# FISCAL NOTE

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|---|---|---|---|
| **Bill #:** | SB0072 | **Title:** | Continuation of health insurance as a retirement incentive |
| **Primary Sponsor:** | Mangan, J | **Status:** | As Amended by Senate State Administration Committee AND the Senate Business, Labor, and Economic Affairs Committee |

Sponsor signature Date David Ewer, Budget Director Date

## Fiscal Summary

| | FY 2006 Difference | FY 2007 Difference |
|---|---|---|
| **Expenditures:** | | |
| General Fund | ($319,358) | $373,595 |
| State Special Revenue | $26,285 | $344,070 |
| Federal Special Revenue | $11,682 | $152,920 |
| Other | ($511,527) | $135,084 |
| **Revenue:** | | |
| General Fund | $0 | $0 |
| **Net Impact on General Fund Balance:** | $319,358 | ($373,595) |

- ☐ Significant Local Gov. Impact
- ☒ Technical Concerns
- ☐ Included in the Executive Budget
- ☒ Significant Long-Term Impacts
- ☐ Dedicated Revenue Form Attached
- ☐ Needs to be included in HB 2

## Fiscal Analysis

ASSUMPTIONS:

**Department of Administration**

1. The population of individuals eligible for the retirement incentive is assumed to be those individuals meeting at least one of the following criteria for normal retirement: 1) a member who has attained age 60 and has five years of membership service; 2) a member who has 30 years or more of membership service regardless of the member's age; or 4) a member who is employed as a judge or a protective service worker who has 20 years, or more, of membership service regardless of the member's age. Assume that the eligible population in existence during the July 1, 2005 to October 1, 2005 time frame indicated in the bill, is the same as the normal retiree population in existence as of the December 10, 2004 pay-period end. The years of service and age of the members in the population are advanced forward eight months to the end of August 2005, to obtain the most reliable estimate of years of service and age by the selected termination date assumed in this fiscal note. Data on the retiree eligible population was obtained by the DOA

personnel division from a membership file produced by MPERA for monitoring retirees eligible for the Voluntary Employee Benefit Association program.

2. For purposes of this fiscal note, it is assumed that individuals eligible for this benefit who elect to retire during the time period specified in the bill will terminate service on August 31, 2005. It is further assumed that all positions vacated by individuals eligible for this benefit are filled after a six-week vacant period, or on October 17, 2005. The six-week period was arrived at by assuming that each position description is revised during the time a potential retiree has given notice, the position is advertised for two weeks, two weeks are allowed for reviewing and interviewing potential candidates, and two weeks are allowed for the successful candidate to give notice to his old employer.
3. It is assumed that all retirees have their birthday on September 1st. If they become Medicare eligible during any 12-month period when they are entitled to the insurance benefit, their benefit ceases as of September 1st.
4. Human resources data obtained on the identified retiree eligible population indicates that 58 percent of the eligible population are in positions categorized as Officials/Administrators or Professional. These positions typically recruit from an applicant pool with a greater level of experience and training and it is not reasonable to assume that individuals hired into these positions would be at an entry salary level. For purposes of this fiscal note, it is assumed that new hires into the managerial and professional categories will primarily be transfers from other positions within state government and will be paid at 95 percent of the salary received by the retiring incumbent. The remaining 29 percent of the retiree population are assumed to be filled at the equivalent of an entry salary for their position and grade, which is estimated to be 80 percent of the current salary rate.
5. The average attrition rate within state employment has historically been 12 percent annually in absence of any termination incentive. In any three-month period the termination rate can be annualized to three percent.
6. The insurance benefit is limited to a maximum of four years, or until the member becomes Medicare eligible at age 65, whichever comes first.
7. The total population of eligible normal retirees has been stratified into the following levels:
    a. Individuals greater than or equal to 59 years of age employed in positions classified in EEO categories 1 & 2 for Officials/Administrators and Professionals. Assume that all individuals in this category will retire during the incentive period and their positions will be filled at a rate that is 95 percent of the current salary. However, assume people aged 62 and over will retire in the near future regardless of the status of SB 72. Only the fiscal impact SB 72 has in creating *additional* vacancy savings and salary differential savings are included in this note. The potential savings are calculated net of the vacancy and salary differential savings we would expect to have generated, regardless of the outcome of SB 72, through the natural service retirement of individuals age 62 and over. The actual current salary for employees 59 through 61 years old has been captured from the human resource database and is used to calculate vacancy savings and salary differentials six-years out. The actual years of service as well as age with respect to when someone becomes Medicare eligible, has been used to arrive at the estimated insurance premium cost, and has been limited to a maximum of four years benefit or the member attaining age 65, whichever is less.
    b. Individuals greater than or equal to 59 years of age employed in EEO categories 3 through 8 for Technical, Paraprofessionals, Office/Clerical positions. Assume that all individuals in this category will retire during the incentive period and their positions will be filled at an entry rate. Individuals age 62 and over are omitted from the group for the calculation of vacancy and salary differential savings due to the likelihood that they would be retiring anyway, in absence of SB 72. See item a) above for information on what data was captured to arrive at both savings and cost projections.

c. Individuals less than or equal to 58 years of age in EEO categories 1&2 (see professions in EEO categories above). Assume that the incentive would attract only those individuals interested in leaving at sometime during the year and their termination dates would be condensed into the three-month incentive period. These people are assumed to be far enough away from Medicare eligibility that the gap between when their insurance benefit expires and when they become Medicare eligible would be a disincentive to leaving right away. The annual attrition rate of 12 percent was used as the factor to determine the count of individuals who would receive the insurance benefit in the bill. However, on an annualized basis we could expect 3 percent of these people to retire anyway, so the vacancy savings was calculated for only the additional 9 percent of this population segment whose retirement decision was driven by SB 72. Vacated positions are assumed to be filled at a rate that is 95 percent of the current salary. Vacancy and salary differential savings and the number of years the insurance benefit is provided, are based on weighted averages of these measures for this segment of the population. The weighted average hourly salary rate with fringe benefits is $28.83. A maximum of 48 months for receipt of the insurance benefit was used to calculate the insurance cost.

d. Individuals less than or equal to 58 years of age in EEO categories 3-8 (see professions in EEO categories above). Similar to the assumptions for the population segment covered in item c above, 12 percent of this segment would leave during the incentive period and receive the insurance benefit, and vacancy savings is calculated on the additional 9 percent who choose retirement at this time because of SB 72. Vacated positions are filled at an entry rate which is assumed to be 80 percent of the current weighted average annual salary plus benefits, or $19.60 for this segment of the population. A maximum of 48 months for receipt of the insurance benefit was used to calculate the insurance cost.

8. There is no grandfathering of insurance benefits calculated into this fiscal note. Insurance benefits begin in the month following termination.
9. The core plan for non-Medicare retirees currently costs $455/month and includes medical, prescription, dental, and basic life coverage. The age for Medicare eligibility is assumed to remain at 65 throughout the benefit payout period. If Medicare rolls to an older age the insurance benefit cost to the state, as a result of this bill, will increase beyond what this fiscal note projects. It is assumed that the state share contribution from July 1, 2005 through December 31, 2005 is $460/month; $506 for January 1, 2006 through December 31, 2006; and $557 for January 1, 2007 through December 31, 2007. In each calendar year beyond 2007 the state share contribution is assumed to increase by 15 percent annually, which is equivalent to the claims trend rate projected by the State Employee Group Benefit Advisory Group. The core plan for non-Medicare retirees costs 99 percent of the state share contribution. The table below shows the results of calculations for the monthly health insurance premium rates.

| | Wt. Avg. Non-Medicare Rate |
|---|---|
| FY 2006 | $483 |
| FY 2007 | $526 |
| FY 2008 | $593 |
| FY 2009 | $682 |
| FY 2010 | $784 |

10. This fiscal note assumes that HB 2 passes and contains language stating that appropriated amounts for personal services reflect reductions totaling at least the cost of the incentive projected in this bill.
11. Potentially, there could be an increase in post-employment health care claim costs as a result of this bill. Currently, some retirees, who are not yet Medicare eligible, choose to discontinue their health insurance

coverage with the State of Montana and the health plan does not bear the cost of their future claims. A small percentage of the people who would retire with this incentive might have chosen to discontinue their insurance coverage in absence of this bill. The impact of this future increase in post-employment benefit payments has not been factored into this fiscal note due to uncertainties in predicting these figures.

12. Funding for both the savings and insurance cost is prorated to its source based on FYE 2002 total state personal services extracted from SABHRS:

| | |
|---|---|
| General Fund | 37 percent |
| State Special Revenue | 36 percent |
| Federal Special Revenue | 16 percent |
| Other | 11 percent |

13. There would be some savings generated by the "ripple down" effect of a high-level position being vacated and a lower paid employee moving up to fill the position; then a lower paid employee moving up to fill that person's position, and so forth. The savings generated by this type of scenario cannot be reasonably estimated due to all the uncertainties in the assumptions that would need to be modeled. This fiscal note does not include any savings from this possible "ripple down" effect.
14. Amendments to the bill designate that the personal services contingency appropriation found in HB 13 be used to offset any unrealized savings.

**Montana University System**

1. These calculations include eligible MUS employees on Payroll as of January 1, 2005, projecting age and years of service toward August 31,2005: PERS members who have attained age 60 and have at least 5 years of service; PERS members who have 30 or more years of service, but are not over age 65; PERS who are up to 4 years, but not past age 65; PERS who are at least 65, regardless of years of service.
2. All retirements are assumed to occur on August 30, 2005.
3. For staff under PERS, the savings is calculated in FY 2006 on the basis of the position being vacant one month and the new hire paid at 80 percent of the retiring employee's salary. In FY 2007, costs are calculated on the FY 2006 salary plus 4 percent for 9 months of the year.
4. It is assumed that 35 percent of eligible employees will take advantage of the provision.
5. The cost of insurance is $506 for FY 2006, $557 for FY 2007, and a 15 percent increase each year thereafter.
6. For purposes of this fiscal note, 60 percent of funding is assumed to be funded with non-state, non-general fund sources (research, tuition, etc) and 40 percent with general fund.

FISCAL IMPACT:

| | FY 2006 Difference | FY 2007 Difference |
|---|---|---|
| **Department of Administration** | | |
| Expenditures: | | |
| Personal Services | | |
| Vacancy Savings | ($2,146,927) | $0 |
| Salary Differential Savings | (1,716,990) | (2,418,532) |
| Health Benefit | 3,936,931 | 3,374,283 |
| TOTAL | $73,014 | $955,751 |
| | | |
| Funding of Expenditures: | | |
| General Fund (01) | $27,015 | $353,628 |
| State Special Revenue (02) | 26,285 | 344,070 |

| | | |
|---|---|---|
| Federal Special Revenue (03) | 11,682 | 152,920 |
| Other | 8,032 | 105,133 |
| TOTAL | $73,014 | $955,751 |

**Montana University System**

| | | |
|---|---|---|
| Expenditures: | | |
| Personal Services | | |
| Salary Differential/Vacancy Savings | ($1,979,132) | ($1,280,198) |
| Health Benefits | 1,113,200 | 1,330,116 |
| TOTAL | ($865,932) | $49,918 |
| | | |
| Funding of Expenditures: | | |
| General Fund (01) | ($346,373) | $19,967 |
| Other-University Funds | (519,559) | 29,951 |
| TOTAL | ($865,932) | $49,918 |
| | | |
| Net Impact to Fund Balance (Revenues minus Funding of Expenditures: | | |
| General Fund (01) | $319,358 | ($373,595) |
| State Special Revenue (02) | ($26,285) | ($344,070) |
| Federal Special Revenue (03) | ($11,682) | ($152,920) |
| Other | $511,527 | ($135,084) |

LONG-RANGE IMPACTS:

**Department of Administration**

The future savings and costs of SB 72 through FY 2010, when the insurance benefit would no longer be available since the bill is amended to cap the benefit at four years, are shown below:

| | FY 2008 | FY 2009 | FY 2010 |
|---|---|---|---|
| Expenditures: | | | |
| Salary Differential Savings | ($2,418,532) | ($2,418,532) | ($2,418,532) |
| Health Benefit | 2,713,137 | 1,909,493 | 372,037 |
| TOTAL | $294,605 | ($509,039) | ($2,046,495) |

Beyond FY 2010, the possibility of accurately predicting savings from salary differentials, between the rate paid to retirees now and the rates their replacements over time will make, is not likely. Assuming the new hires do not terminate from their positions, as their years of service increases, this salary differential can be expected to diminish.

**Montana University System**

The future savings and costs of SB72 through FY 2009 are shown below:

| | FY 2008 | FY 2009 |
|---|---|---|
| Expenditures | | |
| Health Benefit | $1,328,640 | $1,254,144 |

<u>TECHNICAL NOTES:</u>

**Department of Administration**

1. This fiscal note does not cover the impact to the retirement systems of individuals retiring earlier than they would in the absence of SB 72. This impact would need to be analyzed by actuaries with knowledge of pension systems. It appears that the total pension payouts as a result of this bill could increase over actuarially projected payouts in absence of this bill.
2. According to a report recently issued by the Department of Administration, the number of state employees eligible for full and early service retirement will jump from 36 to 61 percent by May of 2008. The State of Montana has done little to no succession planning in order to prepare the enterprise for the knowledge transfers needed to take place to accommodate the bubble of baby-boomers eligible to retire within the next five years. The effects of SB 72 could exacerbate this problem.
3. In the event that SB 72 becomes effective agencies will need more funding for health insurance premiums in the pay plan bill.
4. References to HB 13 should be changed to HB 447.

**Montana University System**

5. The retirement window of July 1, 2005 – October 1, 2005 is problematic for the University System, in particular relative to faculty. The time period is immediately prior to and during the initial month of fall semester. It will be impossible to hire new tenurable faculty during this time frame. Faculty throughout the nation routinely engage in job searches prior to the end of an academic year (i.e., March-May). Adjunct faculty, in lieu of tenure track faculty, are easier to recruit. However, certain disciplines may still be problematic resulting in the cancellation of some scheduled classes.