

Denver Board of Water Commissioners

Title:

**Denver Water Retirement Program Study - Phase II -
Evaluation of Retiree Medical**

Meeting Date: 5/13/2009

Contract/Proposal

 Action by Consent Action Information

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Creation of Rule of 75 and Retiree Medical

In 1995 Denver Water conducted a review of the retirement program for benefit adequacy and portability. At that time employees could retire with an unreduced retirement when they reached the minimum age of 62 and had at least 26 years of service. Retirement under this combination age and years of service was called the Rule of 88 because the minimum age and years of service sum to 88. While retirement under the Rule of 88 provided an adequate benefit, it did not allow for sufficient portability as many employees felt trapped by the age and years of service requirements of the design.

Based on the conclusions of the 1995 review, the Board approved a change in the minimum age and years of service for an unreduced retirement. The new combination was a minimum age of 55 with 20 years of service. This combination is referred to as the Rule of 75. In 1995 the Board also introduced the Retiree Medical Plan which allowed qualified retirees to remain on Denver Water's medical plan between the ages of 55 and 65. The Retiree Medical Plan was thought to be necessary in order to facilitate the Rule of 75 because without medical coverage retirement at age 55 and portability was less likely to be achieved. An important distinction of the Retiree Medical Plan from the Pension Plan is that it is not protected by the Retirement Plan documents. Rather, it is part of the Board-offered medical benefits and is subject to annual approval by the Board. When initially introduced, the benefit offered to retirees included a fixed amount subsidy of the published premium of \$125 per month. As we now know, the subsidy was much higher than that because the published premiums were not full cost premiums and, as a result, there was an un-quantified subsidy to employees and retirees alike.

Evaluation of Medical Benefits and Premiums

In 2006 the Board undertook a comprehensive study of its medical plan benefits. As a result, starting in 2007 the Board began assessing all medical premiums based on an understanding of the actual cost of medical benefits. The cost basis, currently in use today, is a blend of the medical costs for all active employees and retirees who qualify for retiree medical. Retirees pay higher premiums than active employees to reflect their higher cost contributions to the medical plan. However, even with the higher retiree premium payments, the retirees receive a larger subsidy from the Board than do active employees.

Accounting Implications of Retiree Medical

Denver Water complies with generally accepted accounting principles (GAAP) and follows specific accounting processes as developed by the Governmental Accounting Standards Board (GASB).

Starting in 2007, an accounting change (GASB 45) required Denver Water to begin accounting for Retiree Medical benefits as an Other Post Employment Benefit (OPEB). Like pension benefits, OPEBs are considered part of the compensation provided by an employer to the employee for services during employment but delivered to the employee post-employment. Thus, like pension benefits, the liability of an OPEB must be accounted for as it is earned over the employee's service with the employer (as opposed to when the benefit is provided).

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The 2007 accounting change effectively changed how Denver Water reports and pays for retiree medical. Prior to GASB 45, Denver Water incurred costs of approximately \$2 million per year for those on Retiree Medical. This pay-as-you-go amount was part of the annual budget and finance process of the Board's medical program. After GASB 45, the Board still incurs \$2 million of pay-as-you-go costs but also is required to account for the accrued future medical benefits earned by active employees despite the reality that these benefits will be paid in retirement. The accrued benefits for active employees are approximately \$3 million per year. Unless this amount is funded in an irrevocable account (which we have not yet elected to do), it appears as a liability on the Board's balance sheet. Thus, after GASB 45 the "cost" of retiree medical totals approximately \$5 million per year with approximately \$3 million per year presented as a long-term liability. At the end of 2008 the Board's OPEB liability was \$5 million.

Retirement Program Study—Phase II

The Board's Retirement Program Committee (RPC) has completed the first phase of a comprehensive retirement plan review. This review did not, however, include an assessment of the Board's Retiree Medical Program. The RPC has now embarked on such an evaluation (Retirement Program Study-Phase II).

Phase II of the Retirement Program Study has the following goals:

1. Review the assumption that retiree medical remains a critical component of the Rule of 75 and that the benefit is comparable to that offered by our peer group.
2. If retiree medical remains a critical component of the Rule of 75 and is a comparable benefit, develop methods to enable the Board to manage the OPEB liability, minimizing its costs and increasing its predictability.
3. Increase the Board's awareness of retiree medical programs and keep them informed about the study process.
4. Determine if there are alternative ways of providing retiree medical benefits that meet goal 2 above.

RECOMMENDATION:

Approvals:



David LaFrance, Director Finance



Carla Elam-Floyd, Manager Human Resources


Manager Approval:

Documents Attached:

 File Attachment