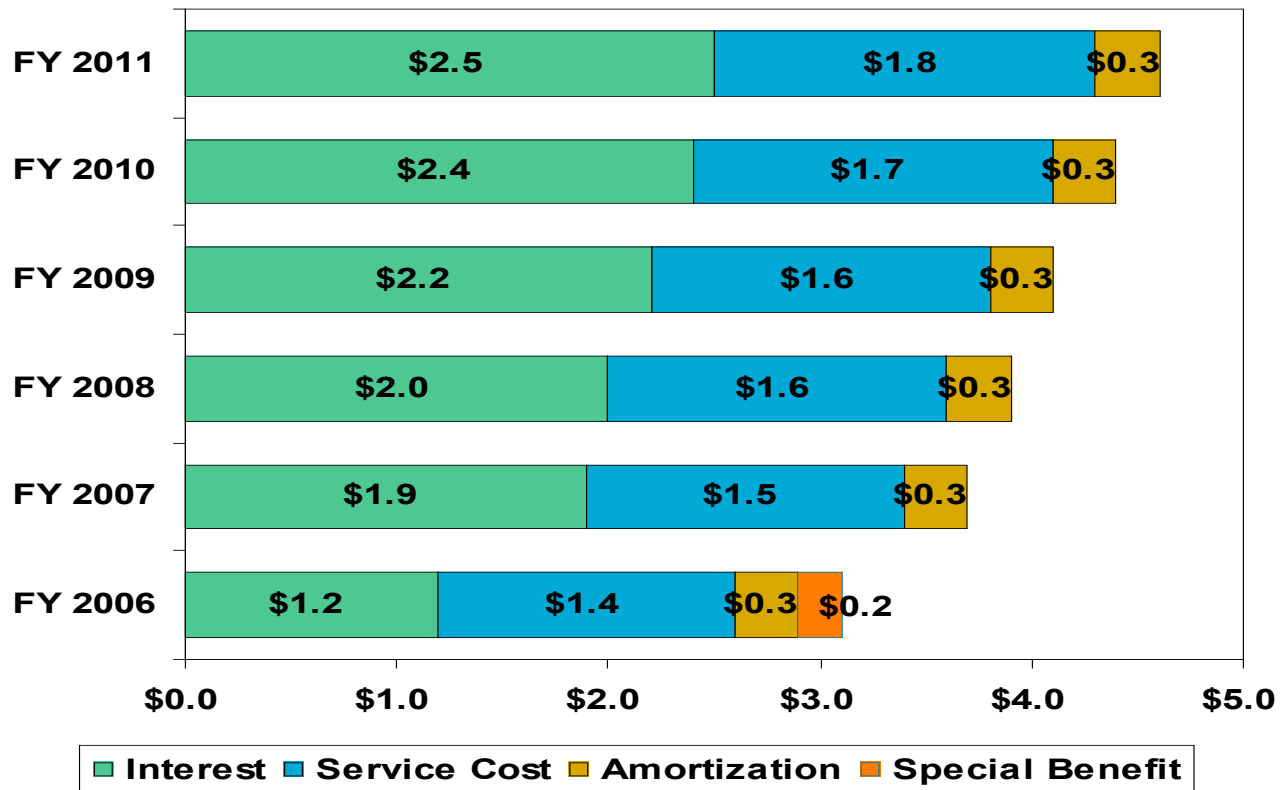
\*FY 2007 is the first time plan will get a full year of federal credits under Medicare Part D



# What If We Do Nothing?

Unfunded Liability Grows Each Year with Interest and Newly “Earned” Benefits

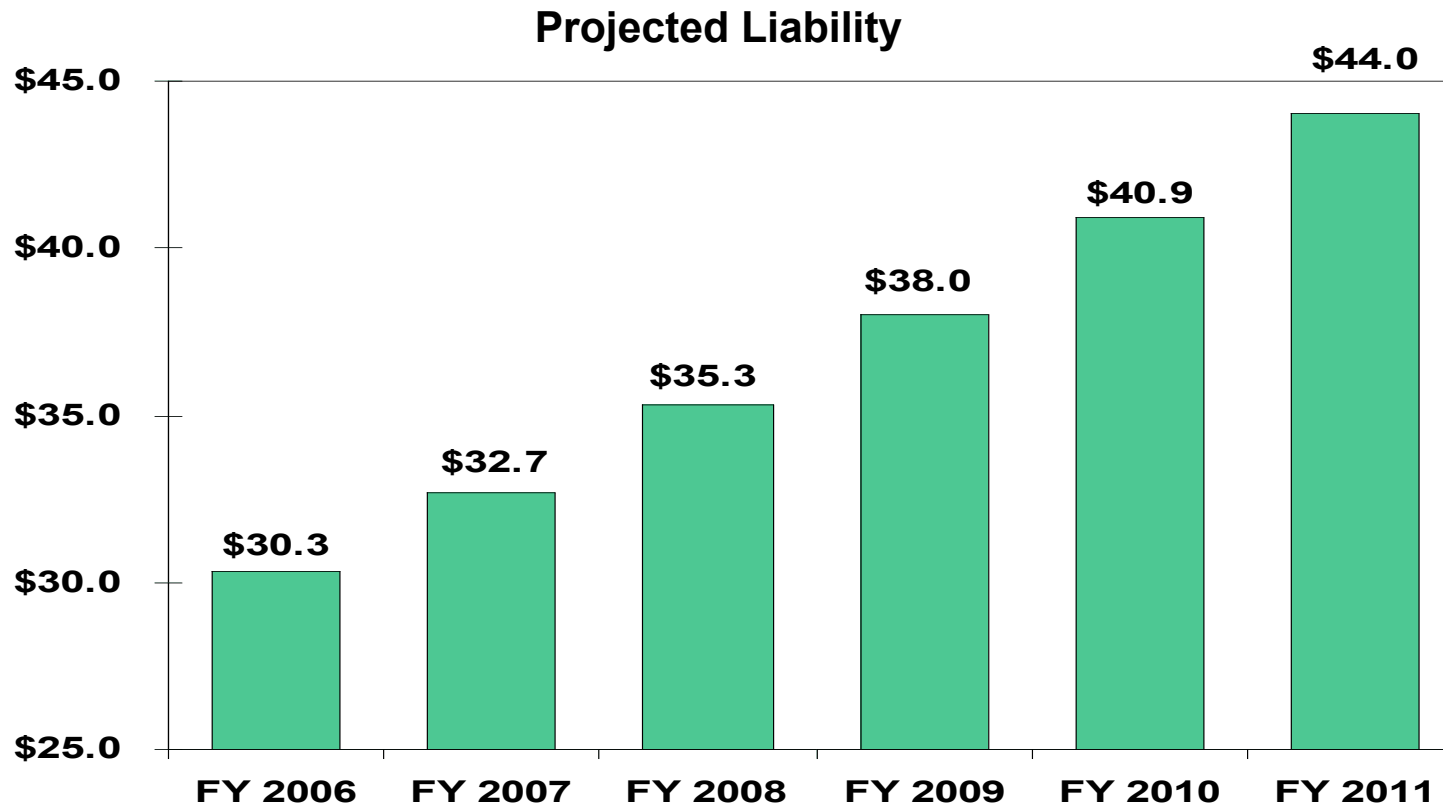
Projected Expense Components





# What If We Do Nothing?

The Result is an Increasing Liability for Vassar



The liability grows each year with the annual expense and is reduced by cash (premium) payments



## What Can We Do to Address Costs?

- Eligibility
  - older age, longer service needed to be eligible
- Retiree Contributions
- Subsidy Approach
  - percentage-of-cost vs. fixed dollar amount
- Subsidy Formula
  - function of age and/or service at retirement
- Plan design
  - increase cost sharing features; limit covered services
- Plan sponsorship
  - maintain a plan or open to market choice



## **Which Groups Could Be Affected -- Grandfathering Strategies**

- Current retirees: changes would affect one-third of the liability and all current cash costs
- Need to balance cost savings against disruption to those in or near retirement
- Could apply changes only to those
  - not yet retired
  - not yet hired
  - hired after a set date
  - retiring after a set future date
  - with age and/or service at or above a set level



# Developments in Retiree Health Care Products

- Defined Dollar Benefit programs
- Defined Contribution programs
  - Funded accounts
  - Notional (unfunded) accounts
  - Employee pre-funding
- Medigap Plans
- Medicare Advantage Plans



## Potential Approaches: Defined Dollar Benefit Programs (DDB)

- Vassar's cost would be a dollar amount instead of a benefit (percent)
  - Annual cost would be known
  - Not subject to medical inflation
  - Often targeted to a certain cost level
  - DDB could be set to rise slowly
- Option: Continue to sponsor a medical plan
  - Retiree cost = Vassar premium cost - DDB
- Option: Do not sponsor a plan
  - Retiree would buy an individual policy
  - Retiree cost = Policy premium cost - DDB
  - Market choices may help retirees keep cost increases down



## Potential Approaches: Defined Contribution Programs (DC)

- Vassar could make a defined contribution toward an individual account
  - Annual contribution would be known
  - Not subject to medical inflation
  - No accounting liability for future benefits
  - Funded or notional (unfunded)
- Ideally, funds would be used only for medical care after a certain age
  - Pay for choice of coverage available in the market
    - e.g. Medigap, Medicare Advantage, and traditional Medicare
  - Pay directly for out-of-pocket medical expenses
    - Requires some added administration



## **Potential Approaches: Defined Contribution Programs** (continued)

- Funded DC Accounts
  - Health Reimbursement Accounts (HRAs)
  - Health Savings Accounts (HSAs)
    - employee must be covered by a high deductible health plan
    - federal rules govern funding limits and design
    - funding is immediately vested
  - VEBA
    - dedicated accounts in trust, maintained by the employer
    - funds belong to the employees
  - Additional contributions to retirement programs, e.g. 403(b)
- Notional (unfunded) DC Accounts
  - Book entries, no cash committed
  - Could use HRAs



# Comparing the Approaches: Defined Benefit v. Defined Contribution

## Defined Benefit Plan

- Retiree coverage is known
- Employer provides a specific medical plan or plans
- Typically no funding while an active employee
- Not portable
- No vesting
- Creates accounting liability for future payments (FAS106 et al)
- Employee shares in cost only after retirement

## Defined Contribution Plan

- Health care benefit is not defined
- Employer may or may not offer a benefit plan for purchase in retirement
- Employer funds or credits an individual account while employee is active
- Account balance may be portable
- No accounting liability for future benefits; liability is fund built to-date
- Employee may be able to contribute to account while active



# Employee Account Pre-funding Available Vehicles

Savings Vehicle	Contribution	Contribution May Be Made By	Investment Earnings	Disbursements for Health Care	Limitations on Contributions
<b>HRA</b>	Tax-Free	Employer	NA	Not Taxable	Non-discriminatory
<b>HSA</b>	Tax-Free	Er/Ee	Tax-Free	Not Taxable	HDHP; maximum contribution
<b>403(b)</b>	Tax-Free	Er/Ee	Tax-Deferred	Taxable	Employer must have Plan; pre-tax and total contribution limits; min. required distributions after specified age
<b>Traditional IRA</b>	Tax-Free	Employee	Tax-Deferred	Taxable	Maximum contribution; tax-deduction limit for active retirement plan participant based on income; minimum required distributions after specified age
<b>Roth IRA</b>	Post-Tax	Employee	Tax-Free	Not Taxable	Contribution limits based on income
<b>VEBA</b>	Post-Tax	Er/Ee	Tax-Free	Not Taxable	Employer must have plan



## **Medigap Plans**

- Individual medical coverage, filling in Medicare coverage “gaps”
- Designs are federally set; up to 12 designs available
- Plans are insured; insurer may offer any or all designs
- Part B and Prescription Plan premium are additional

## **Medicare Advantage Programs**

- Alternative to traditional Medicare; widely available
- Medicare pays an insurer to offer complete “Medicare” benefits
- Various plan types (HMO, PPO, etc.) & benefits available
- Part B premium is additional
- Plan sponsors believe Medicare Advantage will be successful, with more stable costs than earlier versions of these kinds of plans