Retired Employees Association of Orange County, Inc.

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August 16, 2010

County of Orange Board of Supervisors
10 Civic Center Plaza 5th Floor
Santa Ana, CA 92701

Attn: Janet Nguyen, 1st District Supervisor & Board Chair
Bill Campbell, 3rd District Supervisor & Vice Chairman
John M. W. Moorlach, 2nd District Supervisor
Shawn Nelson, 4th District Supervisor
Patricia C. Bates, 5th District Supervisor

RE: Board Hearing of August 17, 2010 Agenda Item #34

Dear Honorable Board of Supervisors:

We want to thank you for continuing this item from the July 27th Board of Supervisors meeting until the meeting tomorrow, August 17, 2010. As we identified in our last letter, retirees were not represented on the PPO Rate Setting Committee, even though this Board explicitly directed that retirees participate in that process. Instead, the County permitted retirees to participate only in the HMO Request for Proposal process. Contrary to your understanding, we have learned your Executive Assistants were not part of the actual rate setting process; rather, their role was minor and consisted of a short briefing, *after* rates were determined by Human Resources (HR) and Mercer.

This failure to provide transparency and participation is clearly the reason we have major differences today. Indeed, HR agreed to permit REAOC only one-hour to discuss the massive rate increases for 2011, and agreed to address only a fraction of the written questions REAOC submitted in advance of that meeting. Unable to obtain critical information from HR directly, REAOC was forced to make a public records act request to obtain information to determine what documents exist regarding tens of millions of dollars in reserve funds. It is clear from its response to that request that HR will continue to refuse to make available for review many of the requested documents, possibly forcing REAOC to seek judicial intervention to enforce its request.

Because Fund 292 is a commingled pool of monies belonging to active employees, the County and retirees, the County's unilateral and opaque management of that fund creates the impression and threat of self-dealing, that is, of the County managing the commingled fund for the financial benefit of itself and to the detriment of retirees. And in fact, the County months ago gave itself and some active employees the benefit of some $17 million of the fund's reserves, in the form of a premium rate "holiday," but as of this date has given retirees none of the benefit of their share of the excess reserve. Under these circumstances, it is critical that the County accounting processes be totally transparent to retirees and be subject to forensic oversight by a third party. To date, the County has done neither of these things.

Despite these issues, retirees need medical insurance in 2011. In limited review we found the following four issues that make HR's recommendations to the Board inappropriate. Please remember the last time we requested a rate reduction for rate year 2008 it was granted *over the objections of HR*. That year, with REAOC's proposed rates, reserve fund still *grew* by $3 million.

Given this information we urge you to adopt the same premium rates for retirees for 2011 as currently exist for 2010. This action is appropriate for the following reasons:

1. Retirees are due a reduction of premiums of $8,631,604 to match the $17.2 million paid in 2009/2010 to the County and employees out of fund 292. The retention of existing 2010 rates will result in retiree contributions of $17 million rather than $21 million, thus giving retirees the benefit of approximately $4 million of that $8.6 million (depending on actual claims expenses for 2011). While a rate reduction of $8.6 million is clearly justified, to do so would mean that retiree rates would actually drop by $4.3 million for 2011 and then, if the HR assumptions are correct, will result in an increase of $8.6 million or over 50% in 2012. This roller coaster effect will wreck the personal finances of retirees on fixed incomes and force them out of coverage. Stretching out the savings will allow more current retirees to attain Medicare coverage which helps to hold down their costs and allow more savings under the National Health Care Law to be manifested and be used to lower subsequent rate increases.

2. The County will receive considerable additional Federal funding for Retirees to offset costs, from the National Health Care Act of 2010. These funds are not accounted for in 2011 rates, despite the fact that the State of California and through State administered plans many other public entities include this revenue in their budgetary projections.

3. The County's own numbers demonstrate that the Health Insurance Trust Fund 292 reserves will be more than adequate to meet obligations *without* the proposed $4 million in retiree premium increases.

4. The Human Resources proposed rate increase is flawed and continues to fail to recognize the factors that led to the excess fund balance in the first place.

The following further explores each of these reasons.

1. <u>Fund 292 "Rebates"</u>: The Human Resources Department determined in 2007 that the Health Insurance Fund 292 had excessive revenues to meet its obligations. Your Board at the time authorized a rebate of premiums to current and former participants in the plan. REAOC expressed concerns regarding the rebate approach, including potential tax consequences that had not been addressed and problems with determining which active and retired participants would receive the rebate. The Auditor Controller also expressed concerns regarding the practicality of implementing a rebate. Later, at the urging of HR, your Board abandoned the rebate plan.

   The County instead decided to implement a "premium holiday" for active employees. Because the County pays the majority of active employee premiums as part of employees' compensation package, the County retained the majority of the rate holiday funds, and active employees paid nothing for coverage for a six-month period. However, despite expressly acknowledging that retirees are entitled to the benefit of a large portion of the reserve surplus, the County has not provided any rate holiday for retired employees. By not applying the rate holiday to all enrollees including retirees, the County has yet to treat plan participants even handedly. The County can (and must) meet its fiduciary responsibilities by providing a cash benefit to retirees that matches the cash value of the active employee rate holidays.

The equivalent cash value can be determined by looking at exactly what was not paid by employees and what was paid by retirees. The Human Resources report shows the $17.2 million in premiums that would have been paid by employees and the County if the rate holiday had not been implemented for employees. It is also possible to see from the Human Resources report that during these same months, retirees and the Retiree Medical Trust contributed $8.6 million in premiums to the 292 health fund. Employees and the County received 12 months benefit in claims and paid for 6 months worth of contributions. Retirees on the other hand received 12 months of claims and paid for 12 months worth of contributions. Retirees are due their proportionate share of reserves or in effect retirees are paying not just their own claims experience but for half of the employees claims experience as well.

REAOC expressed to Human Resources on August 9, 2010 that it wishes to use this amount due to retirees now in the way of rate relief. Rate relief is the smoothing of payments for coverage that permits planning and proper use of personal assets and better matches to the actual pensions received monthly. For the past year and it is anticipated for next year pensions were not increased because of the cost of living formulas in place when current retirees retired. Human Resources has refused to make that recommendation, and indeed has refused to make any recommendation as to what approach to take with regard to retirees' portion of the excess reserves. Months have gone by since active employees received their "share" of the excess reserves. Your Board must now ensure that retirees receive fair and equal treatment with regard to those funds.

2. <u>New Federal Funding</u>: The National Health Care Act adopted in March 2010 provides reinsurance of retirees ages 55 through 64. Under this new law claims for early retirees in a group health plan are eligible to receive 80% offset of claims costs for claims between $15,000 and $90,000, per a letter from Carl Crown to REAOC in July 2010. REAOC asked the County to provide the sum of reimbursements that would have been received had the program been in place for the period June 2009 through May 2010. REAOC representatives were told the information had been analyzed and the plan savings could be considerable, but they refused to share that analysis with REAOC.

   The new law requires the employer savings be passed along to retirees, however, Human Resources has told REAOC that retirees will not receive any benefit from the new law until January 2012, some *17 months* after the County is scheduled to receive payments on behalf of retirees. This delay given the proposed rate increases will be devastating to retirees. With the rate increase retirees will see a net increase of up to $3,700 per year for retirees with full Medicare coverage and $6,600 per year for retirees who do not qualify for Medicare. In addition, the Retiree Medical Trust payments will increase on average between $4 and $9 per month.

   Already retirees pay far more for coverage than employees or the County and for most retirees the 24.6% increase amounts to more than a 30% increase because they are paying for an ever increasing portion of the costs of coverage. Some retirees will see premiums of $30,000 per year and pay $26,000 more than the $4,000 paid by employees and $16,000 more than the $14,000 the County pays for those employees (Attachment 1 and 2). Should the proposed rate increase go into effect, Fund 292 will receive a windfall and the retirees will receive nothing, while the new laws' intent to retain coverage for retirees will be thwarted. Orange County should follow the example set by the Governor and the State of California which applies in the majority of California Counties, by appropriately budgeting *this year* for the federal pre-65 offset.

3. Excessive Reserves: According to the most recent CEO quarterly report the fund balance in 292 even after the $17.2 million rate holiday for the County and employees, is $20.6 million, more than enough to account for $4 million of the relief due to retirees this coming year. This balance is 35% over the nearly $59 million in claims actually paid during the prior year per Exhibit II ASR 40 and Exhibit II ASR 41 from July 27, 2010 for actives and retirees against a targeted reserve of 15%. If the fund is reduced through rate smoothing and claims continue at current levels, with no adjustments for new federal grant revenues, the fund balance will be $18.4 million by December 31, 2011 still well in excess of the 15% target. Should the Human Resources' assumed 18 month trend projection of over 11% increase occur, then the fund would have a balance of $16.3 million, or 28% of actual prior year claims and far in excess of the 15% reserve which the Human Resources report targets as being more than adequate.

   Further, the Human Resources report states that the reserves serve two purposes, reserving for those claims that have already been incurred and not paid, and a Premium Stabilization reserve that can be used to offset unusual claims and smooth contributions. The REAOC requested action keeps both reserves in place and uses the premium stabilization fund for its stated purpose to stabilize rates to recognize previous overpayments and to account for a large adjustment credit due to the fund in the coming months.

   In light of these numbers, it is clear that the rate smoothing that REAOC requests will give retirees their fair share of the excess reserve, to match the payout that active employees and the County have already received, and will have *no* impact of the county's 2010/2011 budget.

4. Flawed Revenue and Expense Projections: The Human Resources Department's recommendations are flawed for many reasons. The flaws are clearly demonstrated by the fact that HR implemented a $17 million rate holiday for active employees in 2009/2010, and now is imposing a very large rate increase for 2011 of (18.7% for the actives and a 24.6% for retirees). The Human Resources department could have and should have used the stabilization reserve fund more prudently and avoided this "roller coaster" approach to insurance rate setting.

   Further we have found the materials submitted by Human Resources to be incomplete and misleading. For example on Exhibit I to ASR 41 from July 27, 2010, the third line lists total claims of $20,246,819. Yet on Exhibit II Wellwise & Sharewell Combined show claims of $20,631,429. Based on this nearly $400,000 discrepancy it is not clear which exhibit reflects the accurate listing of revenues and claims (if either). Further the Exhibit 1 does include revenue that is directly tied to claims of $1,695,000 or interest credits of $140,000 and yet these revenues are omitted and thus overstate the so called loss ratio printed on Exhibit II.

   On July 27, 2010 your Board adopted 2011 insurance rates for employees in the Wellwise and Sharewell plans see "ASR 40". These employees share the same funding, claims and reserve pools in fund 292 as retirees. The rate action recommended is misleading. For example Exhibit II to that report shows premiums for actives of $34,553,142. Yet in fact the actual premiums paid were $17.3 million.

   The Human Resources report estimates that at year end the fund balance will be between $16 and $18 million. The HR report does not state the current $20,620,096 fund balance as of March 31, 2010 per the CEO quarterly report. Further, it does not explain how the current fund 292 balance will fall by $3-$5 million despite the recommended $29 million in increased revenues for 2011. These sorts of "estimates" are what caused the fund balance to grow so large in the first place. This trend will only continue—to the severe detriment to retirees—unless 2011 rates reflect *accurate* revenue and expense projections.

We recognize the need to adopt rates for 2011. The Human Resources recommended rate increase will cost retirees and the Retiree Medical trust an additional $4.3 million. The $8.6 million due retirees and the Retiree Medical Trust are properly only to be paid for medical coverage of retirees, and failure to use these funds for anything other than medical insurance purposes would result in the misuse of funds held in trust. Applying credits for these funds owing in the 2011 and 2012 years would permit credits in an expeditious manner and grant some relief to retirees who desperately need it.

Yours Truly,

Linda Robinson Doug Storm

Linda Robinson and Doug Storm
Co-Presidents, REAOC

Attachments

Cc: Tom Mauk, CEO
Carl Crown, HR Director
Darlene Bloom, Clerk of the Board
Nicholas S. Chrisos, County Counsel
David Sundstrom, Auditor Controller
Steve Delaney, CEO, OCERS
Orange County Register
LA Times