State of Delaware
Retirement Benefit Study Committee

Overview: Other Post-Employment Benefits (OPEB)

September 26, 2019

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Executive Order Number 34: Retirement Benefit Study Committee

- Rick Geisenberger, Committee Chair and Secretary of Finance
- Michael Begatto, Executive Director, AFSCME, Council 81, appointed by the Director of the Office of Management and Budget
- Rep. Ruth Briggs-King, appointed by the Minority Leader of the House of Representatives
- David Craik, Director of the State Office of Pensions
- Colleen Davis, State Treasurer
- Mike Jackson, Director of the Office of Management and Budget
- Aaron Klein, SVP and Director of Business Performance and Analysis, WSFS Bank, appointed by the Secretary of Finance
- Sen. David Lawson, appointed by the Minority Leader of the Senate
- Rep. John L. Mitchell, appointed by the Speaker of the House of Representatives
- Mike Morton, Controller General
- Faith Rentz, Director of the Office of Statewide Benefits and Insurance Coverage
- Sen. David Sokola, appointed by the President Pro Tempore of the Senate
- Jeff Taschner, Executive Director, Delaware State Education Association, appointed by the Director of the Office of Management and Budget

Executive Order Number 34

- **Challenges**
  - Escalating costs of post-retirement health care
  - Growing $7 billion+ unfunded Other Post-Employment Benefit (OPEB) liability and its impact on Delaware's fiscal health
  - Risk that "pay-go" increasingly crowds out education, social service, public safety, infrastructure and other key priorities
- **Opportunity**
  - Delaware's long, successful, bipartisan tradition of cooperation, credible analysis and focus on fiscal management
  - Develop meaningful policy responses to above challenges

Executive Order Number 34

The Committee shall:

a) *Study the results of any available actuarial work that addresses the impact of Other Post-Employment Benefits on the State of Delaware, or commission additional actuarial work if needed;*

b) *Identify the options available to the State and quantify the potential effects of each; and*

c) *Assess the desirability of the options (or a combination of options) according to the following criteria:*

   1) *the extent to which and over what time-horizon the option eliminates or reduces the State's unfunded liability;*

   2) *fairness in the distribution of cost between or among employees and retirees, taking into account such considerations as employees' and retirees' ages, length of State service, starting and ending dates of service, and income levels;*

   3) *the transparency of each option's impact on current and future beneficiaries;*

   4) *ease of administration for the State and of use by beneficiaries;*

   5) *the extent to which the option affects the State's position in the labor market, including taking into account its competitiveness with other employers, turn-over rates, and incentives or disincentives to retire; and*

   6) *fiscal considerations, including an assessment of the cost of continuing the insufficient funding of this growing liability including:*

      (a) debt rating implications and the cost of capital;
      (b) impacts on operating budget growth and programs; and
      (c) tax and revenue policy implications.

Executive Order Number 34

- **Other Committee Duties**
  - Present preliminary findings to DEFAC at its March 16, 2020 meeting
  - Report findings and recommendations to Governor and General Assembly by March 31, 2020
  - Report periodically (at least annually) if Committee is extended

Other Post Employment Benefits (OPEB) | The Basics

- **OPEB benefits** are retirement benefits other than pensions – typically, as in the State of Delaware, retiree medical coverage

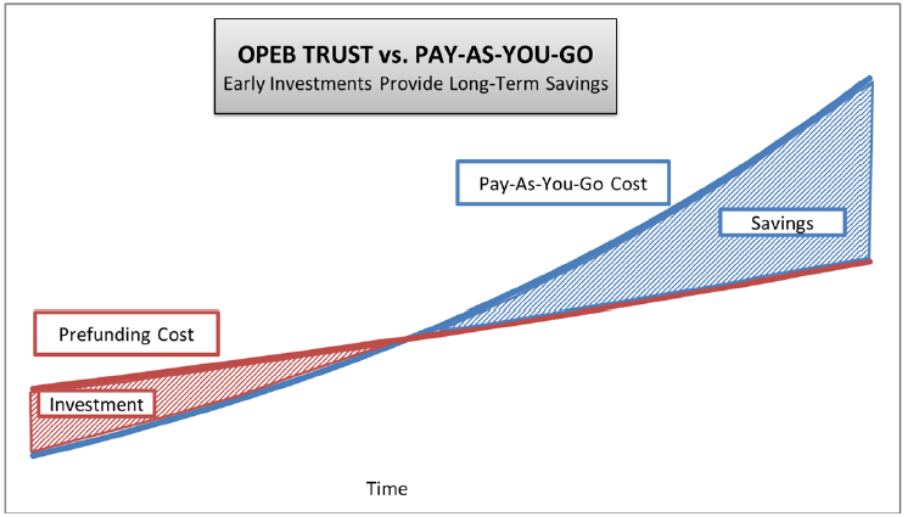
- Unlike pensions, for which trusts have long been in place to help ensure the long-term funding for retirement obligations, **most state and local governments traditionally paid OPEB costs only as incurred** by those who had already retired – rather than funding the projected long-term costs on an actuarial basis during an employee's years of active service
  - With growing numbers of retirees and rising healthcare inflation, large, unfunded OPEB liabilities have developed
  - While coverage levels can vary widely, a 2016 study by the Center for Retirement Research at Boston College estimated that the total state and local government OPEB unfunded liability nationally was **$862 billion**, two-thirds at the local level. With this study based on 2013 valuations, the total today is likely even higher

- Recognizing this growing problem, the Government Accounting Standards Board (GASB) issued new standards about a decade ago: **state and local governments must now provide actuarial valuations of their retiree health and other OPEB programs** to identify the magnitude of long-term program costs *(GASB 45)* – just as long done for pensions

- More recently, newer GASB Statements 74 and 75 now require that **state and local governments must recognize their full net actuarial OPEB liability on their balance sheets**

Other Post Employment Benefits (OPEB) | The Basics

- OPEB actuarial valuations include an **Annual Required Contribution (ARC)**, generally indicating the amount a public employer would need to fund each year, to meet the following commitments:
  - To set money aside for future benefits for current employees during their active years of service
  - To amortize any unfunded liabilities for both active and future employees
- In the short-term, the ARC is typically much higher than the cost of claims/premiums for eligible retirees already receiving benefits (**"pay-go"**)
- Over the long-term, funding the ARC allows a government to harness investment returns for prefunded amounts to pay a portion of future OPEB benefits
  - Generates long-term savings
  - Moderates future pressures to increase funding and/or cut benefits
- While fully funding the ARC is not legally "required," the government must report its full OPEB liabilities under accounting standards



Source: *Retiree Health Care: A Cost Containment Guide*, League of California Cities

Delaware OPEB Benefits

- **Eligibility**: retiree healthcare coverage begins at commencement of a vested pension benefit (or qualified disability)
  - Most State employees hired post-2011 can retire at any age with 30 years of service, age 60 with 20 years of service, or age 65 with 10 years of service
  - Pre-2012 hires can retire at any age with 30 years of service, age 60 with 15 years of service, or age 62 with 5 years of service
  - State Police, Judges, Correctional Officers, and other specified peace officers can generally retire earlier given the different characteristics of their jobs, and general State worker also have an early retirement option at age 55 with 15 years or any age with 25 years of service

- **Multiple Plan Options**: First State Basic PPO, Highmark Comprehensive PPO, Aetna HMO, or Aetna CDH; Highmark Medicare Supplement Plan upon eligibility; Express Scripts Rx
  - Spousal coverage available with State paying the same % of premiums as for retiree; surviving spouses also eligible
  - Highly competitive co-pays, deductibles, and out-of-pocket maximums, varying by plan selected; retail Rx co-pays of $8 generic / $28 preferred / $50 non-preferred

Source: State of Delaware Postretirement Health Plan, GASB 74/75 Report as of June 20, 2018 Measurement Date, Cheiron, Revised October 2018

Delaware OPEB Benefits

- Retiree share of premium (pre-Medicare) effective 7/1/2012:
  - If hired before 7/1/1991 or on disability retirement, no employee contributions; 100% State funded
  - Otherwise, with 20 or more years of state service: 4.0% for the Basic plan, 5.0% for the CDH, 6.5% of the HMO, and 13.25% for the Comprehensive PPO
  - State contribution is reduced for retirees with <20 years of service (varies by date of hire and years of service), and no state contribution if <15 years of service for those hired on or after 1/1/2007 (10 years of service if hired earlier)
- Medicare-eligible pensioners who retired after 1/1/2012 contribute 5.0% of the Medicare supplement offered by the State (retirees prior to 1/1/2012 do not contribute)

	Total Monthly Premium (Rate)	State Pays	Monthly Premium (Rate) Paid By State of DE Employee
Highmark Delaware First State Basic Plan			
Employee	$695.36	$667.52	$27.84
Employee & Spouse	$1,438.68	$1,381.16	$57.52
Employee & Child(ren)	$1,057.02	$1,014.76	$42.26
Family	$1,798.42	$1,726.50	$71.92
Aetna CDH Gold Plan			
Employee	$719.68	$683.70	$35.98
Employee & Spouse	$1,492.22	$1,417.64	$74.58
Employee & Child(ren)	$1,099.56	$1,044.60	$54.96
Family	$1,895.74	$1,800.96	$94.78
Aetna HMO Plan			
Employee	$725.94	$678.78	$47.16
Employee & Spouse	$1,530.58	$1,431.08	$99.50
Employee & Child(ren)	$1,110.52	$1,038.34	$72.18
Family	$1,909.82	$1,785.70	$124.12
Highmark Delaware Comprehensive PPO Plan			
Employee	$793.86	$688.68	$105.18
Employee & Spouse	$1,647.34	$1,429.08	$218.26
Employee & Child(ren)	$1,223.46	$1,061.38	$162.08
Family	$2,059.40	$1,786.54	$272.86

SPECIAL MEDICFILL WITH PRESCRIPTION				
Retired Prior to or on 7/1/12				
	PERCENTAGE STATE SHARE	TOTAL COST	STATE SHARE	PENR SHARE
Individual	100%	$459.38	$459.38	$0.00
Individual	75%	$459.38	$344.54	$114.84
Individual	50%	$459.38	$229.69	$229.69
Individual	0%	$459.38	$0.00	$459.38

SPECIAL MEDICFILL - NO PRESCRIPTION				
Retired Prior to or on 7/1/12				
	PERCENTAGE STATE SHARE	TOTAL COST	STATE SHARE	PENR SHARE
Individual	100%	$260.44	$260.44	$0.00
Individual	75%	$260.44	$195.33	$65.11
Individual	50%	$260.44	$130.22	$130.22
Individual	0%	$260.44	$0.00	$260.44

SPECIAL MEDICFILL WITH PRESCRIPTION				
Retirement Effective 7/2/12 & Later				
	PERCENTAGE STATE SHARE	TOTAL COST	STATE SHARE	PENR SHARE
Individual	100%	$459.38	$436.42	$22.96
Individual	75%	$459.38	$327.32	$132.06
Individual	50%	$459.38	$218.21	$241.17
Individual	0%	$459.38	$0.00	$459.38

SPECIAL MEDICFILL - NO PRESCRIPTION				
Retirement Effective 7/2/12 & Later				
	PERCENTAGE STATE SHARE	TOTAL COST	STATE SHARE	PENR SHARE
Individual	100%	$260.44	$247.44	$13.00
Individual	75%	$260.44	$185.58	$74.86
Individual	50%	$260.44	$123.72	$136.72
Individual	0%	$260.44	$0.00	$260.44

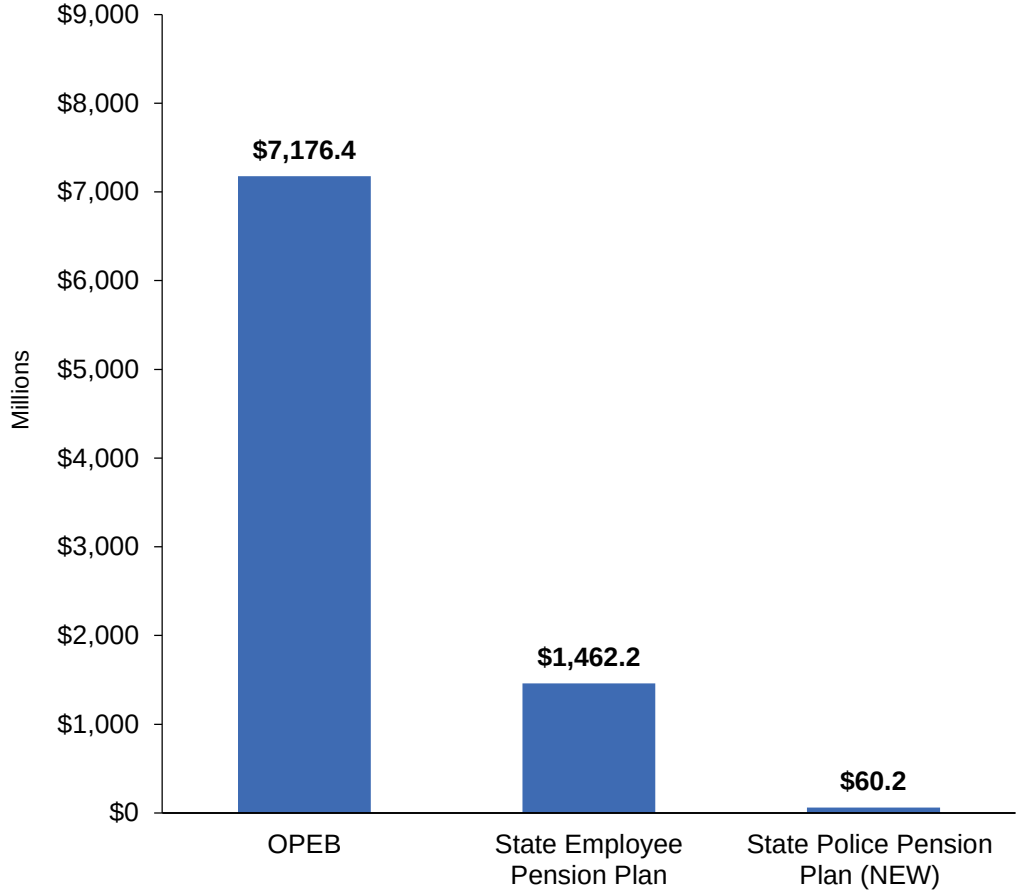
Source: State of Delaware Postretirement Health Plan, Actuarial Valuation Report as of July 1, 2018, Cheiron, December 2018 ; State of Delaware Department of Human Resources. Options outlined in red are the highest enrolled.

OPEB Pressures

Unfunded Liabilities

- As of July 1, 2018, the State of Delaware OPEB plan was just **4.4% funded** with a total unfunded OPEB liability of nearly **$7.2 billion** (includes approx. $0.4 billion TTF)
- In contrast, as of June 30, 2018, the State Employee Pension Plan was **86.0% funded** with an unfunded liability below **$1.5 billion** and the smaller State Police Pension Plan was 88.6% funded with an unfunded retiree liability of $60.2 million

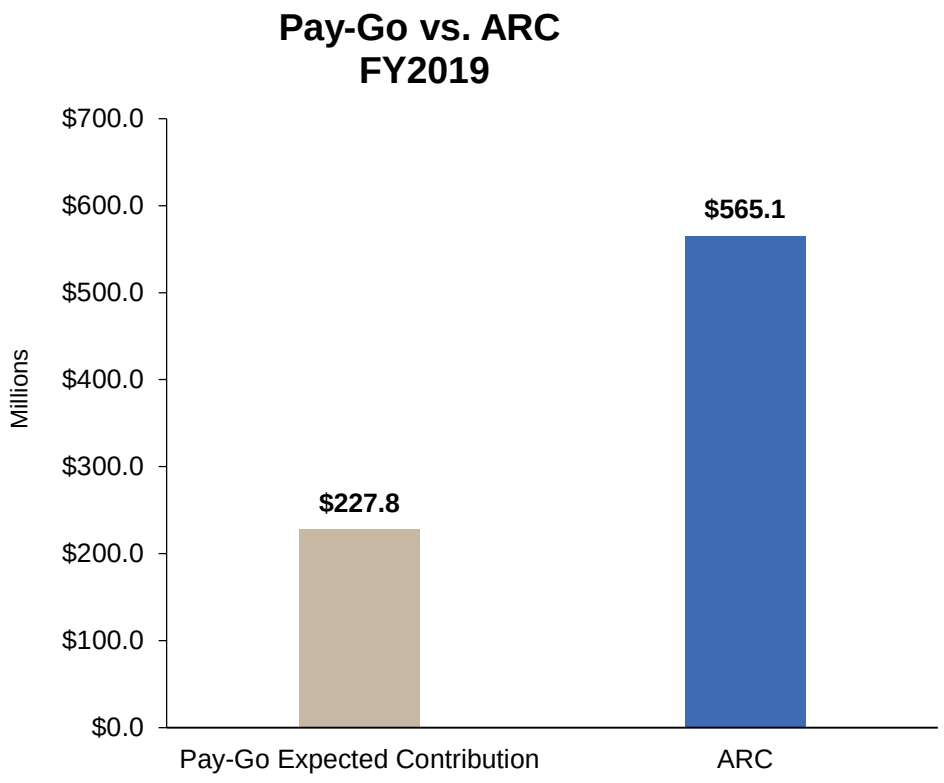
Delaware Unfunded OPEB Liability vs. Unfunded Pension Liability (As of 7/1/2018)



Sources: State of Delaware Postretirement Health Insurance Plan issued December 2018, State of Delaware Employee Pension Plan Valuation Report issued January 2019, State of Delaware Police Pension Plan Valuation Report Issued January 2019. Based on Governmental Accounting Standards Board (GASB) standards, the most recent 2018 State Comprehensive Annual Financial Report relies on the prior valuation. TTF = Transportation Trust Fund.

Current OPEB Payments Barely Half of Actuarial Levels

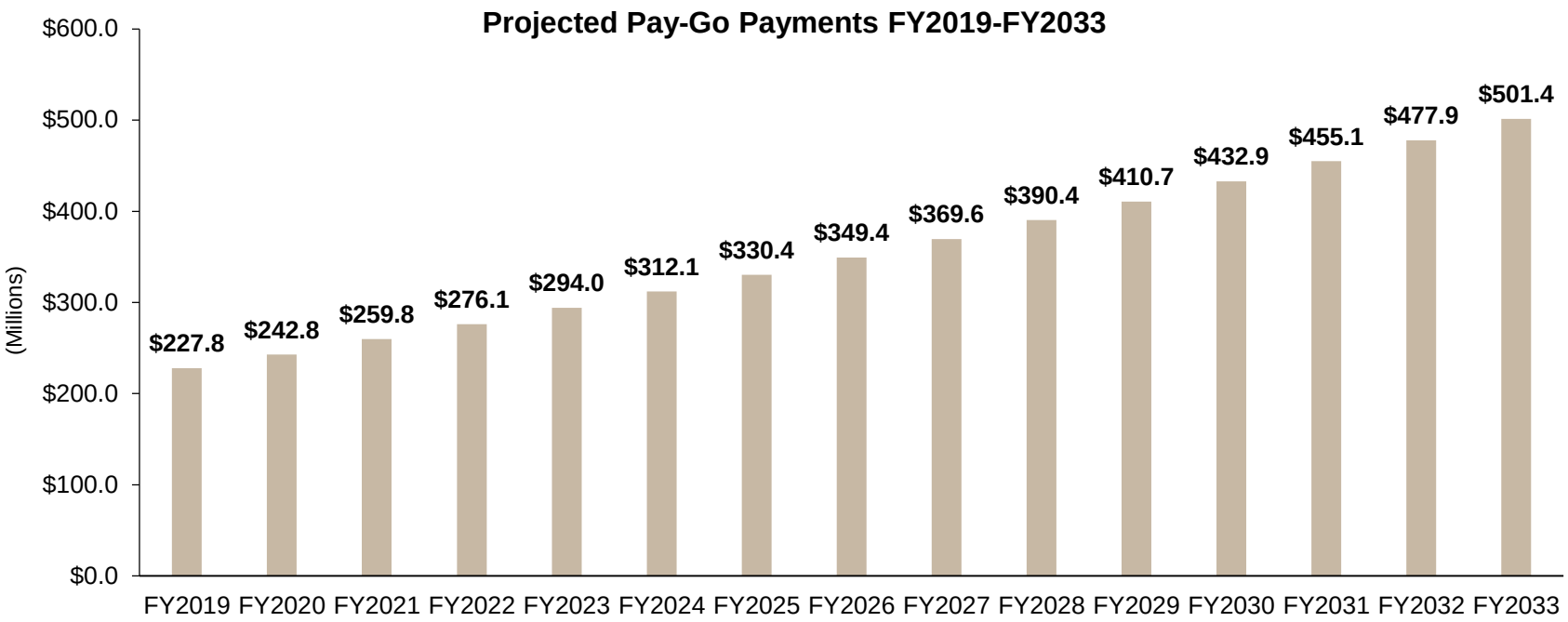
- The State's OPEB actuarial valuation calculates an **Annual Required Contribution of $565.1 million** in FY19 in order to actuarially fund the future benefits for current active employees and pay down a portion of the unfunded liabilities (inclusive of current "pay-go" costs for those already retired)
- The FY2019 payment just for benefits for those already retired total $227.8 million, and the State contributed an additional $7.8 million in prefunding (% of payroll)
- This still leaves State funding **$329.5 million below the ARC**, only 41.7% of actuarially recommended levels



Source: State of Delaware Postretirement Health Insurance Plan issued December 2018

OPEB Cost Projection

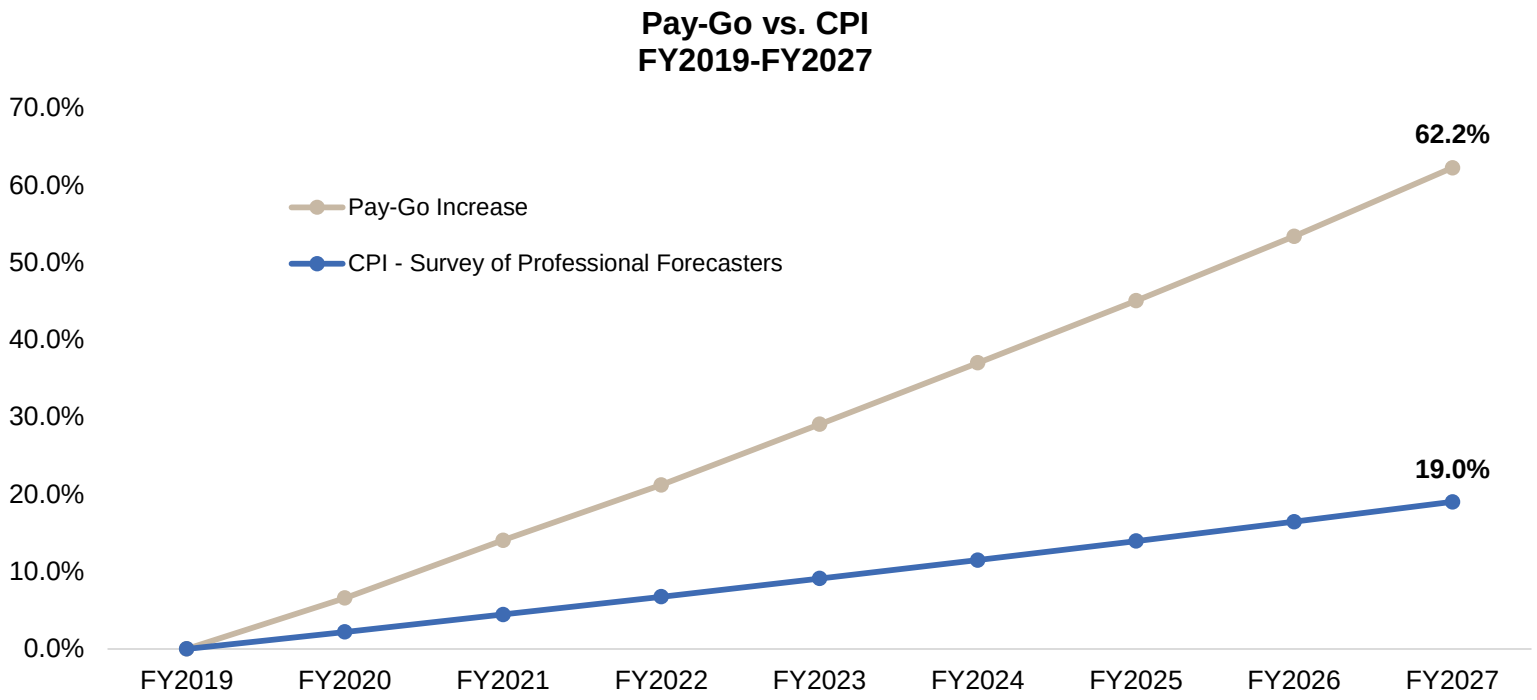
- Even without paying the full ARC, Delaware's $227.8 million pay-as-you go retiree health expenses are projected to double in 12 years and exceed $500 million per year by FY2033 – after already having more than doubled from $100.8 million in 2008
- Prospectively, this represents a compounded growth rate of 5.8% per year. As further discussed on later slides, key factors including growing numbers of retirees, improved mortality, and healthcare



Source: State of Delaware Postretirement Health Insurance Plan Valuation, issued December 2018

OPEB Outpacing Inflation

- Through at least FY2027, OPEB pay-go increases are projected to outpace national inflation by more than 3x –an additional average cost of **$17.7 million** per year



Source: State of Delaware Postretirement Health Insurance Plan Valuation, issued December 2018; Survey of Professional Forecasters, Q4 2018

Rating Agency Perspectives: Metrics are Quantitative and Qualitative

Moody's Ratings Scorecard and S&P Numeric Scores

US state and territories rating methodology scorecard
Delaware (State of)

Rating Factors	Measure	Score
Factor 1: Economy (25%)		
a) Per Capita Income Relative to US Average [1]	95.8%	Aa
b) Nominal Gross Domestic Product ($ billions) [1]	$75.0	Aaa
Factor 2: Finances (30%)		
a) Structural Balance	Aaa	Aaa
b) Fixed Costs / State Own-Source Revenue [2]	13.3%	Aa
c) Liquidity and Fund Balance	Aa	Aa
Factor 3: Governance (20%)		
a) Governance / Constitutional Framework	Aaa	Aaa
Factor 4: Debt and Pensions (25%)		
a) (Moody's ANPL + Net Tax-Supported Debt) / State GDP [2] [3]	11.9%	Aa
Factors 5 - 10: Notching Factors [4]		
Adjustments Up: None	0	
Adjustments Down: Pension or OPEB Characteristics	-0.5	
Rating:		
a) Scorecard-Indicated Outcome		Aa1
b) Actual Rating Assigned		Aaa

[1] Economy measures are based on data from the most recent year available.
[2] Fixed costs and debt and pensions measures are based on data from the most recent debt and pensions medians report published by Moody's.
[3] ANPL stands for adjusted net pension liability.
[4] Notching factors 5-10 are specifically defined in the US States and Territories Rating Methodology.
Source: US Bureau of Economic Analysis, Delaware's audited financial statements and Moody's Investors Service

S&P Global Ratings Numeric Score
Economy 1.8
Financial Management 1.0
Budgetary Performance 1.3
Debt & Liability Profile 2.6
Government Framework 1.4
Composite Score 1.6

(1.0= Strong Rating;
4.0= Weak Rating)

Rating Agency Perspectives: Standard & Poor's (8/1/2019)

"Beyond the near term, the state faces a significant OPEB liability that has grown despite past reform efforts. As it stands, Delaware's net OPEB liability (NOL) as of the June 30, 2018…is $7.2 billion, ***which we consider significant****. This amount is 4.5x higher than the $1.6 billion state share of the aggregate net pension liability of Delaware's pension plans (which are well funded in our opinion).*

On a per-capita basis, we estimate the unfunded liability to be $7,460 and rank it among the ***highest in the nation****…*

Reform efforts included pre-funding the obligation in 2002 and 2003 with lump sum payments and establishing an OPEB trust in 2007 – the funded ratio for this trust is ***currently very low,*** *in our opinion, at 5.0% under GASB Statement No. 74 reporting.*

Although we understand there are no immediate plans to implement additional OPEB reforms, we believe it is possible the state could begin to take additional action to address this liability. ***The state's retirement benefit study committee*** *is expected to present its findings and recommendations at DEFAC's March 2020 meeting, in accordance with Executive Order 32.*

We anticipate that the state will continue to address its OPEB liabilities, which have grown at a rapid pace in recent years, in an effort to curb the long-term liability… In our view, ***inaction in addressing this liability*** *over our two-year outlook horizon* ***could affect the state's credit quality.***

In our view, OPEB plans that operate on a pay-as-you-go basis (such as Delaware's) effectively defer contributions until the moment benefits are due. As unfunded OPEB liabilities grow, contributions in the future can be expected to escalate. We believe the state's ability to effectively manage its OPEB liability will be ***an important credit factor over time."***

Rating Agency Perspectives: Moody's and Fitch (8/2019)

Moody's Investor's Service (8/1/2019)

- *"Relative to highly-rated states, **Delaware's leverage is high*** and consists mostly of unfunded pensions and retiree healthcare liabilities."
- "The high leverage largely stems from the state assuming total responsibility for funding post-employment benefits of local school districts."
- "At the close of fiscal 2018, the state's reported ***net OPEB liability was $7.6 billion, or 10% of GDP and 120% of own-source revenue***…"

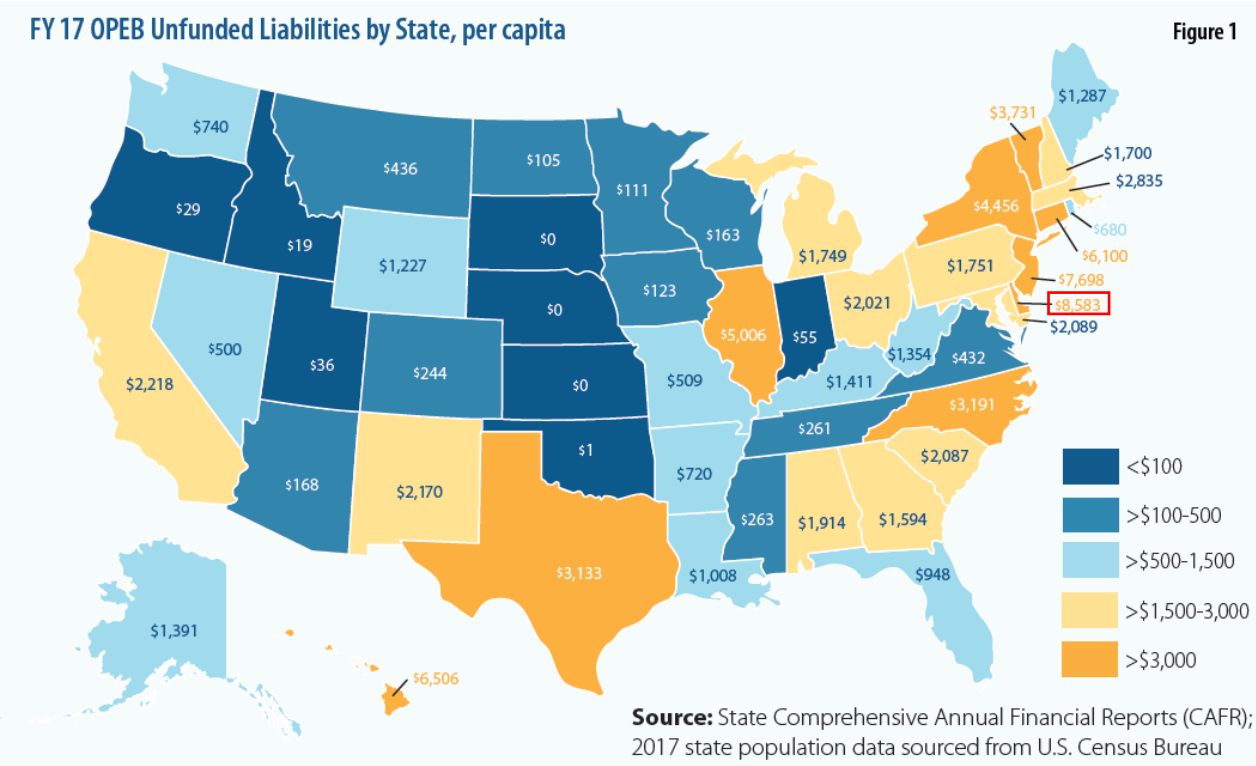
Fitch Ratings (8/5/2019)

- "The unfunded actuarially ***accrued OPEB liability*** of over $7.6 billion ***equals 15% of 2018 state personal income***."
- "While Fitch views the OPEB liability as a more flexible obligation as compared to pensions, ***the relative size of the liability in the context of its relation to personal income and already above-average long-term liabilities is a concern***."

OPEB Across State Governments: Preliminary Findings

OPEB Liabilities Per Capita

- As of FY2017, **Delaware's unfunded OPEB liability per capita is the highest of all states** at more than $8,500
- While this metric is somewhat limited in applicability given the broader role of Delaware state government in comparison to many other states, it is nonetheless **indicative of relatively high OPEB cost pressures**



Source: Center for State & Local Government Excellence and NASRA,"Other Post-Employment Benefits by State (OPEB) FY2017 Snapshot," July 2019.

OPEB Spending as a Share of Total Expenditures

- According to a recent report by the Center for State & Local Government Excellence and the National Association of State Retirement Administrators, **Delaware spent 3.0% of actual expenditures on pay-go retiree medical expenses in FY2017 – tied for 7th highest among states**
- According to the same report, **had the State contributed its full OPEB ARC, it would have been 6.7% of total expenditures – 4th highest among the states** at full actuarial funding (based on FY2014 data)

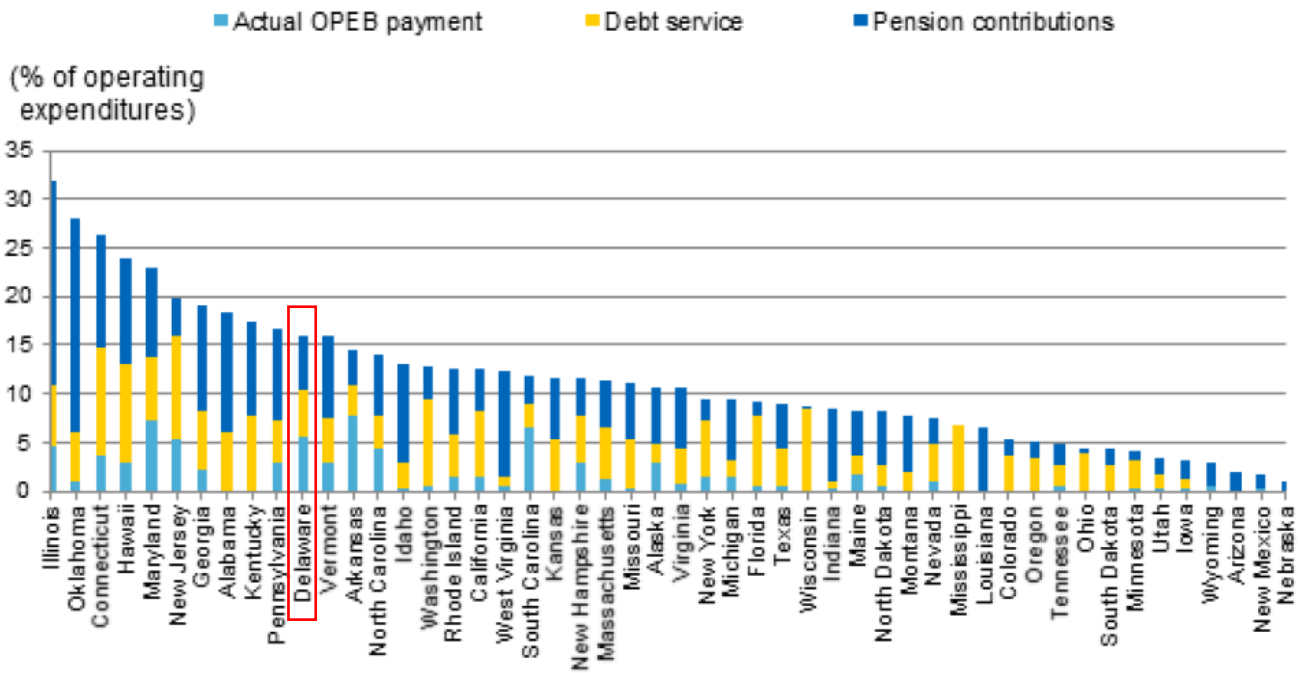
State	Type of Subsidy	FY17 OPEB ADC ($ millions)	FY17 % OPEB ADC Contributed ($ millions)	% of State Expenditures at Actual Expenditures
HI	Percentage of premium	815	81	5.8
ND	Fixed-dollar contribution	341	82	5.4
NJ	Percentage of premium	6,225	32	4.8
MI	Percentage of premium	1,403	101	4.2
GA	Percentage of premium	1,221	102	3.6
CT	Percentage of premium	1,210	57	3.1
DE	**Percentage of premium**	**543**	**44**	**3.0**
SC	Percentage of premium	796	62	3.0
NC	Percentage of premium	995	100	3.0
AK	Percentage of premium	176	84	2.5

State	Type of Subsidy	% of State Expenditures at Full ADC in 2014
NJ	Percentage of premium	14.8
TX	Percentage of premium	11.2
HI	Percentage of premium	7.1
DE	**Percentage of premium**	**6.7**
ND	Fixed-dollar contribution	6.6
AL	Percentage of premium	5.6
IL	Percentage of premium	5.5
CT	Percentage of premium	5.4
SC	Percentage of premium	4.9
NH	Percentage of premium	4.5

Source: Center for State & Local Government Excellence and NASRA, "Other Post-Employment Benefits by State (OPEB) FY2017 Snapshot," July 2019.

Total Long-Term Liability Pressures on the Operating Budget

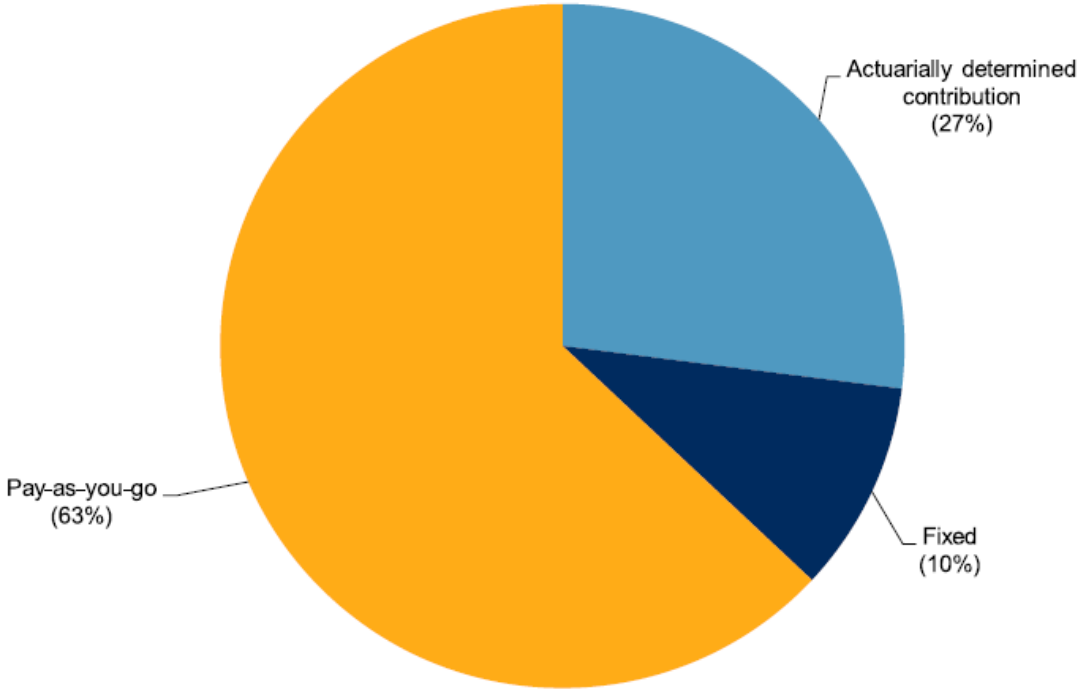
- In FY2016, Delaware's **comparatively high spending on long-term liabilities as a percentage of operating expenditures (rank = 11), was driven largely by OPEB pay-go costs**, given relatively moderate debt service and pension contributions



Source: Standard & Poor's, "U.S. State Retiree Medical and Other Postemployment Benefit Liabilities Keep Rising As States Prioritize Other Obligations," October 2017.

Current OPEB Funding Approaches Among States

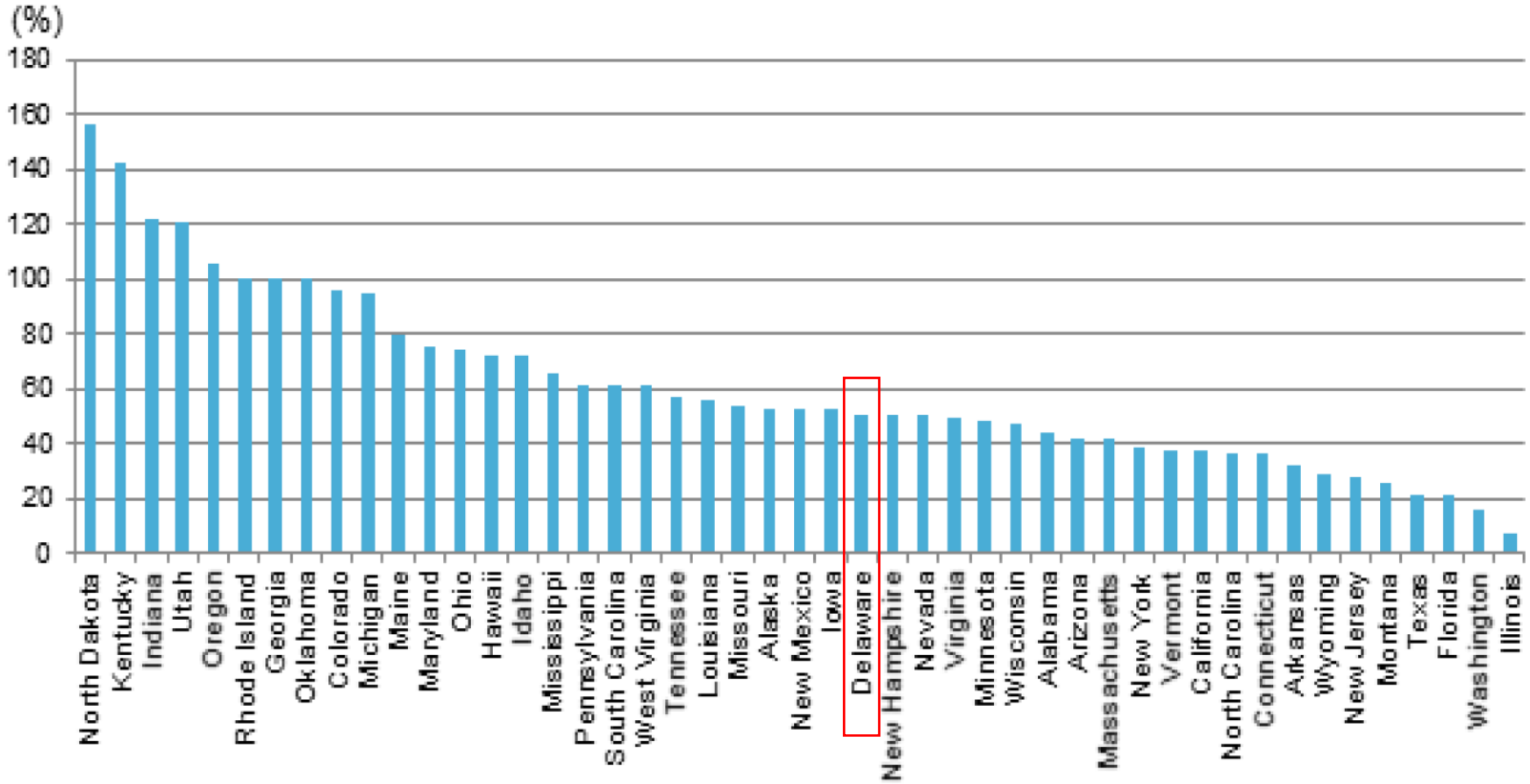
Type Of Funding Method



Source: Standard and Poor's, "Retiree Medical Benefits Generate Unique Cost Drivers And Risks for U.S. States," September 2019.

OPEB Spending as a Percentage of ARC

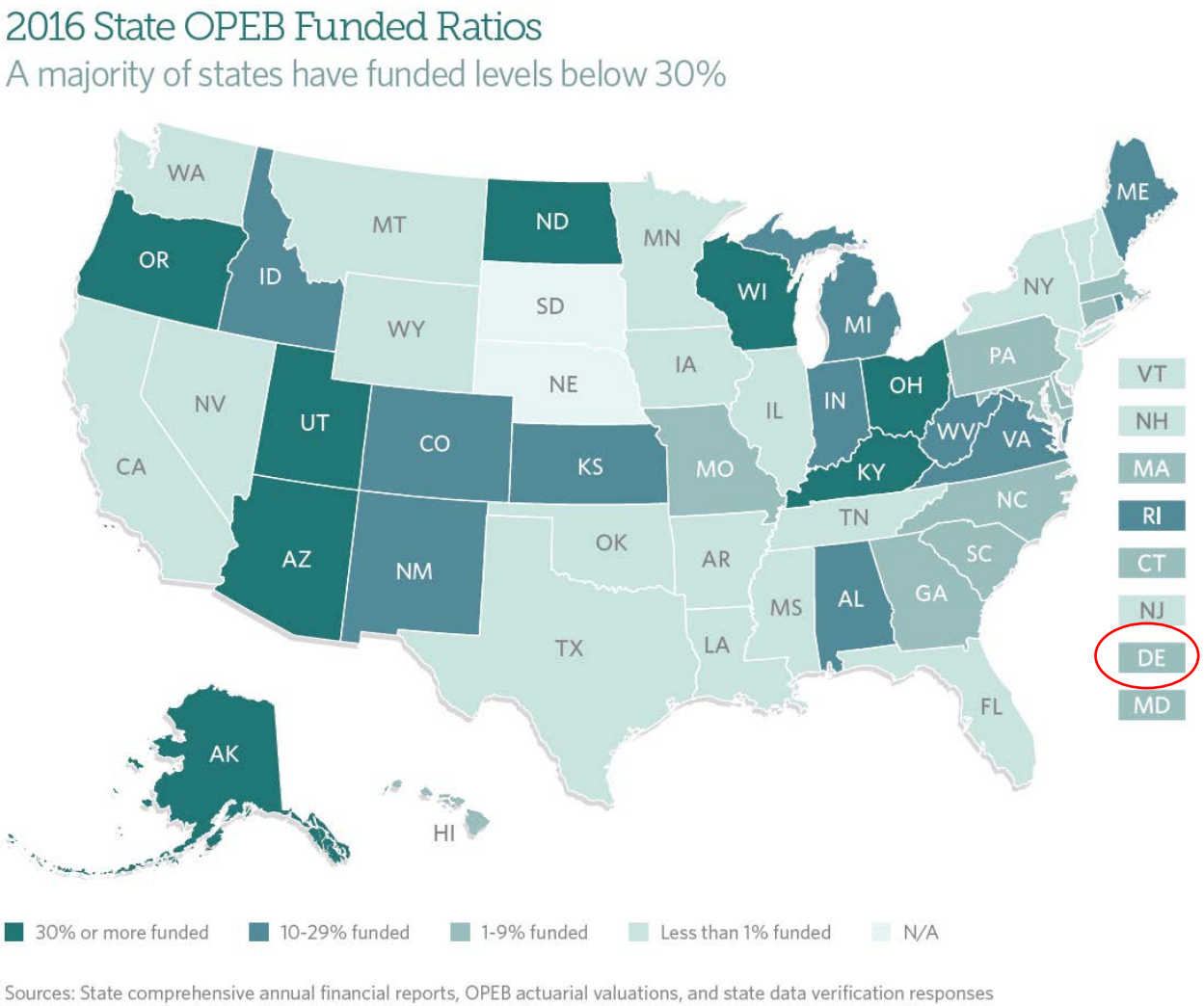
- Delaware's FY2016 **OPEB spending as a percentage of ARC ranked 26th** among reporting states



Source: Standard & Poor's, "U.S. State Retiree Medical and Other Postemployment Benefit Liabilities Keep Rising As States Prioritize Other Obligations," October 2017.

OPEB Funded Ratios

- From an actuarial funding perspective, **most state governments are still in the process of building OPEB reserves**
- As of 2016, only six (6) states were >50% funded
- 19 states had >10% funding
- In that year (and still), Delaware's OPEB funded was <5%

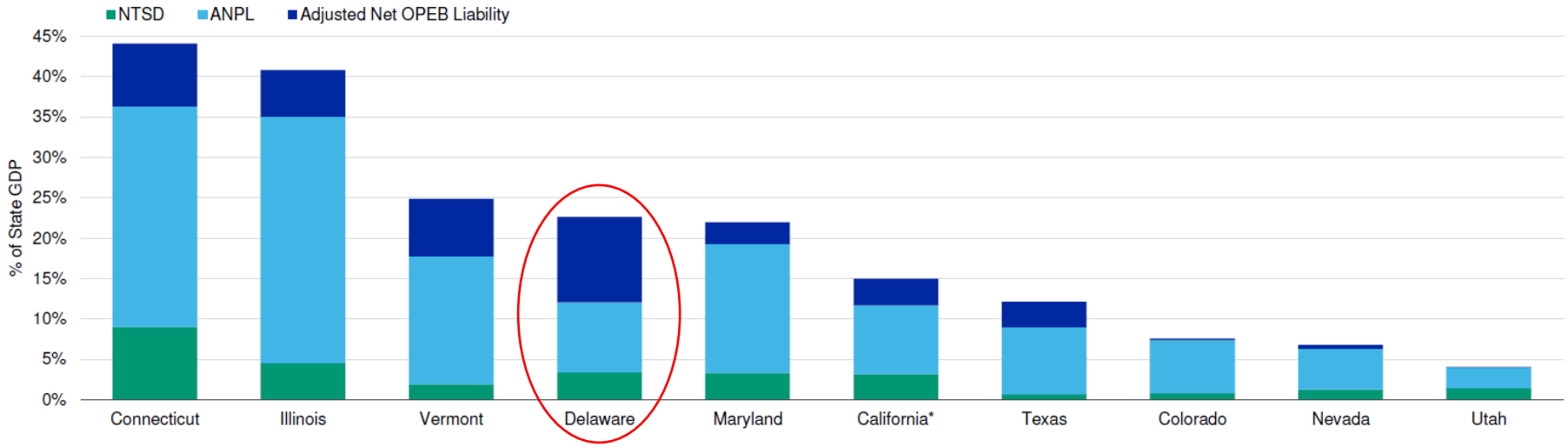


Source: Pew Charitable Trusts, "Update: 50-State Survey of Retiree Health Care Liabilities," December 2018.

Long-Term Liabilities Relative to State GDP

- **Delaware's comparatively large unfunded OPEB liability drives much of the State's overall balance sheet leverage** (net tax supported debt, unfunded pension liability, and unfunded OPEB liability) **as a percentage of state Gross Domestic Product (GDP)**

Unfunded OPEBs are a material portion of overall balance sheet leverage for some states
Net tax supported debt, ANPL and Adj. NOL as % of state GDP



*California's OPEB data excludes the Trial Judges plan, which represents a small segment of the state's overall OPEB exposure.
Source: Moody's Investors Service, state and OPEB financial reports

Source: Moody's Investors Service, "New OPEB Accounting Sheds Light on Credit Impact of Retiree Healthcare Liabilities," October 2018. NTSD = "Net Tax Supported Debt" (excludes debt from school districts). ANPL – "Adjusted Net Pension Liabilities," a figure calculated by Moody's to compare pension liabilities using certain standardized actuarial assumptions. NOL = "Net OPEB Liability" (total OPEB liability net of any pre-funding in a trust).

Delaware Actions Since 2005

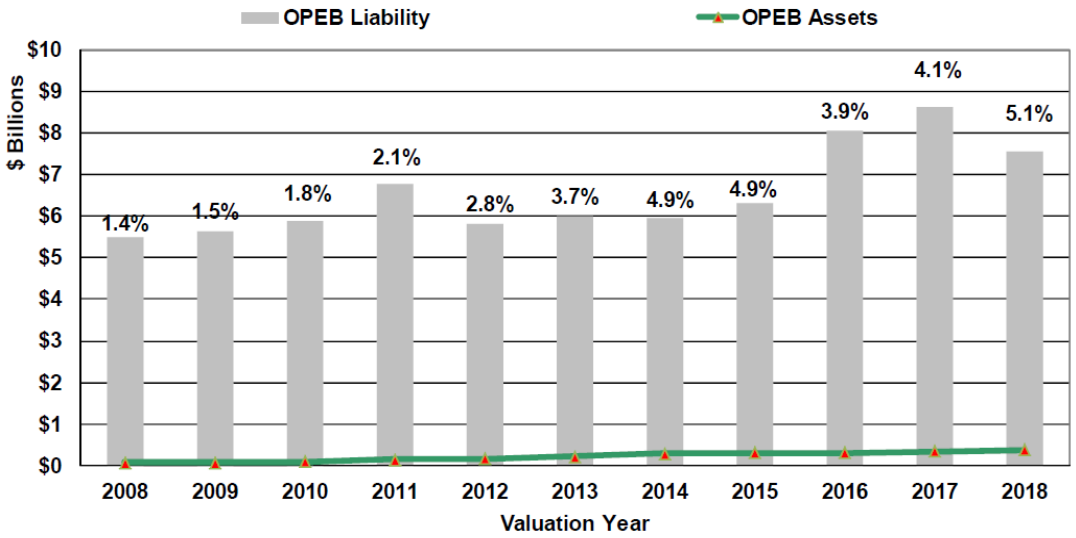
2005 Delaware Retirement Benefit Study Committee | Findings

- The original 2005 Retirement Benefit Study Committee did not reach consensus regarding a detailed path for future OPEB funding. However, **the Committee did reach a higher level, "broad-brush" consensus around the following five areas**:
  - Pay-as-you-go funding was not a sustainable long-term option
  - The implementation practices of the State's pension fund could serve as a model for OPEB funding, or, at minimum, as a measurement tool to track OPEB funding progress
  - Partial funding of the ARC over a number of years was an appropriate and realistic strategy as long as the "ramp up" to full funding would not be excessively long
  - A multi-year funding plan was needed
  - Any changes considered for employee health care coverage should take into consideration changes in the value of the ARC. The State Employee Benefit Committee was encouraged to look at ways to maintain quality healthcare coverage for employees and retirees while exploring cost efficiencies

Source: State of Delaware, Report to the Governor, Members of the General Assembly and Members of the Delaware Economic and Financial Advisory Council, 2005

Steps Taken and Progress to Date

- In 2007, the State **started an OPEB Trust** after beginning to set aside OPEB funding several years earlier
- The State made **plan modifications for new hires** in 2011 (effective for those hired on/after 7/1/2012) and shifted costs of retiree Rx benefits to Medicare in 2013
- Since 2005, the **State has also modified certain actuarial assumptions that affected the size of liability recognized – both positively and negatively** – toward presenting a more realistic view of the challenge, though not a change in ultimate payouts and cost



Nonetheless, the size of the State's net OPEB liability has more than doubled since 2005:

2005: $3.1 Billion

2018: $7.2 Billion

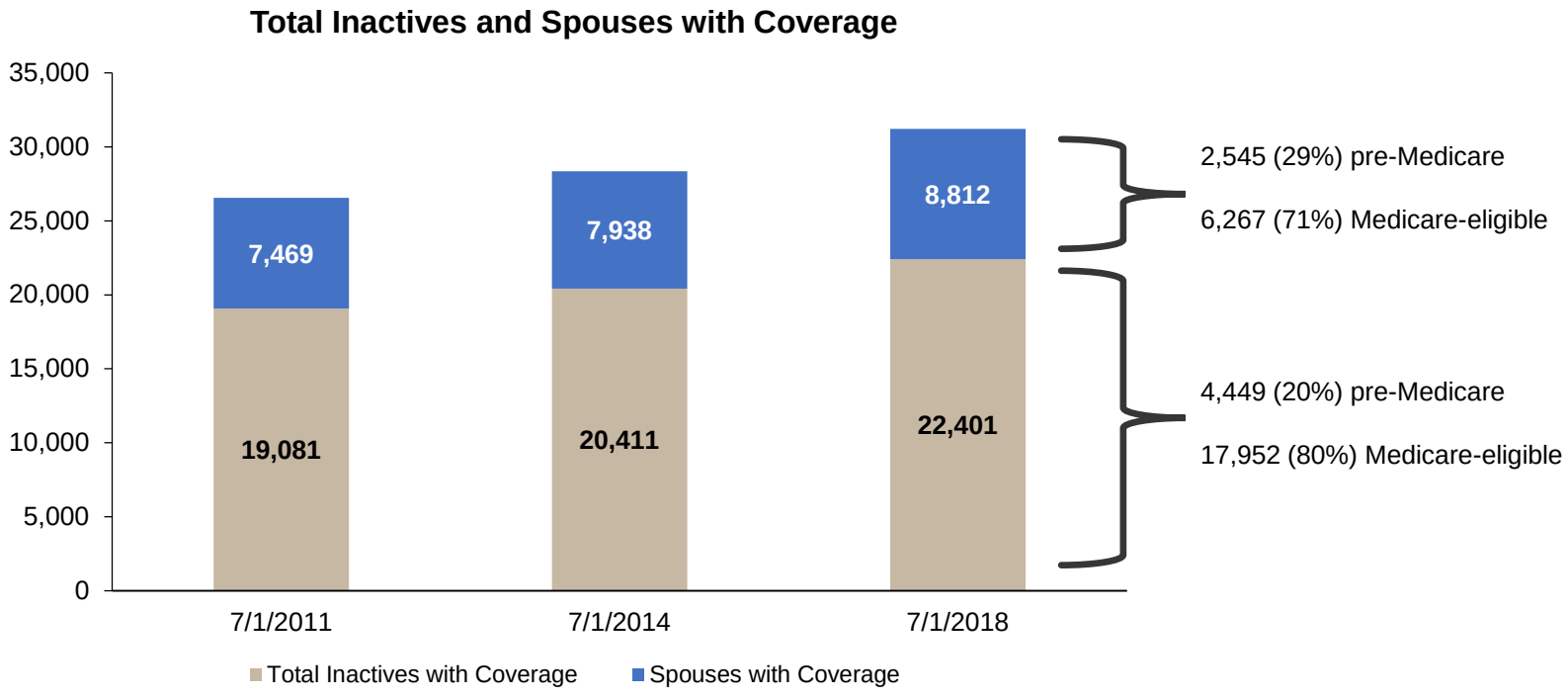
OPEB Trust Assets

- As of the most recent actuarial valuation (through 7/1/2018), Delaware's OPEB trust held $381.8 million in assets, representing a 5.05% funded ratio
- Current estimates of OPEB Trust assets: **$410.1 million**
- The Trust's assets have come from various sources:
  - Percent of payroll contributions
  - Dedication of healthcare program savings
  - Escheat revenues
  - Medicare Part D reimbursements
  - Low Income Program subsidies from Medicare for ACA-eligible retirees
  - Interest earnings on OPEB Trust assets
- The OPEB Trust is managed by the Delaware Public Employees Retirement System, with investments held jointly with those for State pensions

Drivers of OPEB Costs

More Retirees

- With factors including baby boomers reaching retirement age and improving mortality, the **total number of Delaware state retirees continues to grow**



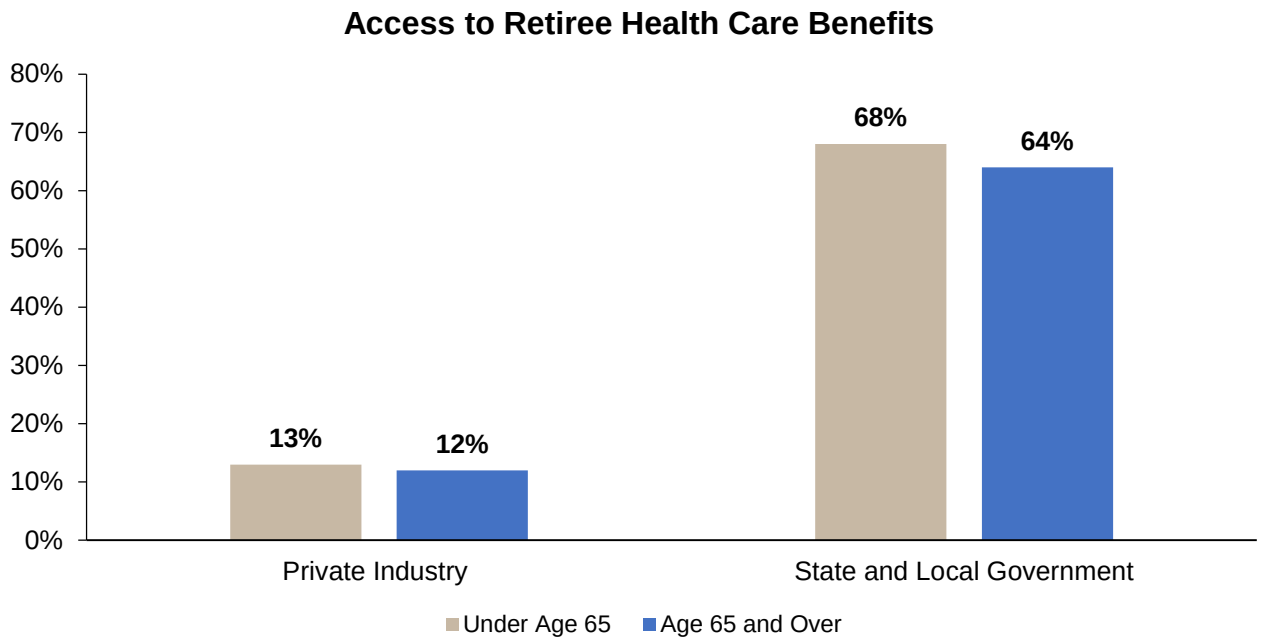
Sources: State of Delaware Postretirement Health Plan Actuarial Valuation Reports, 2011-2018.

Rising Healthcare Costs

- From FY2005 through FY2020, Highmark PPO premiums grew at compound annual growth rates above general inflation (2.0%):
  - Pre-Medicare plan: 4.4% (4.8% from FY2015-FY2020)
  - Medicare plan: 2.8% (4.9% from FY2015-FY2020)
- The most recent Delaware OPEB actuarial valuation report assumes inflation factors of 5.5% and 4.0% for Pre-Medicare and Medicare eligible retiree medical coverage, respectively, beginning in 2019, with Rx costs growing by 7.0%
  - These medical/Rx inflation factors are assumed to decrease steadily each year thereafter to 4.0% by 2039
  - If medical inflation grows just 1.0% faster than assumed, the unfunded liability would be $637.2 million higher

Retiree Health Care Benefits By Sector

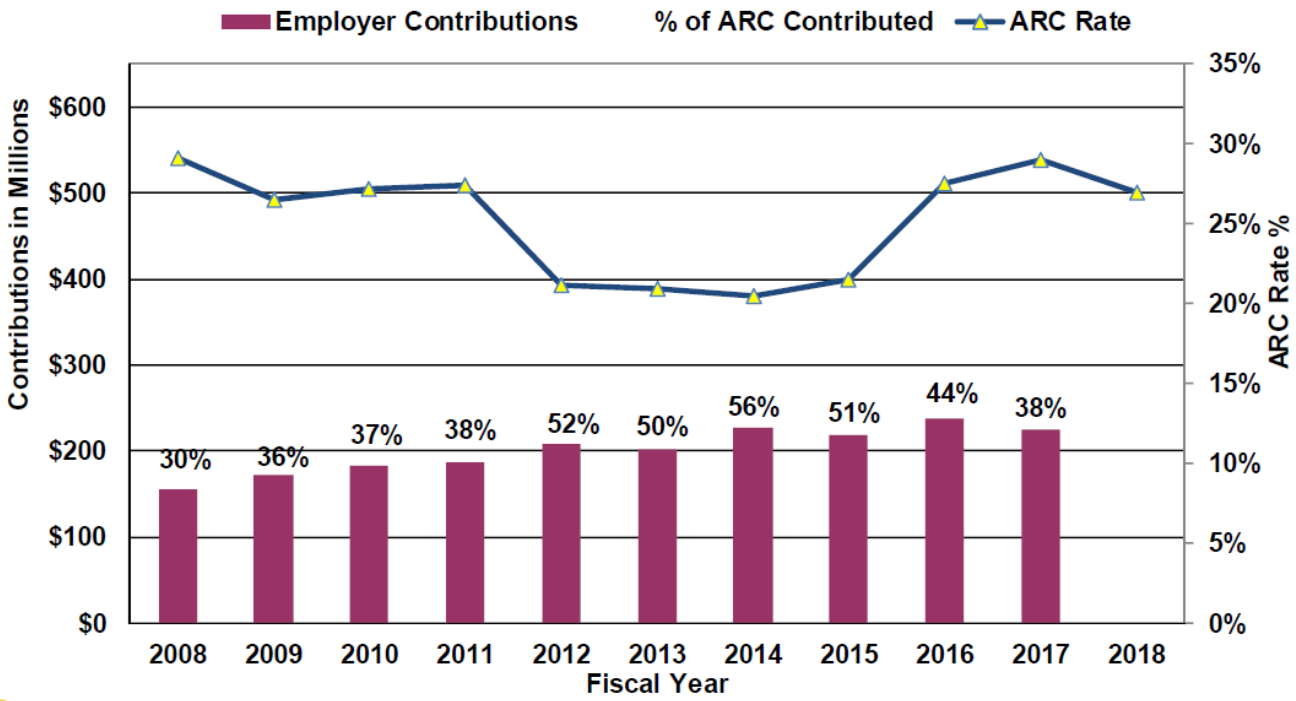
- Compared to private industry, access to retiree healthcare in state and local governments remains prevalent, however, structures and degree of public employer subsidy vary widely
- In subsequent meetings, benefit benchmarking data and case studies of emerging practices will be provided



Source: Bureau of Labor Statistics, National Compensation Survey, March 2019

Funding

- Solving through increased funding alone would have required another $337.3 million in contributions in FY2019 – growing on an annual basis thereafter
- In recent years, contributions have fluctuated between 20% and 30% of the ARC – such that the remaining 70-80% is left unfunded and compounds thereafter



Source: Cheiron, State of Delaware 2018 Postretirement Health Insurance Plan Valuation

Actuarial Assumptions and Considerations

- With greater prefunding and a change in funding policy, a higher discount rate could potentially be reasonably assumed
- The State's OPEB valuations use a discount rate that assumes pay-as-you-go funding, based on the applicable rate of a 20-year General Obligation bond (3.87% as of June 30, 2018; expected to be lower for 2019)
  - Using a discount rate of 7.0% (matching the pension assumption), the unfunded liability would have been $4.6 billion
  - If the discount rate were 1% higher (4.87%), the State's unfunded liability of $7.2 billion would have been $6.1 billion
  - If the discount rate were 1% lower (2.87%), the State's unfunded liability would have been $8.5 billion
- The State's OPEB valuations also now assume a 30-year rolling amortization to calculate the ARC. Under this amortization method, the unfunded liability would effectively never be paid off
- These and other actuarial considerations may merit further analysis by the Committee as part of developing any recommended approach

Potential OPEB Reform Goals | Why This is Important to the State and its Employees

Avoid Erosion of Core Services

- State has limited financial resources
- OPEB pay-go costs are substantially fixed expenses

Maintain Capacity for Salaries

- Pension and OPEB costs can crowd out the opportunity for future raises
- OPEB funding should be linked to the period of current employment

Ensure Long-Term Benefit Security

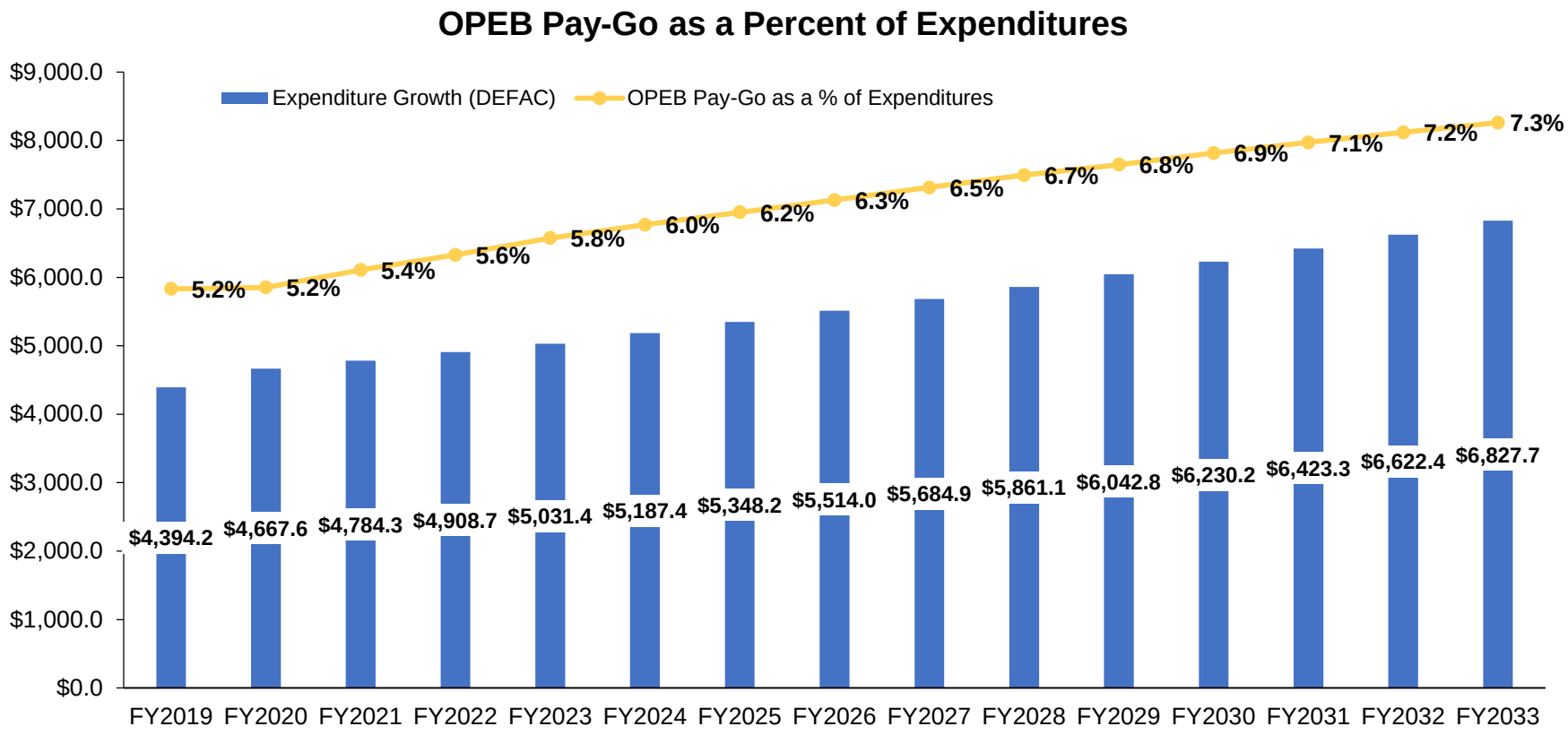
- If costs become unsustainable, benefits can be impaired
- Alternative structures may provide greater flexibility

Improve Public Confidence

- Delaware's OPEB liability has been noted as a credit concern
- Higher credit ratings = lower borrowing costs

Sustainability of the Status Quo?

- As expected pay-go costs continue to grow, it will increasingly crowd out the State's ability to invest in other priorities – from services to the public to current compensation



Sources: State of Delaware Postretirement Health Insurance Plan Valuation 2018; State of Delaware DEFAC Report FY2019. Analysis assumes continued overall General Fund growth mirroring DEFAC's projected FY2024 revenue growth rate annually through FY2033 of 3.1%.

Committee Approach

Discussion and Next Steps

- **OPEB Policy Options**
  - Funding approaches
  - Benefit Eligibility
  - Benefit plan design / healthcare cost containment
  - Actuarial considerations / Discount Rate
- **Goal Setting**
- **Potential Next Meeting Dates**
  - November 12, 2019
  - December 10, 2019
  - January 7, 8 or 9, 2020
  - March 9, 2020

Thank you!

pfm