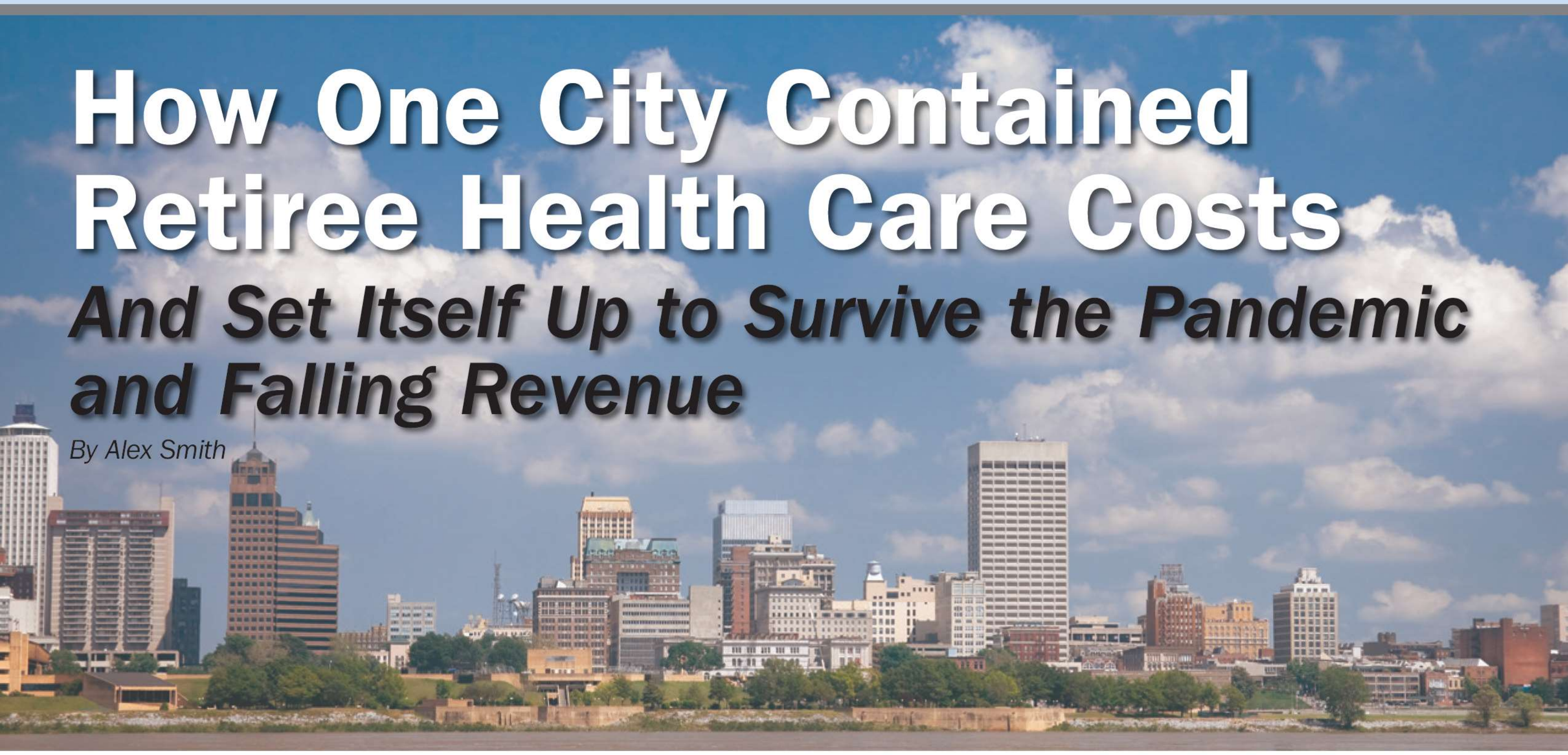
THE MAGAZINE OF THE INTERNATIONAL PUBLIC MANAGEMENT ASSOCIATION FOR HUMAN RESOURCES

NOVEMBER 2020

HR NEWS

IPMA-HR

Labor & Employee Relations



How One City Contained Retiree Health Care Costs

And Set Itself Up to Survive the Pandemic and Falling Revenue

By Alex Smith

Public sector organizations have struggled for decades to manage growing economic burdens related to other postemployment benefits (OPEB) liabilities. Drastically cutting retiree health care benefits has been a common response.

The COVID-19 pandemic has only made it tougher for state and local governments to continue providing health care benefits to retirees. According to the U.S. Department of Labor Statistics, the pandemic has exacerbated fiscal challenges for public sector entities in the following ways:

- Government revenues declined sharply due to enormous drops in income and sales taxes as people lost their jobs or had their hours reduced.
- States with suddenly smaller tax bases pulled back on making payments to pension and retiree health care funds, which provided some short-term budget relief but increased unfunded liabilities and shifted costs to later years.
- Instability across financial markets widened the already looming gap between what public pension plans owe and what they are able to pay.

The pandemic's continued impacts on the economy and public health make the longer-term revenue picture for public sector organizations murky, at best. Those of us who work as HR professionals in this sector need to pay more attention than ever to how we spend taxpayer money. At the same time, the need to hire and retain great employees makes getting benefits right critical for state and local governments.

Maintaining the status quo might not be an option for long. Eliminating retiree benefits sparks anger and engenders mistrust. In practical terms, then, both doing nothing and taking the usual option can drive early retirements, which compounds financial problems and intensifies challenges related to recruiting talented people to work in state and local government.

Delivering robust benefits, including retiree health care and pensions, is key to keeping public employees—our police and firefighters, teachers and sanitation workers—as safe and stress-free as possible. But the pandemic has created an unprecedented crisis. Between February and September 2020, government organizations in the United States shed an estimated 831,000 employees by making layoffs and issuing furloughs.

What follows is a concise explanation of how the City of Memphis was able to improve its financial standing and increase its ability to attract and retain top talent by containing retiree health care costs. Putting ourselves on a better financial footing three years ago greatly increased our ability to weather the COVID-19 storm.

The Challenge

In 2014, Memphis faced a $551 million fiscal deficit and $1.3 billion in OPEB liabilities, as mandated by the Governmental Accounting Standards Board. We made the very tough decision to eliminate our 70 percent health premium subsidy for most of our 4,000 Medicare-eligible and non-Medicare-eligible retirees. We then redirected the funds for premium subsidies into our pension system.

Unsurprisingly, the affected retirees were angry. But so were active employees who saw the retirement benefits they had been promised being reduced. The attrition rate in the police and fire departments over the next year was the highest in the city's history. We lost 185 officers from the police department in 2015 alone.

Public safety recruitment has been getting tougher nationwide. Research by the Police Executive Research Forum showed the number of law enforcement applicants across the United States

Options the City of Memphis Considered When Looking to Continue Offering a Retiree Health Benefit

	Description	Benefits	Concerns
Option A. Individual marketplace	Move retirees to individual plans via an insurance marketplace and subsidize retirees' costs with a health reimbursement arrangement	Offered the education, advocacy and choice we were looking for	Required retirees to make a major change
Option B. Lower subsidies	Reinstate some premium subsidy below 70 percent	Simplified enrollment and somewhat defrayed costs for most retirees	Kept the city's costs and liabilities tied to future premium increases
Option C. No change	Stick with the elimination of the subsidy for most retirees	Reduced the city's costs and OPEB liabilities	City would continue losing talent to retirement and organizations that offer more competitive benefits

dropped by 63 percent from 2013 through 2017. Memphis was not spared from this trend.

Employee turnover is also expensive: The average cost to hire and train a new employee is just over $4,100.

Fast-forward to January 2016 when a new mayor, Jim Strickland, brought me in as chief human resources officer. In our very first meeting, Strickland told me my top priority was to attract and retain top talent in public safety for the city. The loss of retiree health care came up repeatedly during discussions with active employees. Clearly, this was something we needed to address in order to attract and retain talent.

Finding a Solution

In April 2016, city leaders began searching for a solution that would allow us to continue offering a retirement health care benefit while meeting all other fiscal obligations. Although we considered reinstating the original health premium subsidy, we pegged the cost of doing that at $10 million each year and determined that it was not sustainable. We ended up with three viable options, as detailed in the accompanying table above.

When we analyzed the financial impact of each option, we learned that monthly premiums for the city's plans were significantly higher than those for private individual plans that could selected via a marketplace. Switching to having retirees choose their own plans would allow the city to reduce its expenditures even while offering a generous defined-contribution health reimbursement arrangement. Lowering costs in this way would permit the city to continue providing a retiree health benefit at a sustainable level in perpetuity.

Even better, we learned that going through the individual marketplace would save 99 percent of Medicare-eligible retirees as much as $2,106 in health care costs each year. And most importantly, the city could begin providing a health care option for non-Medicare-eligible retirees.

Satisfied that Option A was our best choice, we chose Willis Towers Watson's individual marketplace for retirees and they took us through the transition.

Some of my colleagues were worried whether retirees would be able to adapt to a change this significant. The transition had its bumps. Every big change does. But we trusted the process, and the results were more than worth it.

Public sector organizations that are looking at doing the same thing today may have an advantage that we did not. The pandemic has forced everyone, including seniors, to adapt and use more online services. As a result, retirees may be more comfortable with virtual shopping and buying experiences.

Results

Highlights for the city and retirees include

- Estimated program savings are $5 million per year for the next 20 years.
- Memphis's OPEB liabilities were immediately reduced by $319 million.
- Medicare-eligible retirees have enrolled in 223 unique plans from 34 different carriers.
- Medicare-eligible retirees have reduced their health care spending by as much as $2,106 annually.

Moving our retirees to individual plans was the best benefits decision we ever made. The savings and fiscal breathing room afforded by making the change have been an enormous boon for the city since the beginning. Now, during the pandemic, it has given us bandwidth to focus on other critical matters. With our retiree health care program on a sound footing, we can attend to other priorities.

Alex Smith is CHRO for the City of Memphis, Tenn. She is on ***LinkedIn****.*

—N