Post-Retirement Health Care Savings Plan

March 10, 2003

The merits of a post-retirement health care savings plan (PRHCSP) are evident. A key concern to present (and certainly future) retirees is the cost of health care, which now comes from their post-tax dollars. This is often a rude awakening for faculty entering retirement, as during employment the University not only covers the major portion of the cost, but most additional costs come from an employee's pre-tax dollars.

A PRHCSP has the advantages that each of our present 401a, 403b and 457 plans have; all University and employee contributions come from pre-tax dollars and earnings on the balance invested are not subject to income taxes. The contributions can be invested in one or more funds chosen by the employee from a select group of investment options. A PRHCSP has another very important advantage; upon retirement or termination of employment from the University, withdrawals to pay for health insurance premiums and other appropriate health care costs are not considered to be taxable income. Thus, the PRHCSP avoids taxation on contributions as they go in, on accumulated investment earnings, and on tax post-employment distributions when used for health care

We believe there is no question that the University should embrace this plan. However, there are questions about the amounts to go into the savings plan and the source of these funds. The rules of the program say that each individual in a given "class" must put in the same amount ($ or % of salary). This "class" cannot be directly defined by age. However, those nearing retirement would probably want to (and certainly should) put in more than younger faculty as they have fewer years to put in funds or have the earnings accrue.

Recommendations:

1) For Faculty Members* the "class" is defined as the number of years employed at the University.

2) Plan contributions will be collected and invested by Minnesota Life Insurance Company.

3) Claim payouts will be managed by the University’s Employee Benefits Department.

4) Plan implementation will ideally be by July 1, 2003 but no later than January 1, 2004.

5) All Faculty Members would have a basic contribution each year to the PRHCSP of one and a half percent (1 1/2%) of salary. This would, for now, come from the 13% contribution of the University to each individual’s Faculty Retirement Plan (FRP).

6) All Faculty Members who in fall 2003 have served seven years or more would contribute an additional amount as a catch-up provision. Additional contributions from those starting their eighth (8th) or later year in fall 2003 should be in steps of 0.2% per service year up to those in their 25th year of employment at the University when it would reach 3.6%. This additional 3.6% contribution, over and above the one and a half percent new contribution from the University, would be the same for all eligible employees with 24 or more years of service in Fall 2003. For a given individual these contributions would be frozen at the percentage dependent on their service at the U up to fall 2003. It should be clear that the contributions to the new fund would be mandatory; each member of each specific class (years of service with our definition) must contribute in the same manner. The recommended input by faculty members with different degrees of service should be reexamined at least once every three years.

7) The additional money, 0.2% to 3.6% of salary, would also come from the university’s present 13% contribution to the basic (401a) plan, reducing the input to that plan by the amount going into the PRHCSP. This is not a reduction to the individual’s total retirement funds; rather a transfer to a more tax advantaged plan (PRHCSP). If the individual wishes to make up for the smaller amount going to the 401a plan, additional funds could be contributed to either of the Optional Retirement plans (403b or 457) up to the maximum permitted.

The rationale for these contributions is to provide a reasonable sum of money at the time of an individual's retirement. Though people now very close to retirement can never completely catch up to accumulate enough money to pay for a significant fraction of their health care premiums, these additional steps will help and would perhaps be sufficient for those who still have a fair amount of time left before retirement. The goal is to have the accumulated savings in this plan reach something in the order of magnitude of an individual's last year's salary within +/-25%, though this is unrealistic for those with less than 10 to 15 years to retirement. Even one year's salary would probably not provide (based on an annuity analysis) all of the funds for health care insurance, but could provide a significant fraction.

8) We also believe that those in Phased Retirement should be in a separate faculty class. For this class we propose a significant increase in the individual's input (essentially taken from the University's contribution to the basic Faculty Retirement Plan) to the PRHCSP, tentatively 10% of salary. This would greatly help those now approaching retirement through the Phased Retirement Plan. This contribution would be reviewed periodically when the entire plan is reviewed and may eventually be phased out.

9) For faculty in either a Phased Retirement or a Terminal Leave program, there should be a change in how the University pays the additional health care coverage after leaving the University (two or more years depending on eligibility for Medicare benefits). At the time a faculty member ends regular employment at the University, a sum equal to the University cost of faculty health care (either single or family coverage) for the total time involved should be placed in the individual's PRHCSP fund. This would not represent a change in the present University rule, which provides health care benefits for retirees during the phased retirement period.

Summary:

A recurring annual contribution of one and a half percent (1 1/2%) of salary would be made by all participants in the FRP. For the present that would come from the 13% University contribution to each individual's FRP. An additional contribution by each individual who has been here for seven years (i.e. in the eighth year of service) would be 0.2% of salary. For those who have been here longer this would rise by 0.2% for every year of service until the 25th year of service (after 24 years) when the individual's contribution would be 3.6%. This (3.6%) would be the same for those with still longer service. Thus the maximum input to an individual's PRHCSP would be 5.1% of salary. The additional money, 0.2% to 3.6% of salary would also come from the university's present 13% contribution to the basic (401a) plan. Those in phased retirement would make still larger contributions. Those leaving the University through Phased Retirement or Terminal Leave would receive whatever funds due for future health care as a lump sum into their PRHCSP account.

* The actual definition of a "Faculty Member" in the Faculty Retirement Plan is rather lengthy, but is essentially: "any employee of the University who holds an appointment of atleast67% time for a duration of at least nine months and holds one of the following titles (if an employee holds more than one appointment, the first title of appointment will govern): a) Faculty (94xx classes); b) Administrative staff members with personnel classifications 9301-9399; c) Professional staff members with personnel classifications 9701 through 9799; and d) University of Minnesota Extension Service (MES) academic staff with personnel classifications 9621 through 9640who are not eligible for a federal appointment. A "T" temporary appointment does not affect an employee's status in one of the above-described categories. "Faculty Member," however, shall not include the following: 1) Faculty members with Visiting, Adjunct, or Clinical prefixes; 2) Staff members filling administrative or professional positions on an acting basis; 3) Research Specialists (9755); 4) Clinical Preceptors (9756); and 5) Industrial Fellows(9757)."

There are exclusions from the PRHCSP: "An employee shall be ineligible for future contributions to the PRHCSP if the MSRS determines that the employee falls within any one of the following categories: a) The employee is a foreign national and plans to return to the country in which he or she is a citizen upon termination of public employment. b) The employee will receive employer-paid post retirement health care coverage through his/her public employer, or through a spouse's employer. The insurance must provide full-coverage for the employee's lifetime. c) The employee will receive post retirement health care coverage from the military."

COMMENT:

Note, because of the difficult financial circumstances for the University this year, we have modified our previous plan which was submitted 13 December 2002. In that plan, we had proposed one-and-a-half percent of salary would be contributed by the University to the Post-Retirement Health Care Saving Plan (PRHCSP). Now the expectation is a zero salary increase, and yet we believe that this program should be initiated now. Thus, we propose that for the present, the base one-and-a-half percent of the salary going into PRHCSP for all faculty would come out of the University's present contribution to the retirement plan (13% of salary). Aside from this, the plan would be the same as recommended previously, including the increased contributions for those who had been at the University seven years or more and the increased contribution for those in phase-retirement.

There are two very strong caveats that we would like to add. First, we are going under the assumption that there will be no additional funds for any University group this year for PRHCSP. If this is not the case, then we would expect that similar funds would go into PRHCSP for faculty, rather than having all of the money coming out of the faculty members' present retirement plan contributions.

Second, we ask that in the future, when the University again reaches a point that there are reasonable new funds, that the one-and-a-half percent taken out of the basic faculty retirement plan would be put back in, returning the University's FRP contribution to 13% of salary. The University FRP has been an excellent one. We greatly regret the need to reduce the basic plan by this change yet we think overall it is a good idea. However in the future, we are very desirous of seeing the plan return to its present level of contributions.

This plan was approved by the :
- Retirement Subcommittee on Monday, March 10, 2003,
- Faculty Affairs Committee on Tuesday, March 11, 2003,
- Faculty Consultative Committee on Thursday, March 14, 2003.

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