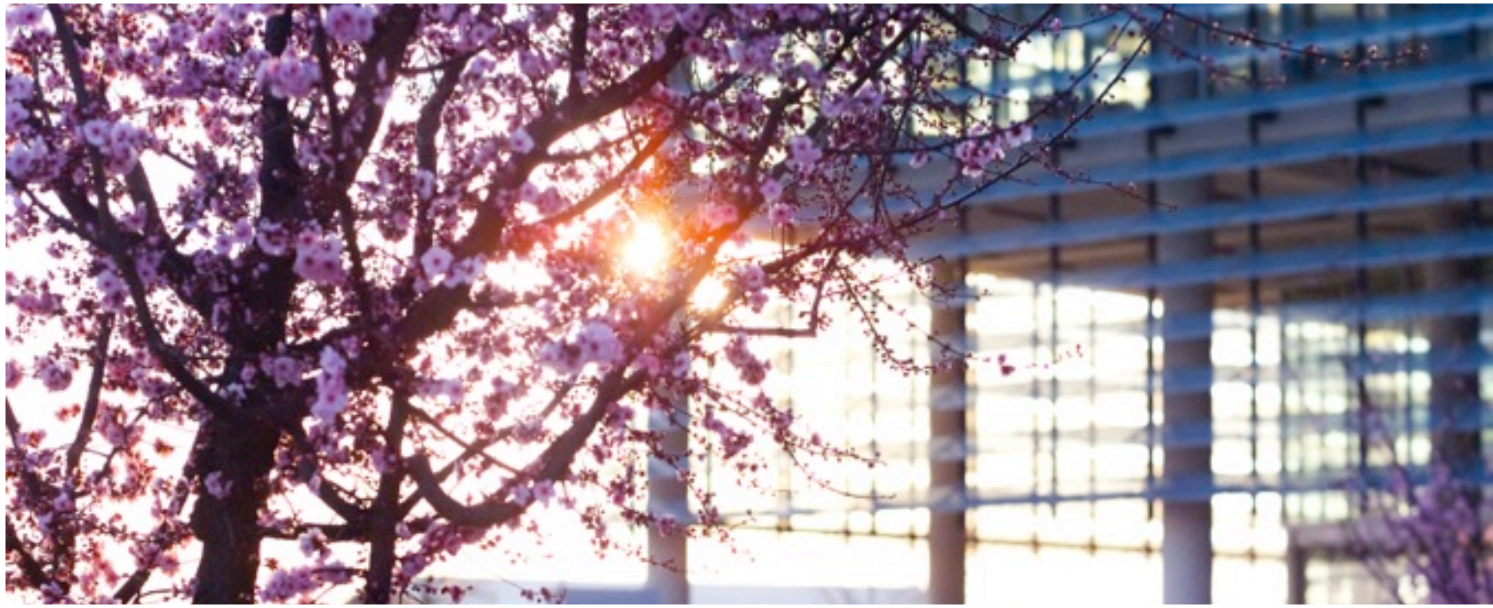


Retiree Health Benefit Program Consultation

Retiree Associations

September 8, 2017

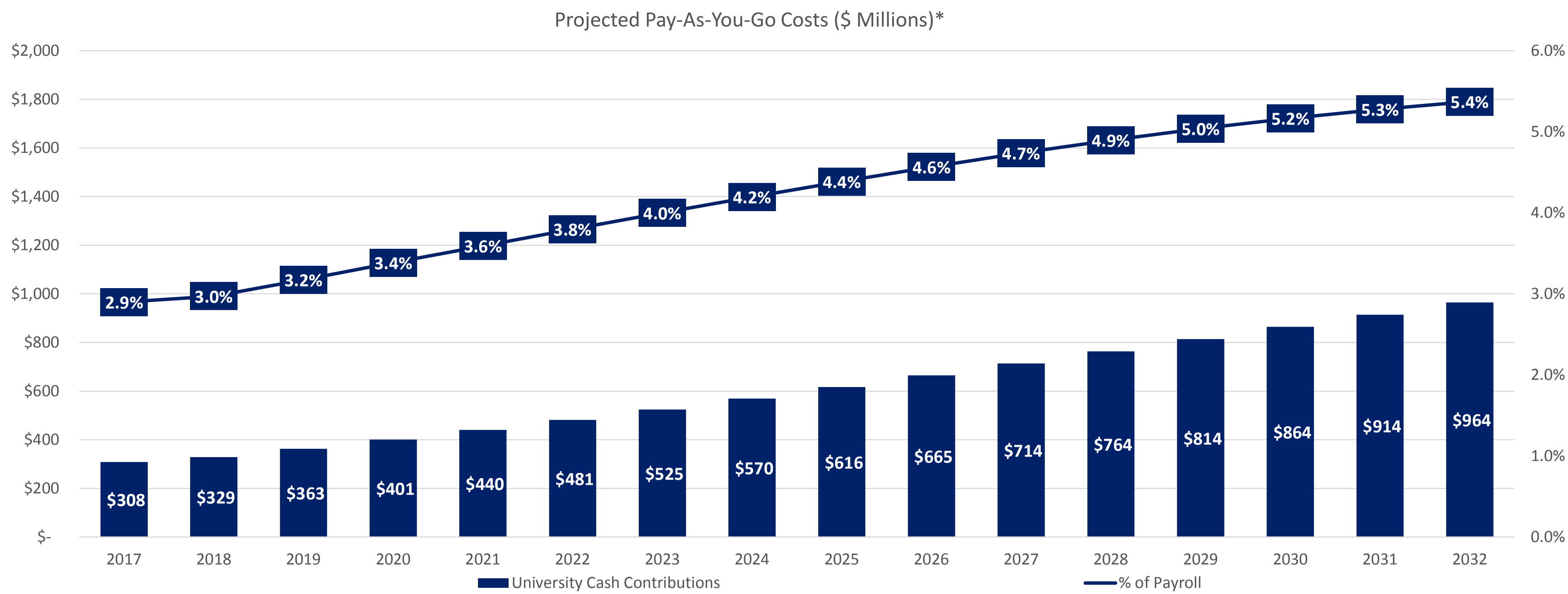
UNIVERSITY
OF
CALIFORNIA

Executive Summary

- The University currently spends approximately $300 million per year on retiree health benefits for 43,000 UC retirees and survivors. The Retiree Health Benefit Program has a $21.2 billion unfunded liability as of July 1, 2016.
- For 2018, the UC contribution will increase by 7.2%, or $19.6 million dollars
- The current and projected cost increases are greater than inflation and are growing faster than the University's budget
- The Regents policy implemented in 2010 helped slow anticipated growth of University pay-as-you-go costs, which have been held nearly flat for the past five years; however, a new policy is needed to address future UC cost growth
- The current policy steadily reduced the University's contribution to 70% of aggregate premiums. The 70% level for the University's share was reached for pre-Medicare in 2015 and will be reached for Medicare retirees in 2018.
- A budget target for University contributions to the Retiree Health Benefit Program will provide cost predictability for the University's operating budget. There is currently a budget target for the University contributions for the active health and welfare program.
- A budget target, combined with programmatic changes, could slow the growth in operating costs and would significantly reduce the unfunded liability, thus helping sustain the program well into the future
- While a budget target and adjustment to the floor will provide cost certainty to the University, we realize that this will result in greater cost uncertainty for our retirees, with greater year to year fluctuations.
- We know how important health benefits are to our retirees, and although UC retiree health benefits are not a vested or guaranteed benefit, we are sensitive to the potential impacts on retirees as a result of cost and plan changes. UC Human Resources, in partnership with UC Health, will continue to manage the program and plan design to keep costs down and to deliver a choice of quality benefits that are also affordable.

The University "Pay-As-You-Go" cash contributions are expected to increase as a percent of payroll

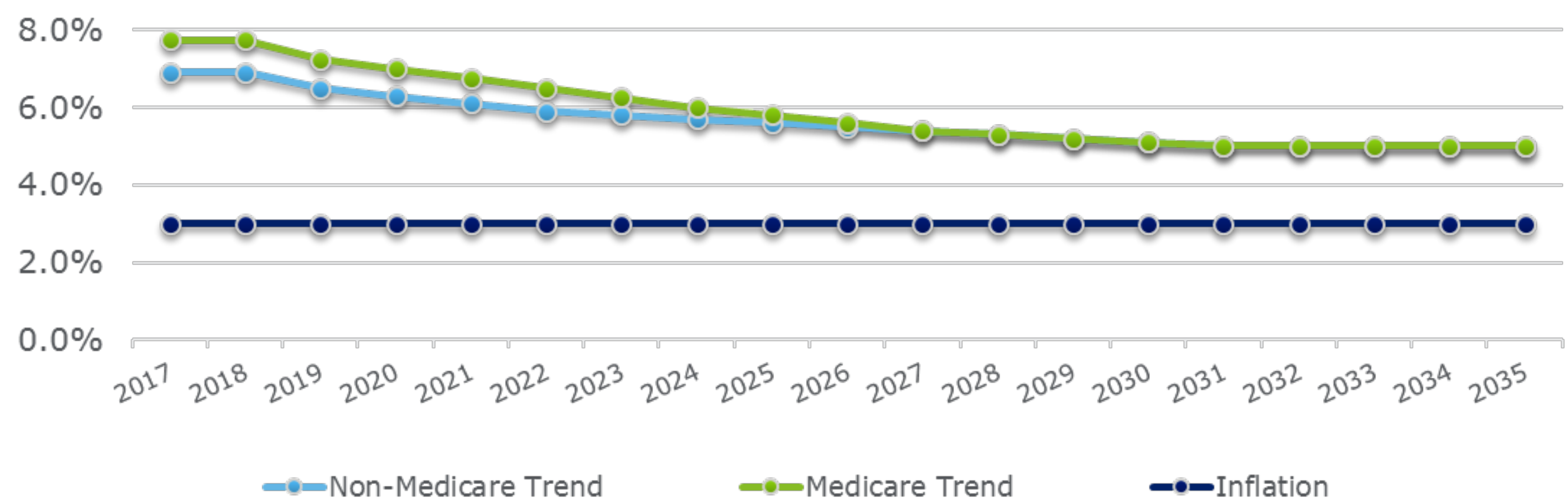
- The University **"Pay-As-You-Go" cash contribution** requirements are expected to escalate more quickly than price inflation
  - Increase is driven by UC's retiree health costs, which are projected to grow at the **medical trend rate (currently at ~7%)**
  - Increase is also driven by our **growing retiree population**
  - Combined impact of these two drivers could cause a greater portion of annual budget growth to be **diverted to fund retiree health costs rather** than to fulfill the mission of the University



**Based on total payroll projections provided by Segal (includes 0.7% employee headcount growth)*

Medical trend is expected to be notably higher than price inflation

- Plan costs are expected to increase over time due to **growing retiree health population** and **expected future medical inflation (trend)**
  - Medical trend is a significant driver of future pay-as-you-go costs
  - Medical trend is expected to be notably higher than price inflation
- The chart below illustrates the current assumption for medical trend compared to price inflation



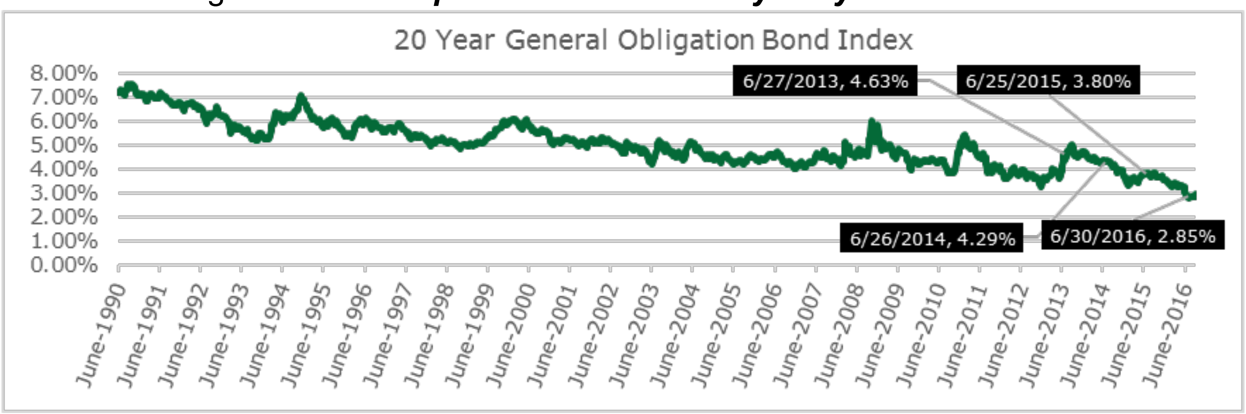
- Since medical trend is higher than the anticipated growth of revenue, the retiree health program could divert monies from other operational needs if additional efforts are not made to manage costs

New accounting standards have highlighted the long-term costs of retiree health benefits

Changes in how Retiree Healthcare (OPEB) liabilities need to be reported on financial statements has highlighted the size of the unfunded obligation.

GASB Changes – Reporting Benefit Liabilities

- Effective FYE June 30, 2017, the University will report retiree health liability under GASB 75
- Similar to recent accounting changes for pensions, under GASB 75 the entire net OPEB liability must be reported on the face of the financial statements rather than in the footnotes
- The new GASB 75 standard requires the discount rate for pay-as-you-go plans to be determined based on the index rates for a 20-year General Obligation Bond, which were at historically low levels at 6/30/2016
- The index rate at 6/30/2016 was 165 basis points lower than the assumed return on the University's assets, which was the basis for discounting liabilities under the prior accounting standard
- The decrease in discount rate increased the GASB liability by $5.0B*
- The liability is highly sensitive to the index rate; as noted in the table below, the index has increased 73 basis points as of 6/30/2017, which would have reduced the 6/30/2016 GASB 75 liability by $2.4B
- GASB changes have ***no impact on the University "Pay-As-You-Go" cash contribution requirements***



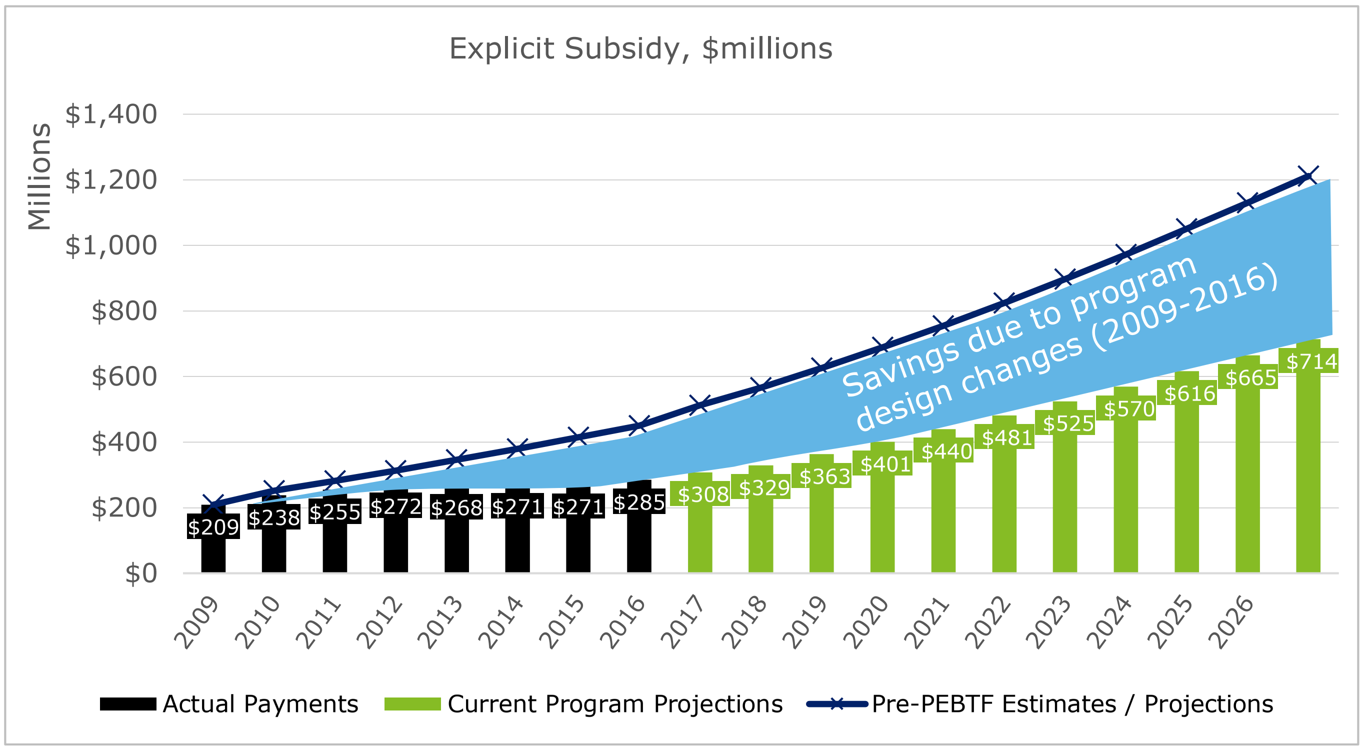
Discount Rate	*2.85%*	*3.58%*	*4.50%*
Basis	Index Rate – 6/30/16	Index Rate – 6/30/17	STIP/TRIP return
6/30/16 Liability	***$21.2B***	***$18.8B***	***$16.0B***

1% increase in discount rate decreases liability ***$3.3B***

Liability reflects Campus, Medical Centers, Hastings and Other (CMCHO)

Regents policy implemented in 2010 and recent program changes have slowed growth in costs

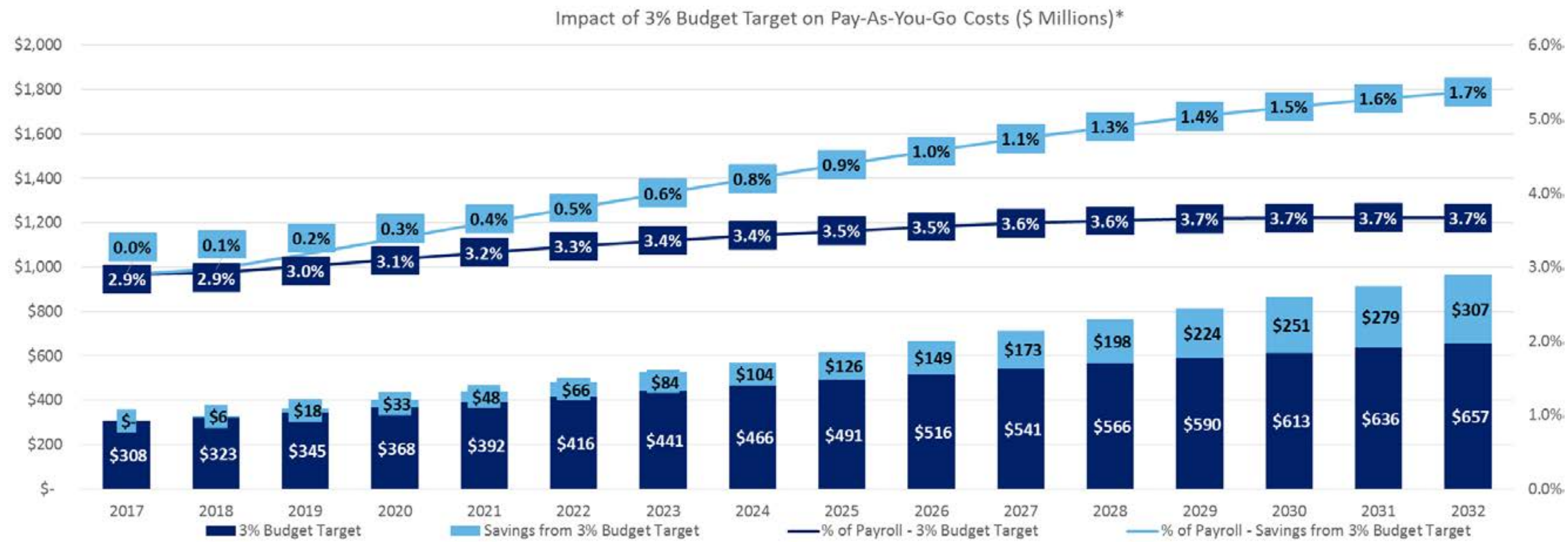
- Recent program changes have helped slow anticipated growth of pay-as-you-go costs which have been held nearly flat for the past five years
- Below is a graph comparing ongoing University “pay-as-you-go” cash costs to the projected costs of the program as it existed before the 2010 PEB Task Force Recommendations

Key Changes	***Impact on University “Pay-As-You-Go” Cash Costs***
• Per Regents policy, beginning in 2010 maximum University contributions decreased 3 percentage points per year to a floor of 70% of total premiums (pre-Medicare floor reached in 2015; Medicare floor reached in 2018); changes to graduated eligibility for retirees who leave prior to age 65 for the 2013 tier of University hires • Beginning in 2014, Medicare retirees outside of California enrolled in Medicare Exchange/Coordinator with a $250 per month HRA subsidy • Implemented Employer Group Waiver Plans for Medicare retirees • Implemented custom network HMO (Blue & Gold) and removed certain high cost plan options for pre-Medicare retirees	

Despite recent changes, there is still a long tail for the future cash requirements of the program driven primarily by the Medicare eligible population.

Implementing a 3% budget target is consistent with the University’s long-term price inflation assumption

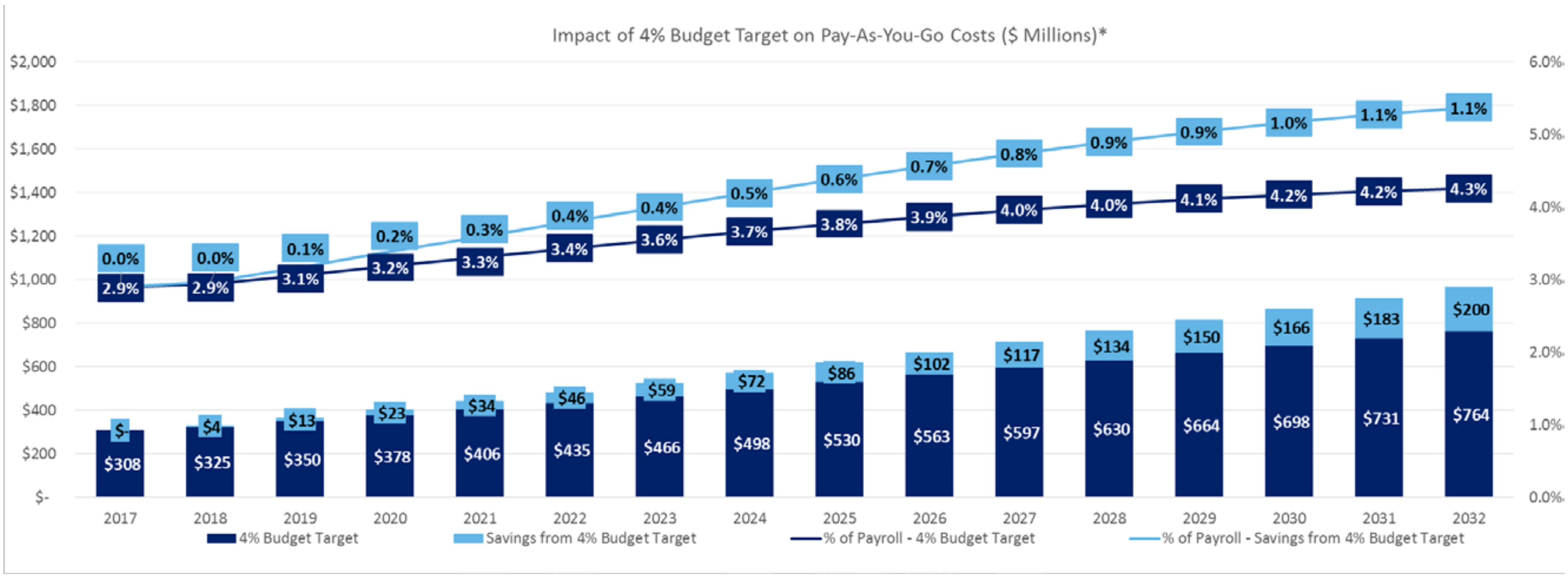
- Baseline University “Pay-As-You-Go” cash contribution is expected to grow more quickly than payroll
  - Medical trend and retiree headcount growth is expected to outpace wage and employee headcount growth
  - In 2032, cash contributions are projected to be 5.4% of projected payroll (~85% higher than current % of payroll)
- Implementing a 3% budget target is projected to keep University cash contributions closer to current levels as a percent of payroll
  - In 2032, cash contributions are projected to be 3.7% of projected payroll (~30% higher than current % of payroll)



*Based on total payroll projections provided by Segal (includes 0.7% employee headcount growth)

Projected University "Pay-As-You-Go" Cash Contributions – Impact of 4% Budget Target

- Baseline University "Pay-As-You-Go" cash contributions are expected to grow more quickly than payroll
  - Medical trend and retiree headcount growth is expected to outpace wage and employee headcount growth
  - In 2032, cash contributions are projected to be 5.4% of projected payroll (~85% higher than current % of payroll)
- Implementing a 4% budget target is projected to steadily increase University cash contributions as a percent of payroll
  - In 2032, cash contributions are projected to be 4.3% of projected payroll (~50% higher than current % of payroll)



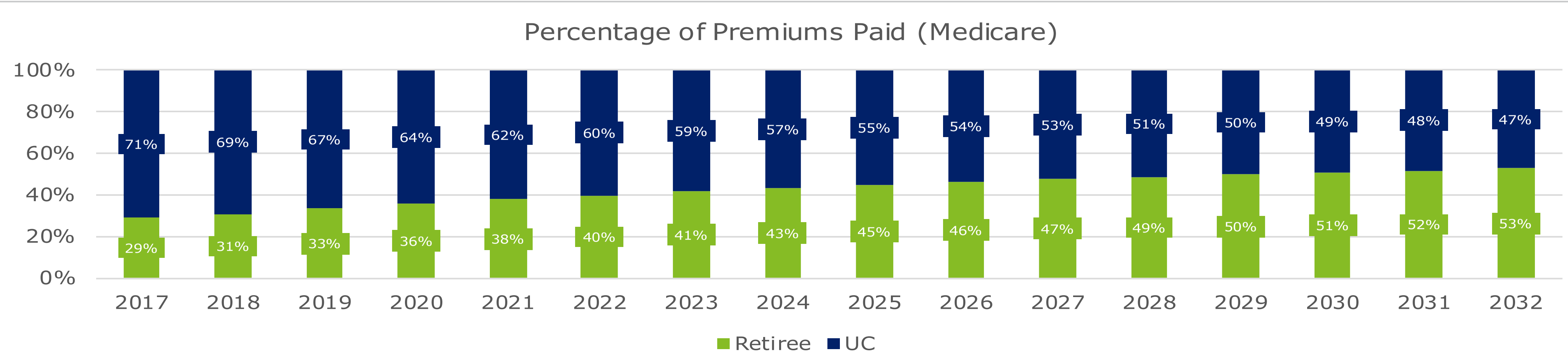
*Based on total payroll projections provided by Segal (includes 0.7% employee headcount growth)

A budget target will provide cost predictability for UC and shift costs above the target to retirees

- A 3% or 4% annual budget target of per capita University contributions is a means of controlling cash contribution requirements and obligations by directly addressing the rising costs associated with medical trend.

How a 3% or 4% Budget Target Would Work

- The University will share in the payment of rate increases up to the 3%/4% budget target. Rate increases above the budget target will be borne by the retirees.
- In years where medical trend is greater than the budget target, and barring other plan changes, retirees would pay an increasing portion of plan costs.
- HR would be responsible for implementing plan changes designed to achieve the budget target while mitigating the adverse impact on retirees.
- The University would need to determine if there would be any exceptions to those impacted by the budget target (e.g., retirees over 65 not eligible for Medicare)
- The graph below provides an illustrative projection of the share of Medicare premiums paid by UC and retirees assuming a 3% budget target is implemented in 2018 without any plan changes and medical trend grows at the rates previously noted.



This chart projects the aggregate portion of premiums paid by Medicare retirees receiving the full University contribution (i.e. 100% graduated eligibility).

Pre-Medicare Retiree Contributions with 3% or 4% Budget Target

Pre-Medicare Retiree Impact

The table illustrates how a 3% or 4% budget target could impact pre-Medicare retirees five years after implementation (2022) under a range of rate increase environments. This example compares monthly rates for pre-Medicare retirees with and without a budget target for the most affordable (Kaiser) and most expensive (UC Care) plans.

Key Assumptions

The following assumptions were made in projecting costs for this illustration:

- Premiums applicable for Calendar Year 2017
- Participant has single coverage
- Eligible for 100% of the maximum University contribution
- Medical trend is projected at a low (3.5%), medium (6.0%) and high (8.5%) annual increase levels

Active vs. Pre-Medicare Retiree (Monthly Rates - Single Coverage)		**2017**			**2022 Low - 3.5%**			**2022 Medium – 6.0%**			**2022 High – 8.5%**		
		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions	
Medical Plan	Budget Target		University	Member		University	Member		University	Member		University	Member
UCCare	No Budget Target	$ 754	$ 476	$ 278	$ 895	$ 566	$ 329	$ 1,009	$ 638	$ 371	$ 1,134	$ 715	$ 419
	4% Budget Target					$ 566	$ 329		$ 579	$ 430		$ 579	$ 555
	3% Budget Target					$ 551	$ 344		$ 551	$ 458		$ 551	$ 583
Kaiser	No Budget Target	$ 604	$ 476	$ 128	$ 717	$ 566	$ 151	$ 808	$ 638	$ 170	$ 908	$ 715	$ 193
	4% Budget Target					$ 566	$ 151		$ 579	$ 229		$ 579	$ 329
	3% Budget Target					$ 551	$ 166		$ 551	$ 257		$ 551	$ 357

Medicare Retiree Contributions with 3% or 4% Budget Target

Medicare Retiree Impact

The table illustrates how a 3% or 4% budget target could impact Medicare retirees five years after implementation (2022) under a range of rate increase environments. This example compares monthly rates for Medicare retirees with and without a budget target for the most affordable (Kaiser) and most expensive (High Option) plans.

Key Assumptions

The following assumptions were made in projecting costs for this illustration:

- Premiums applicable for Calendar Year 2017 with standard Part B premium ($121.80)
- Participant has single coverage
- Eligible for 100% of the maximum University contribution
- Medical trend is projected at ~~a~~ low (3.5%), medium (6.0%) and high (8.5%) annual increase levels

Active vs. Medicare Retiree (Monthly Rates - Single Coverage)		2017			2022 Low - 3.5%			2022 Medium – 6.0%			2022 High – 8.5%		
		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions		Premiums	Contributions	
Medical Plan	Budget Target		University	Member		University	Member		University	Member		University	Member
High Option	No Budget Target	$ 539	$ 328	$ 211	$ 640	$ 389	$ 251	$ 721	$ 439	$ 282	$ 811	$ 493	$ 318
	4% Budget Target					$ 389	$ 251		$ 399	$ 322		$ 399	$ 412
	3% Budget Target					$ 380	$ 260		$ 380	$ 341		$ 380	$ 431
Kaiser	No Budget Target	$ 374	$ 328	$ 46	$ 444	$ 389	$ 55	$ 500	$ 439	$ 61	$ 563	$ 493	$ 70
	4% Budget Target					$ 389	$ 55		$ 399	$ 101		$ 399	$ 164
	3% Budget Target					$ 380	$ 64		$ 380	$ 120		$ 380	$ 183

Program Design Options

Potential Design Change Options

Description	Potential University Impact[1]	
Potential changes to Program Design		
Increase contributions for non-Medicare, over 65 retirees[2]	<2%	$200-$400M
Implement 70% cost sharing for retiree dental benefits	2%	$500M
Group Medicare Advantage PPO replacement for Medicare PPO and High Option retirees	2%	$500M
Include Health Net Medicare retirees in Group Medicare Advantage PPO plan	2-5%	$500M-$1.0B
Eliminate 50% of benefits for spouses and dependents	9%-14%	$2-$3B

1. These figures are rough estimates; actual savings will require additional actuarial analysis and will depend on final plan design. Unless otherwise noted, all information presented in this document are based on the census, assumptions, methods and plan provisions used in the 6/30/2016 GASB 75 actuarial valuation.

2. Increased contributions for non-Medicare retirees over 65 to the same level of average Medicare eligible retiree.

Cost Sharing

Increase Contributions for Non-Medicare Retirees over 65

Overview

- Non-Medicare retirees over age 65 represent $3.1B of liability ($2.7B attributed to current retirees)
- Non-Medicare retirees pay less for coverage than Medicare retirees
- Non-Medicare retirees have not contributed towards Medicare in the past and they also saved UC from having to contribute to Medicare during their careers

	Non-Medicare over 65	Medicare (California)
Retiree Contribution (Including Part B)	$1,108	$1,786
Implicit Subsidy	$12,380	N/A
Explicit Subsidy	$7,104	$3,687
Average Plan Costs	**$20,592**	**$5,473**
Average Age	73	75

Potential University Impact	***Retiree Considerations***
• Each $1,000 increase in retiree contributions for non-Medicare retirees will reduce the liability by ***$0.2B*** *(less than 1%)*	• Availability of coverage outside of group plan for those who choose coverage on a public exchange versus paying a higher contribution

Cost Sharing

Implement 70% Cost Sharing for Dental Benefits

Overview

- The University currently contributes 100% towards dental, subject to graduated eligibility
- The table below illustrates retiree contributions assuming UC contributes 70% towards dental in 2017, assuming 100% graduated eligibility:

	Monthly Single Rates	DPPO	DHMO
a)	2017 Premium	$42.75	$20.03
b)	UC Share	70%	70%
c)	Maximum University Contribution (a) * (b)	$29.93	$14.02
d)	Retiree Contribution (a) – (c)	$12.82	$6.01

Potential University Impact

- Dental accounts for $1.8B in liability, having retirees pay for 30% of dental costs would reduce liability by ***$0.5B*** (2%)

Retiree Considerations

- The majority of retirees are enrolled in Dental PPO and would have had to contribute $12.82 per month in 2017 towards dental costs.

Plan Structure and Delivery

Replace Medicare PPO and High Option Plans with Group Medicare Advantage (MA) PPO

Overview

- Transition retirees from the Medicare PPO and High Option plans to a fully insured group Medicare Advantage plan structure; actions for the network Medicare Advantage HMO plan (currently Health Net) – may depend on the outcome of the current HMO bid process
- Plan sponsors may replicate the current plan design
- Medicare Advantage PPO plans typically reduce costs through two principal mechanisms:
  - Capture of incremental CMS revenues
  - Introduction of medical management

Potential University Impact	***Retiree Considerations***
• Could deliver meaningful reduction to "pay as you go" cost and reduce liability by ***$0.5B*** (2%) ▪ No change to administrative process ▪ Products fully insured ▪ Current retirees can default into coverage	• With current contribution approach, lowering plan cost in one plan impacts what retirees pay in all plans • Plan designs may not be exact match • Medical management may be viewed as disruptive, particularly by older members • Limited potential for disruption as a few providers (<5%) may not accept Medicare

Plan Structure and Delivery

Re-bid / Re-design Health Net Seniority Plus Plan

Overview

- Health Net Plan is a Group Medicare Advantage product, but has relatively high costs (higher than Medicare PPO)
- Health Net plan represents the highest liability and cash expense of all Medicare plans due to high enrollment and cost
- Multiple carriers in California offer similar products, current competitive bid process could lower rates
- Although it may not align with the active Health Net plan, it may be preferable to transition Seniority Plus members to Group Medicare Advantage PPO solution along with Medicare PPO and High Option members

Potential University Impact	***Retiree Considerations***
• 15 percent reduction in costs of Health Net alone would reduce liability by ***$0.5B (2%)*** • Presumably this would not be done alone, and would be combined with the transition of the Medicare PPO and High Option plans to Group Medicare Advantage ***$1.0B (5%)***	• Savings would be shared with Health Net retirees, while retirees in other plans would pay more • Retirees may be subject to plan designs changes