M E M O R A N D U M

April 8, 2011

TO: Stephen B. Farber, Council Staff Director

FROM: Karen Orlansky, Director
Office of Legislative Oversight

SUBJECT: **County Executive's FY12 Recommended Budget: Overview of Proposed Changes to County Government Employees' Retirement, Health, and Life Insurance Benefits**

This memorandum responds to your request for an overview of changes in the County Executive's FY12 Recommended Operating Budget to retirement, health insurance (including medical, prescription drug, dental, and vision coverage), and life insurance benefits for County Government employees.

Part A, Policy Issues, summarizes the key policy issues and related questions raised by the County Executive's proposed changes to the retirement and health benefits of County Government employees.

Part B, Summary of County Executive's Proposals, describes the Executive's recommended changes to retirement, health, life insurance, and long-term disability benefits. It highlights changes from the status quo and provides the Executive's estimated FY12 savings associated with specific changes.

Part C, Impact on Employees, contains illustrative examples of the financial impact the Executive's recommended changes to retirement and health benefits would have on individual employees.

A. Policy Issues and Related Questions Raised by the Executive's Proposals

The Executive's proposed changes to the benefits of County Government employees raise multiple policy issues and related questions for the Council to consider as part of its budget deliberations. Staff recommends that the Council's review of the Executive's proposed changes include explicit discussion of:

- The policy issues underlying the Executive's proposals; and
- The FY12 and future year fiscal impact of the proposed changes on individual County Government employees as well as on the County Government's costs.

The Council may want to consider dividing its discussion of employee benefit changes into two phases. The first phase would address where the County should "land" with respect to the parameters of employee benefits, e.g., level of benefits, division of costs between the County and its employees. The second phase would address whether to implement the changes all at once or over a multiple year time period. (The Executive's FY12 budget assumes that all benefit changes are implemented as of July 1, 2011.)

The table on the following page contains an initial list of the underlying policy questions that staff recommends the Council consider during its review of the County Executive's budget.

POLICY ISSUES AND RELATED QUESTIONS	OBSERVATIONS ON THE CE'S PROPOSALS FOR CHANGING COUNTY GOVT. EMPLOYEES' BENEFITS
General	
1. Should employees in all County agencies be offered a comparable package of retirement and health benefits? If not, then what factors should determine how the benefits differ?	Unless similar changes to employee benefits are implemented by the other agencies, the CE's proposals (if implemented) would increase the disparity among benefit packages provided to employees across the County-funded agencies.
2. Should changes implemented in FY12 be part of a multi-year plan designed to achieve an explicitly stated policy goal, e.g., limiting benefit costs to a set percent of personnel costs; modeling County benefits after those of the federal government?	The CE states that his proposals to restructure employee benefits will reduce costs. The CE does not indicate how these changes fit into a long-term compensation policy.
3. Should there be a limit established on the increased costs of benefits shifted to employees in one year? Over time?	In FY12, under the CE's proposals, an employee will pay between \$370 and \$3,700 more for the same health insurance coverage. In addition, defined benefit plan members will be required to contribute an additional 2% of their salaries towards their pension.
4. Should a portion of the County's structural budget problem be addressed by changing the compensation package for new hires?	The CE's FY12 budget does not include any proposals for modifying either the salaries or the benefits for employees not yet hired.
Retirement/Pension Benefits	
5. When considering changes to retirement benefits, should the County seek equivalent savings from employees in the defined contribution plan, which currently costs the County substantially less than the defined benefit pension plans?	The CE's proposal would result in an annual 2% salary "loss" for all employees. Defined benefit plan members would contribute 2% more of their salary; RSP & GRIP plan members would lose a retirement account contribution equal to 2% of salary.
Health Insurance Benefits for Active Employees	
6. In total, what portion of health insurance benefit costs (medical, prescription drug, dental, and vision) should the County Government cover for its employees?	The CE's proposed changes to health insurance would reduce the overall share paid for by the County from about 80% to about 60% of the total cost in FY12.
7. Should all employees pay the same percent share of their health insurance costs? If not, should an employee's cost share vary by his/her: • Annual salary? • Level of coverage (e.g., single, family)? • Plan choice (e.g., HMO, POS)?	Under the CE's proposals, the actual cost share of health insurance paid by employees would range from 30% to 58% of the combined premium. Further, for most employees (because of the added salary-based premium), the CE's pricing results in higher cost shares paid by those enrolled in the least expensive health plans, i.e., single or HMO coverage.
8. Should the cost of health care to County Government retirees be more, less, or the same as that for active employees?	Today, most retirees pay a higher cost share than active employees. Under the CE's proposals, most active County employees would end up paying more than retirees for group insurance.

B. Summary of County Executive's Proposed Changes to Employee Benefits

The Executive proposes a series of modifications to County Government employee benefits. The table below summarizes the Executive's proposed changes and shows his estimated FY12 savings that would result from implementation of the proposal. The proposed changes, if implemented, would produce recurring savings in future years. The Executive recommends implementing all changes on July 1, 2011.

Table 1: Summary of Executive's Proposed Changes to County Government Employees' Benefits

Benefit Type	County Executive's Proposal	CE Estimated FY12 Savings
Retirement	**Pension (Defined Benefit) Plans.** Employees would contribute an additional 2% of salary towards their pensions.	$6,044,180
	Retirement Account (Defined Contribution[1]) Plan. The employer's contribution to employee retirement accounts would be reduced by 2%.	$4,860,290
Health (Medical/ Prescription/ Dental/Vision)	**Minimum 30% Cost Share.** Employees' cost share of medical, prescription drug, dental and vision insurance premiums would increase from a minimum of 20% to a minimum of 30%.	$8,229,530
	Additional Salary-Based Charge. Employees with an annual salary between $50,000 and $89,999 who enroll in a medical and/or prescription drug plan would pay an additional $910 per year. Employees with an annual salary of $90,000 and above who enroll in a medical and/or prescription plan would pay an additional $1,560 per year.	$7,418,000
Prescription Drug	**Generics.** Employees who buy a brand name drug when a generic equivalent is available would always pay the generic drug copay <u>plus</u> the difference between the cost of the brand name drug and its generic equivalent. Currently, this requirement is waived if a physician prescribes a brand drug and writes "dispense as written" on the prescription.	$1,200,000
	Lifestyle Drugs. The County would eliminate coverage for medications used to treat erectile dysfunction.	$400,000
	Mail-Order Copays. The copay for mail order prescriptions (up to a 90-day supply) would increase from one time to two times the copay for a 30-day supply purchased through a retail pharmacy.	$200,000
Life Insurance	**30% Cost Share and Benefit Level.** The life insurance benefit provided to all employees would be reduced from two times to one time annual salary. Employees' cost share would increase from 20% to 30% of premium.	$1,200,000
Long-Term Disability	**30% Cost Share.** Employees' cost share for long-term disability insurance would increase from 20% to 30% of premium.	$48,000

[1] In this memo, the term, "defined contribution" plan, includes both the Retirement Savings Plan (RSP) and the Guaranteed Retirement Income Plan (GRIP).

The next three pages provide further detail on the two proposed changes that would have the greatest effect on the cost of benefits to County Government employees: retirement and health insurance benefits.

1. Executive's Proposed Retirement Plan Changes

The County Government will pay $124 million (from tax supported and non-tax supported funds) for employee retirement benefits in FY11: $105 million for the defined benefit plan and $19 million for the defined contribution plan. Currently, the defined benefit and the defined contribution plans have approximately the same number of enrollees. While defined benefit plans are more generous to employees and cost the County significantly more than defined contribution plans, the Executive proposes that employees in both plan types forego identical amounts (2% of salary).

a. Defined Benefit Plans: The County Executive has proposed that all employees in a defined benefit plan contribute an additional 2% of salary annually. As shown in the table below, the impact of the Executive's proposal varies among different employee groups.

Table 2: Executive's Proposed Increases in Employee Defined Benefit Contributions

Employee Group	Current Employee Contribution (% of salary) [2]	CE Proposed Employee Contribution (% of salary)	% Increase in Employee Contribution
Non-Public Safety (hired before 10/1/94)	4%	6%	+50%
Police and Deputy Sheriff/Corrections	4.75%	6.75%	+42%
Fire & Rescue	5.5%	7.5%	+36%

b. Defined Contribution Plans: Currently, the County Government contributes 8% of salary into a retirement account for most employees in a defined contribution plan.[3] The Executive proposes reducing the employer contribution to 6% of salary, a 25% reduction in the employer's contribution. Unlike the proposed defined benefit changes, the Executive's defined contribution proposal would not reduce take home pay but would reduce the amount of money available upon retirement.

Table 3: Executive's Proposed Reduction in Annual Retirement Account Contributions

Employee Group	Current Employer Contribution (% of salary)	CE Proposed Employer Contribution (% of salary)	% Reduction in Employee Contribution
Non-Public Safety (hired after 10/1/94)	8%	6%	-25%
Non-Represented Public Safety (hired after 10/1/94)	10%	8%	-20%

[2] Employees in the ERS who earn more than the Social Security Wage Base ($106,800 in 2012) contribute a higher percentage toward their pensions for salary earned above the Social Security Wage Base.
[3] A small number of non-represented public safety employees participate in a defined contribution plan in which the employee contributes 3% of salary and the County contributes 10% of salary.

2. Executive's Proposed Health Insurance Benefit Changes

In FY11, the County Government will pay about $90 million (from tax supported and non-tax supported funds) for employee health (medical, prescription drug, dental, and vision) insurance premiums.

a. Proposed Cost Share Changes: Currently, County Government employees pay at least 20% of health benefit premiums.[4] The Executive proposes a new two-part health care pricing approach.

(1) All employees would pay at least 30% of medical, prescription drug (standard), dental, vision, life, and long-term disability insurance premiums; AND

(2) Most employees who enroll in a medical and/or prescription plan would pay an additional salary-based charge.

Table 4: Executive Recommended Changes to MCG Employee Health Benefit Cost Share

Salary Level	Percent of Workforce *	Current Minimum Employee Health Premium Contribution [4]	CE's Proposed Minimum Annual Employee Health Premium Contribution
Under $50,000	20%	20% of premium	30% of premium
$50,000 - $89,999	65%		30% of premium + $910
$90,000+	16%		30% of premium + $1,560

* Source: *Personnel Management Review*, Montgomery County Office of Human Resources, April 2011.

b. Actual Cost Share: If the Executive's proposals are implemented, employees will pay an actual cost share ranging from **30% to 58%** of the total combined premium for medical, prescription drug, dental, and vision coverage. Because the salary-based charge proposed by the Executive does not vary based on plan choice (e.g., HMO vs. POS) or level of coverage (e.g., single vs. family), employees subject to the added charge will pay a higher percent of the total premium if enrolled in a less expensive plan (e.g., single coverage, HMO plans).

Table 5: Employee Cost Share for Combined Health Insurance Premium*
Current vs. Executive's Proposal

Salary Level	% of Annual Premium Paid by Employee [5]	
	Current Range	Range Under CE's Proposal
Under $50,000	20% to 32%	30% to 37%
$50,000-$89,999		34% to 49%
$90,000+		37% to 58%

*Includes costs for medical, prescription, dental, and vision coverage using calendar year 2011 premium rates.

[4] Non-represented employees hired since 10/1/94 ("Select" plan members) pay 24% of premiums. Also, an employee who chooses the "high option" prescription plan pays an additional 8% of total health insurance premium costs.
[5] The highest employee cost share under current pricing and as proposed by the Executive reflects the cost of high option prescription coverage.

c. Cost Share Increases Translated into Dollars: The Executive's proposal will require County Government employees to pay more to retain their current health care coverage. Employees in a higher cost plan (e.g., Carefirst High Option POS) could mitigate their additional cost of health insurance by switching to a lower cost plan (e.g., Kaiser HMO).

The following table shows the dollar amount of employee health benefit cost under current practice and as proposed by the Executive. The table shows the range of increase in employee health costs if employees stay in their current choice of health and prescription drug plans. The data include costs for medical, prescription drug, dental, and vision coverage using calendar year 2011 premium rates.

Table 6: Annual Employee Health Insurance Premium Costs
Current vs. Executive's Proposal

Salary Level	Annual Employee Health Insurance Premium Costs*		
	Current Range	Range Under CE's Proposal	Increase
Under $50,000	$1,237 to $7,290	$1,855 to $8,587	$371 to $2,163
$50,000-$89,999		$2,765 to $9,497	$1,281 to $3,073
$90,000+		$3,415 to $10,147	$1,931 to $3,723

*Includes costs for medical, prescription, dental, and vision coverage using calendar year 2011 premium rates.

Currently, employees pay different costs for their health benefits based on their plan choices (e.g., HMO vs. POS, standard vs. high option) and level of coverage (e.g., single vs. family). The changes proposed by the Executive would continue price differentials based on plan choices and level of coverage, but would add an employee's annual salary as a factor that determines the actual cost share and dollar amount paid for health benefits. The final section of this memo (beginning on the following page) illustrates how the changes proposed by the County Executive would impact individual employees.

C. Impact on Employees – Illustrative Examples

This section provides five examples to illustrate the effects of the Executive's proposed retirement and health care benefits changes on five hypothetical employees at different salary levels as listed below.

Example	Job Title	Annual Salary	Salary-Based Health Care Charge Category
1	Ride On Bus Operator	$45,000	Under $50,000
2	Code Enforcement Inspector	$55,000	$50,000 - $89,999
3	Police Sergeant	$85,000	$50,000 - $89,999
4	Senior Information Technology Specialist	$95,000	$90,000 +
5	Assistant County Attorney III	$115,000	$90,000 +

The examples on the following pages show how the Executive's retirement proposal would increase employees' pension contribution costs (for defined benefit plan participants) or retirement account contributions (for defined contribution plan participants). For health care benefits, the examples illustrate the effects of the Executive's proposals on employees with either single or family coverage enrolled in a relatively low cost plan (Kaiser HMO) and enrolled in relatively high cost plans (Carefirst point of service medical combined with Caremark high option prescription).

In reviewing the examples, please note:

- All health care premium costs reflect Calendar Year 2011 rates.
- The cost changes assumes that the employees retain their current health care choices.
- Employee "actual" cost share includes combined health premium costs plus the additional salary-based charge for employees earning $50,000 or more.
- The County provides two different high option prescription plans with different premiums and copays. Employees represented by MCGEO or IAFF are offered a plan with $4 (generic) or $8 (brand) drug copays while FOP and non-represented employees are offered a plan with $5 and $10 copays.
- The examples shown on the following pages do not encompass all the possible combinations of health plan choices available to County Government employees. Table 5 of this memo (page 5) of this memo shows that if the Executive's proposed changes were implemented, employees would pay a cost share ranging from 30% to 58% of the total combined health insurance premium. The high end of this range, 58%, would apply to an employee earning $90,000 or more, who opts for single coverage in the United Healthcare HMO and the Caremark High Option prescription plan.