

The University of Oklahoma



Contribution Strategy and Health Insurance Options
Committee

Review of Retiree Medical Plans
Preliminary Findings

October 2008

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Executive Summary

In response to significant increases in healthcare costs experienced by the University and plan participants, President David Boren appointed the Contributions Strategy and Health Insurance Options Committee (the Committee) in April 2007. The Committee was charged with conducting a thorough review of OU and competitive healthcare plans and strategies, and recommending changes that best meet the needs of active employees, retirees and the University.

The Committee submitted several recommendations to President Boren in September 2007, for changes to the contribution strategy and healthcare plans for active employees. Many of the Committee's recommendations for active employee healthcare benefits were adopted, with some modification by the President in response to significant campus discussion and employee input.

The Committee also submitted two recommendations below that impact retiree medical benefits and participants. From the *Final Report of the Contribution Strategy and Health Insurance Options Committee* submitted September 6, 2007:

6. The Committee recommends employees hired on or after January 1, 2008, have a reduced or unsubsidized retiree medical benefit and not be eligible for the current retiree medical benefit program subsidy. The retiree medical benefit and contribution structure for current retirees should remain unchanged at this time. Active employees currently eligible to retire should also be eligible to participate in the same retiree medical benefit and contribution structure as current retirees upon their retirement from the University. For other employees, the Committee recommends service-based employer contributions toward the cost of future retiree medical coverage be investigated.
7. Because of the significant and growing costs associated with the University's post-retirement benefit obligation and the complexity of the analysis of funding requirements and options, the Committee further recommends it continue its work to conduct a further study of these issues.

The separate recommendations regarding retiree medical benefits reflect the Committee's determination that a separate and focused review was required to address retiree medical plan issues. A detailed review of retiree medical benefits also was required as the University is now subject to new financial accounting rules that require the measurement and reporting of the liability associated with post-retirement benefit obligations.

As the Committee engaged in this review, significant analysis, discussion and debate were required. A common point of view grounded the discussion: the Committee's strong commitment to limiting the impact on current retirees, those approaching retirement, and lower paid employees for whom the cost of healthcare can take a disproportionate share of their retirement income, and at the same time, offering a program that would be sustainable for the foreseeable future.

Reaching consensus was difficult. However, the Committee recognized that failure to take action to address the significant cost increases in retiree health insurance now may result in more drastic actions being required in the future. Indeed, the Committee's primary objective was to consider plan alternatives that allow OU to offer a program that preserves meaningful benefits for faculty and staff and is sustainable.

After careful consideration of a range of options, the Committee has established a set of preliminary recommendations that are summarized below. The financial impact of the recommendations will reduce the University's projected post retirement benefit obligation by nearly 35% from \$589 million to \$386 million. The recommended program changes will impact employees that retire more than five years after adoption of the changes. Current retirees will not be affected. Thus, the University's annual cash outlay is not expected to change materially before 2020.

After a period for employee and retiree review and comment, the Committee will establish a final set of recommendations to be submitted to President Boren.

Summary of Preliminary Recommendations

1. The Committee recommends that employees be grouped based on when they will meet age and service requirements for retirement. This will help to insure that changes are introduced gradually, and recognizes that employees further from retirement eligibility have more time to plan and prepare for the financial impact of program changes. The following employee groupings are proposed:
 - **Group 1:** Current retirees
 - **Group 2:** Employees currently eligible to retire and those who will become eligible before 1/1/2014 (or 5 years after adoption whichever is later)
 - **Group 3:** Employees hired before 1/1/2008 who will meet eligibility requirements for retirement between 1/1/2014 (or 5 years after adoption whichever is later) and 12/31/2018 (or 10 years from adoption whichever is later)
 - **Group 4:** Employees hired before 1/1/2008 who will meet retirement eligibility requirements on or after 1/1/2019 (or 10 years from adoption whichever is later)
 - **Group 5:** Employees hired after 1/1/2008

It is important to note that your retiree health benefits will be determined based on your grouping above—reflecting your hire date and the date you become eligible for retirement—which does not require you to retire by the cutoff dates. This means there is no reason to retire in order to preserve your level of benefits.

2. The Committee recommends no changes to the retiree medical insurance benefit program or contribution strategy for:
 - Current retirees (Group 1)
 - Employees currently eligible to retire (Group 2)
 - Employees that become retirement eligible before 1/1/2014 or within 5 years of adoption of retiree medical benefit changes, whichever occurs last (Group 2)
3. For all other active employees (Groups 3, 4 and 5), the Committee reviewed three main areas for change: **eligibility, plan design features** (e.g., deductible, annual out-of-pocket maximum, co-insurance, etc.), and **cost-sharing arrangements**. After considering many alternatives, the Committee decided on the following proposed changes.

Eligibility: The current eligibility rules will continue unchanged. To be eligible for retiree medical coverage an employee must first satisfy one of the following rules:

- Attain age plus years of service greater than or equal to 80, or
- Attain service of 25 years or greater, or
- Attain age 62 with at least 10 years of service.

Plan Design Features: The Committee recommends the following plan design changes in the post-65 OU plan for those retirees eligible for Medicare:

- Introduce an annual \$300 deductible
- Change the benefits coordination method with Medicare to “carve-out and reduce the annual out-of-pocket maximum to \$2,000 (see page 18 for a detailed explanation of this change)

Cost Sharing Arrangements: The Committee recommends that a new arrangement be established for sharing the cost of retiree medical coverage as follows:

- Provide a University subsidy of between 55-85% of pre-Medicare retiree medical premiums, which varies based on the employee’s age at commencement of retiree medical benefits in the OU plan and their years of service at separation
- The percentage of the subsidy will be determined upon benefit commencement (or age 55 if later), and will not change until the retiree reaches Medicare age (65), at which time the OU subsidy will increase by an additional 10%
- Employees will continue to be eligible to retire with 25 years of service or more, but will not become eligible for the OU subsidy until reaching age 55. For example, if an employee retires at age 48 with 25 years of service, he or she could still begin coverage under the OU plan immediately, but would be required to pay the full retiree premium cost between ages 48-55. When the retiree reaches age 55, OU would begin to subsidize a portion of the coverage.
- Employees can defer participation in the OU plan at retirement, with a one-time opportunity to re-enter upon loss of other health coverage or at age 65, whichever is sooner
- Employees hired before 1/1/2008 who become eligible to retire on or after 1/1/2019 (Group 4) will be subject to a “cap” that limits the maximum University annual contribution toward their cost of retiree medical benefits to two times (2X) the premium subsidy provided in the year this provision is adopted
- Employees hired on or after 1/1/2008 (Group 5) will be required to pay 100% of the required retiree premium. The Committee recommends that a subsequent review be conducted to determine what type of University retiree medical insurance support should be provided for these employees.

- Any future required retiree medical contributions would be offset by any payments the University receives on their behalf from the Oklahoma Teachers Retirement System (OTRS)

The following tables summarizes the proposed changes and how they will apply for each group.

Group	Add a \$300 deductible to the Post-65 Program	Change the Medicare coordination method to "carve-out"	Add retiree contribution requirements based on a retiree's age at commencement of retiree medical benefits and years of service at separation	Limit OU's subsidy to 2X the subsidy amount provided in the year of adoption
Group 1: Current retirees	NA	NA	NA	NA
Group 2: Active employees currently eligible to retire and those who will become eligible by 1/1/2014 (or 5 years after adoption whichever is later)	NA	NA	NA	NA
Group 3: Employees hired before 1/1/2008 who meet eligibility requirements for retirement between 1/1/2014 and 12/31/2018 (or 10 years from adoption whichever is later)	Change applies	Change applies	Change applies	NA
Group 4: Employees hired before 1/1/2008 who meet retirement eligibility requirements after 1/1/2019 (or 10 years from adoption whichever is later)	Change applies	Change applies	Change applies	Change applies
Group 5: Employees hired after 1/1/2008	Change applies	Change applies	Required to pay 100% of the premium cost	NA

OU Contributions Strategy and Health Insurance Options Committee – Review of Retiree Medical Benefits

Background

Sharply rising costs for retiree medical benefits consume a growing percentage of the University's operating funds. Funds available to pay for salaries, benefits, and other university obligations continue to grow relatively slowly, especially when compared to the growth in retiree health care expenditures. Given today's national healthcare environment, practically all sponsors of healthcare plans – in the public and private sectors alike – face these escalating costs. Naturally, many institutions have begun taking steps to manage their spiraling retiree medical costs.

For 2008, the annual cost for insuring our retiree population is about \$6 million. Looking ahead ten years, we estimate that the annual cost will be \$26 million, based on the age and service levels of our current population, and our current retiree benefit plan features and contribution strategy. Fifteen years out, the projection is \$39 million. This dramatic increase is attributable in large part to the large number of employees who will meet age and service requirements to retire, but also because the University currently pays the entire cost of future premium increases for its retirees.

Recently, the Governmental Accounting Standards Board (GASB) began requiring the measurement and disclosure of **O**ther (than pension) **P**ost **E**mployment **B**enefits obligations, also referred to as OPEB. These new GASB standards require OU to project the total cost of providing post retirement benefits. Based on our current employees, plan provisions, and retirement patterns, our actuaries have estimated that OU's retiree health program has a projected liability of \$589 million as of 1/1/2008. This liability is the amount that would have to be invested today in an interest-earning account in order to provide enough money to pay all expected costs of post retirement benefits for current plan participants (retirees and active employees hired prior to 1/1/2008).

Since benefit costs are paid on an ongoing basis, the University does not have to use present funds to address the OPEB liability. Like many other OPEB organizations, OU can continue to fund retiree medical plans on a pay-as-you-go basis. But the new GASB reporting and disclosure requirements provide a measure of the massive financial resources that the current retiree health care benefits structure would require. Besides the implications for demand on future cash flows, the OPEB liability directly affects the University's ability to issue debt for present and future capital expenditures.

The OPEB liability indicates that we are on an unsustainable course, and is a call to action. A carefully thought-out plan adopted now will enable us to maintain a significant retiree health benefit for pre-2008 employees, in a way that recognizes years of service, protects employees in or near retirement, and provides younger employees time to prepare for meeting the costs of their healthcare needs in retirement. To postpone action would invite a future crisis at a time when options are much more limited, and even more unpleasant than those we must consider now. It is a risk that the OU community cannot afford to take.

Committee Deliberations and Process

The Committee met several times from December 2007 through August 2008 to evaluate current OU retiree medical plans and eligibility requirements, and to explore and discuss the competitive practices at other universities and private employers. The Committee was assisted by consultants from Segal/Sibson consulting and OU Human Resources staff in gathering and analyzing data and modeling aspects of a range of plan designs and policy changes.

Issues for Review

The Committee agreed to address the following questions within the scope of its current review:

1. How do OU's current retiree medical benefits compare with the programs of similar major universities?
2. How do we insure that any proposed changes avoid affecting employee retirement patterns?
3. Should there be differences in retiree medical benefits for current retirees and future retirees? And if so, how should the University group retirees and current employees hired prior to January 1, 2008 to recognize length of service and provide time to adapt to changes in future retiree medical benefit plan design or participant contributions?
4. What plan design and contribution strategy changes should be considered, and what are the potential human resources and financial impacts of these changes?
5. What University sponsored retiree medical program should be implemented for employees hired on or after 1/1/2008, to support organizational employee attraction and retention goals?

Guiding Principles

At the initial meeting for the review of retiree medical benefits, the Committee reaffirmed that the guiding principles (#1-6 below) adopted during the initial review of medical insurance options for active employees were still appropriate. After discussion the Committee felt that Guiding Principles #7 and #8 should be adopted for the review of retiree medical benefits.

University of Oklahoma Contribution Strategies

- **Guiding Principle #1:** OU wants to be socially responsible with its contribution strategy
- **Guiding Principle #2:** OU wants to address the root cause drivers of healthcare cost by providing appropriate support to facilitate healthier behaviors
- **Guiding Principle #3:** In OU's efforts to attract and retain its required talent and achieve appropriate employee diversity, its benefit programs need to be competitive to all segments of the University population
- **Guiding Principle #4:** The health plan should be affordable to all benefits eligible employees, without creating a hardship on the lower paid employees
- **Guiding Principle #5:** Benefits should provide reasonably comprehensive security for OU's faculty and staff
- **Guiding Principle #6:** Retiree health benefits need to be tied more closely to a total reward strategy, and be more reflective of the service contribution provided to OU
- **Guiding Principle #7:** OU wishes to offer a retiree health plan that is sustainable in the long-term
- **Guiding Principle #8:** OU should consider what effect any changes to the retiree health program will have on retirement patterns

Committee Analysis, Findings, and Recommendations

Question: How do OU's current retiree medical benefits compare with the programs of similar major universities?

The Committee engaged Segal/Sibson to conduct a comparison between OU's retiree medical benefits with plans offered by 14 peer higher education institutions. The peer institutions were the same organizations surveyed during the Committee's review of active employee medical benefits, and were initially selected because of their similarity to OU in either geography, mission, or breadth of academic and medical programs offered. The Committee felt the comparator group would provide a good reflection of our competitive position. Ten of the 14 organizations contacted responded to our request for information.

The Committee reviewed the responses to the peer group survey, and the broader 2006-2007 benefits survey of the College and University Professional Association (CUPA-HR) that included responses from 148 public and 275 private universities, and reached the following conclusions:

CUPA-HR survey results

- 58% of survey respondents provide pre-65 retiree medical coverage
 - Only 13% of this group paid 100% of an employee's premium
 - The majority contribute approximately 50% to retiree and their dependent premiums
 - All institutions allowed participation for retirees in a group plan, even if no institutional contribution was made toward the retiree premium
 - Plan designs are similar to those offered by OU
- 49% of survey respondents provide post-65 retiree medical coverage
 - OU plan has no deductible while the median annual deductible under the survey respondents' plans was \$250

OU Peer Group results

- Employer Contributions – Retirees
 - Six institutions pay a portion of the premium for retirees; four institutions offer access to coverage without any employer contribution toward premium
 - Two of the six institutions pay 100% of the retirees premium, while the other four pay a percentage that typically varies based on age and service
- Employer Contributions – Dependents
 - Two institutions pay a portion of the premium for dependents; eight offer access to coverage without any employer contribution toward premium
- Eligibility criteria
 - The most prevalent criteria was attained age plus a minimum length of service
 - The next most prevalent criteria was a rule of attained age plus service equaling a total, for example the "Rule of 80"
- Medicare Coordination Method
 - Half of the institutions that responded use a Medicare "carve-out" method.

Key findings from the comparison of OU's current retiree medical benefit programs and the surveys are outlined below:

- OU's retiree medical contribution strategy of paying 100% of the retiree's premium appears to be matched by only a small percentage of other universities
- While two universities contribute toward the premiums of dependents of retirees, the predominant approach is to offer dependents access to coverage without an employer contribution, which is consistent with the current OU approach
- OU eligibility requirements for retiree medical coverage are typical in considering some combination of age and service or attained age plus a minimum length of service

- OU Pre-65 retiree medical plan features appear to be consistent with those offered by other institutions
- OU Post-65 retiree medical plan features appear more generous than nearly all other plans
 - There is no plan deductible under the OU plan versus a median deductible of \$250 for other plans
 - OU's coordination of benefits method with Medicare provides higher benefit than other coordination methods

Additional findings from the Segal/Sibson review indicated that in response to rapidly increasing costs and concerns about post-retirement benefit obligations, several universities have begun to take actions to change their retiree medical benefit plans. Summarized below are changes that have been adopted or are being considered by the peer group or other institutions surveyed.

- Changes in eligibility
 - Elimination of coverage for new hires
 - Increases in the age requirement for retirement
 - Preserving some of the benefits features and varying the amount of change based on age and service at the time of the study for current employees
- Changes made for Medicare eligible retirees
 - Change the Medicare coordination of benefits method to “carve-out” or non-duplication of benefits
 - Changes to the pharmacy program, including dropping Rx coverage entirely
 - Addition of Medicare Advantage plan offerings
- Changes in cost sharing with retiree
 - Increase or introduction of retiree contribution requirement
 - Cap on institution subsidy at a multiple of current plan costs (e.g., 2X the 2008 levels)

Question: How do we insure that any proposed changes avoid affecting employee retirement patterns?

Retirement decisions are complex and involve many factors. The Committee recognized the potential for changes in the retiree medical benefit program to impact retirement patterns of faculty and staff. For example, if employees were required to retire by certain dates in order to preserve or earn a better retiree medical benefit, some active employees might choose to accelerate their retirement date. Committee members felt strongly that any changes to the retiree medical benefit program should be introduced in a way that would not motivate, reward, or penalize employees based on when they chose to retire.

The solution agreed to by Committee members is that the date an employee meets the age and service requirements to retire, rather than the date of actual retirement, should determine the retiree medical provisions that would apply upon subsequent retirement. This approach, while administratively more complex, helps insure that there is no benefit improvement received by choosing an earlier retirement date. The administrative complexity of this approach is that the University will have to start tracking retirement eligibility dates for employees to determine what level of retirement benefits they will receive when they actually retire.

Recommendation: *The Committee recommends that eligibility for future retiree medical benefits for current employees hired before 1/1/2008 should be based on when they first meet age and service requirements to retire, and not when they actually leave University employment. That is, all employees who are eligible to retire during the same timeframe would receive the same benefit offerings, whether they retire when first eligible or at a later date.*

Question: Should there be differences in retiree medical benefits for current retirees and future retirees? And if so, how should the University group retirees and current employees hired prior to January 1, 2008 to recognize length of service and provide time to adapt to changes in future retiree medical benefit plan design or participant contributions?

After a review of the significant projected increases in the University's cost of providing retiree medical benefits, the Committee determined that future changes in the program will be required. However, there was strong agreement that the impact of future changes should be limited for current retirees, current employees who have already satisfied eligibility requirements to retire, and other current employees who are "near" retirement eligibility. These groups of employees are less capable of responding to or preparing for the financial impact of changes that increase their costs. The Committee reached consensus that future changes should be identified and communicated to employees well in advance so that they may increase their savings or otherwise prepare for retiree medical costs.

A review of employee demographics in early 2008 indicated that 20% of current employees (2,047 people), will be eligible to retire by 1/1/2013, or in five years. Committee members debated the merits of shorter and longer periods where employees would continue on the same program as current retirees. The consensus reached was that employees more than five years away from meeting retirement eligibility would have time to prepare for the impact of program changes. While a longer period before an employee could be subject to different retiree medical benefits would cushion the potential impact of future changes for additional employees, it would also reduce the University's ability to achieve the desired reduction in future retiree medical benefit costs and post retirement benefit obligations.

The Committee did not consider changes to the eligibility criteria for retirement, as this analysis was considered beyond the scope of the review. Additionally, the competitive analysis conducted did not highlight any substantive differences between the OU criteria

and the peer group. Upon satisfying one of the following three rules, an individual is eligible for OU retiree medical coverage:

- Attained age plus service greater than or equal to 80 (Rule of 80),
- Attained age 62 with at least 10 years of service, or
- At least 25 years of service.

The Committee reviewed the age and service matrix of employees as of January 1, 2008 to determine if there were meaningful groupings of employees based on when they would first become eligible to retire. Too many groupings could be administratively cumbersome and difficult to communicate. Too few groups would likely yield wide differences in benefits, in some cases between employees with very little differences in the dates they became qualified for retiree medical benefits.

After significant discussion and modeling of various alternatives, the Committee reached consensus that five employee groupings should be established. The magnitude of the proposed changes in future retiree medical benefits is determined by the employee or retiree's group, which is based on the date they first meet the criteria to retire.

The groups and rationale are described below:

- Current retirees
 - Consistent with President Boren's direction, there should be no change to the retiree medical plan for those currently retired or near retirement
- Actives currently eligible to retire and those who will become eligible by 12/31/2013 (or 5 years after adoption if later)
 - The Committee decided those within 5 years of becoming eligible qualify as "near" retirement; this represents around 20% of current employees
- Active employees who become eligible to retire after 1/1/2014 (or 5 years from date of adoption if later) but before 12/31/2018 (or 10 years from date of adoption in later)
 - The Committee felt this group would have time to prepare for moderate changes before retirement
- Active employees hired before 1/1/2008, who will become eligible to retire after 12/31/2018 (or 10 years from date of adoption if later)
 - The Committee recognized that this group would not be eligible to retire for at least 10 years and would have time to plan for alternatives, thus allowing for material changes
- Employees hired after 1/1/2008
 - The Committee agreed this group would be eligible for access only to OU coverage and that OU should explore alternative approaches to help this group prepare for the cost of their retiree health insurance coverage

Recommendation: *The Committee recommends that employees be grouped based on when they will meet age and service requirements for retirement in order to insure that changes are introduced gradually and in recognition that employees further from retirement eligibility have more time to plan and prepare for the cost of healthcare during retirement. The following employee groupings are proposed:*

- a. **Group 1:** *Current retirees*
- b. **Group 2:** *Employees currently eligible to retire and those who will become eligible before 1/1/2014 (or 5 years from date of adoption if later)*
- c. **Group 3:** *Employees hired before 1/1/2008 who will meet eligibility requirements for retirement between 1/1/2014 (or 5 years from date of adoption if later) and 12/31/2018 (or 10 years from date of adoption if later)*
- d. **Group 4:** *Employees hired before 1/1/2008 who will meet retirement eligibility requirements on or after 1/1/2019*
- e. **Group 5:** *Employees hired on or after 1/1/2008*

Recommendation: *The Committee recommends no changes to the retiree medical insurance benefit program or contribution strategy for current retirees, employees eligible to retire, and Group 2 employees (those who become retirement eligible before 1/1/2014, or within 5 years of adoption, of these retiree medical benefit changes, whichever occurs later), at this time.*

Question: What plan design and contribution strategy changes should be considered?

Over five meetings, the Committee explored the cost and other impacts of introducing changes to the retiree medical benefit program, to determine whether a change should be recommended, and if so, to which group of employees the change should apply. The consultants from Segal/Sibson and the University's actuary from Fred Bass Associates created financial models to project the impact of potential changes on OU's annual cost of retiree medical benefits and on its post retirement benefit obligation.

The Committee considered current plan provisions, competitive practices from plans sponsored by other universities, and trends observed from other organizations to manage their future costs of providing retiree medical benefits. The benefit plan features listed below were identified as having potential to make a significant impact on the OU's future retiree medical costs, while still maintaining a competitive level of retiree medical benefits.

- Add a deductible to the OU retiree program for post-65 Medicare eligible retirees

- Change the current Medicare coordination of benefits method to “carve-out” (see page below for more details)
- Implement retiree contributions toward the cost of retiree medical coverage based on age at commencement of coverage and service at separation
- Establish a maximum OU contribution toward the cost of future retiree medical costs

A review of the competitive data indicates that OU’s retiree medical program provides a higher level of benefits because:

- OU has no deductible for the post-65 program, while most plans have a median deductible of \$250
- OU uses the most generous coordination method with Medicare, which usually does not require the retiree to pay a portion of the cost of services; however, most other plans use a “carve-out” method that require the retiree to pay a portion of the costs, resulting in lower costs for the plan sponsor
- OU pays 100% of the retiree’s premium, where most other plans pay a percentage of the premium, generally related to a combination of age and service

The Committee directed the consultants to prepare a significant number of iterations of their financial models to project the impact of these plan changes on the different employee groupings. The financial impact on both the retiree and the University were considered and vigorously discussed and debated. Summarized below are the areas where consensus was reached for preliminary recommendations for future changes.

NOTE: The retiree medical benefits for those under age 65 are the same as for active employees. Therefore, plan design changes that affect the benefits for this group, have traditionally mirrored changes for active employees. The Committee expects that this approach will continue in the future. However, the benefits for post-65 retirees, those eligible for Medicare, are currently considered separately and the competitive features of the OU program for post-65 retirees were thoroughly reviewed by the Committee

As indicated earlier, survey data shows a median and average deductible of \$250 for post-65 retirement benefit programs similar to OU’s. Currently OU retirees do not have any deductible, which means they do not incur out-of-pocket costs for Medicare allowable medical expenses. Adding a deductible to the program is a way of sharing the costs of the program with those retirees who access services, while retaining significant value for all participants.

Introducing a \$300 annual deductible is projected to reduce OU’s post retirement benefit obligation by around \$15 million.

OU’s current program provides a higher level of benefits in another key area: how our plan coordinates its benefits with Medicare. For OU’s Medicare eligible retirees, Medicare coverage is primary (meaning, it pays benefits first), and OU coverage is

secondary (meaning, it pays the balance of eligible expenses). The OU plan currently coordinates benefits with Medicare using a method frequently referred to as “Coordination of Benefits (COB).” The principle behind COB is for the plan to pay the full amount not paid by Medicare. This COB approach usually results in the retiree incurring no out-of-pocket costs for Medicare’s covered services. So, while OU’s current COB method provides a very generous benefit for the retiree, it is an expensive plan feature that many organizations have eliminated in recent years because of its cost.

The Committee reviewed the two other frequently used methods of coordinating benefits with Medicare: “carve-out” (also referred to as “Non-duplication of Benefits”) and “exclusion” (also referred to as “Maintenance of Benefit”) to determine how these methods might help to control the growth of future OU retiree medical costs.

“Carve-out” has become the most common form of coordination with Medicare over the last several years as plan sponsors have looked for ways to share the increased costs of retiree medical coverage with participants. The principle behind “carve-out” is that the retiree pays the out-of-pocket expense he or she would incur had Medicare paid nothing (e.g., his share of coinsurance). This means the retiree has a greater financial obligation until reaching the plan’s out-of-pocket maximum for Medicare’s covered services. However, he or she is protected from the impact of a catastrophic event or from certain costs not covered by Medicare.

The principle behind “exclusion” is to consider only the balance of a claim after Medicare has paid for reimbursement under the plan. In this case when a charge is incurred, the Medicare payment would be subtracted from the claim and, then the balance would be applied to the plan deductible and coinsurance provisions of the plan. The exclusion method usually provides a benefit somewhere between that provided under the other two methods.

The Committee reviewed many examples of how the three coordination methods work, and the difference in benefits each provides. After debating the merits of the three methods and costs for participants and the University, consensus was reached to introduce the “carve-out” method for those employees who retire more than five years after the plan changes are adopted. However, the Committee felt that to protect these future retirees from significant costs increases associated with major illness or injuries, the maximum out-of-pocket expense should be reduced from the current \$3,000 per year to \$2,000 per year. The “carve-out” method is offered under most post-65 plans. It continues to provide valuable protection for plan participants.

Switching the Medicare coordination method to carve-out is projected to reduce OU’s future obligation for providing retiree medical benefit coverage by \$73.9 million. *This is one of the most significant changes available to reduce OU’s future plan liability.*

Recommendation: *The Committee recommends that those employees who become eligible to retire more than five years from the adoption of plan changes should be subject to the following plan design changes in the post-65 OU plan for those retirees eligible for Medicare:*

- *Introduce an annual \$300 deductible*
- *Change the coordination of benefits method with Medicare to “carve-out” and reduce the annual out-of-pocket maximum to \$2,000*

Survey data confirmed that OU’s payment of 100% of the retiree medical plan premium is much more generous than competitive practice. Indeed, OU’s current practice significantly contributes to the University’s projected post retirement benefit costs. Thus, the Committee considered several options for introducing a level of retiree contributions in the future. Multiple factors were identified that might influence the portion of the cost of retiree medical premiums for which the retiree should be responsible.

Much of the discussion centered around the concept that longer University service should be recognized by eligibility for a higher level of benefits. However, this discussion is complicated by the fact that the length of the overall participation in OU retiree medical benefit programs, including time in the more expensive pre-65 medical plan, influences the overall value/cost of the benefit provided. For example, an employee who retires at 52 receives a much more lengthy and costly retiree medical benefit than a person who retires at age 65. On the other hand, future OU retirees, especially those in lower paid jobs during their active employment, may not have the means to afford a portion of the premium for coverage.

To balance these considerations, the Committee investigated numerous age and service matrices in an effort to achieve the appropriate balance between University service, age at retirement, and the value/cost of benefits a retiree would receive. A preliminary Retiree Contribution Matrix was developed as a result of this discussion as follows:

Age at Retirement/ Years of Service At Separation	10 – 14	15-19	20 – 24	25+
Under 55	Employees are eligible to retire with 25 years of service. No OU subsidy until age 55.			
55 – 61	Not eligible	55%	65%	75%
62 – 64	55%	65%	75%	85%
65+	65%	75%	85%	95%

- Employees must have a minimum of 10 years continuous service in all cases
- Employee can defer participation in the OU plan at retirement, with a one-time opportunity to re-enter the plan later upon loss of coverage
- For retirements prior to age 65, OU’s contribution locks in at the percentage indicated above, which is based upon the employee’s years of service at separation and the age at the time participation begins under the OU Plan. **When the retiree reaches Medicare age (65) OU’s subsidy increases by an additional 10%.**

Examples:

- Employee retires at age 52 with 27 years of service and elects to begin coverage under the OU Plan at 59; OU will subsidize 75% of the cost prior to age 65 and at age 65 and later OU will subsidize 85%
- Employee retires at age 52 with 27 years of service and begins coverage immediately at that time; OU will subsidize 0% until age 55, 75% from 55-64 and 85% from age 65 beyond
- Employee retires at age 58 with 22 years of service and elects to begin participation in OU's plan at age 62; OU will subsidize 75% between 62-64 and 85% for age 65 and beyond

Current plan provisions require employees who retire early to enroll in the OU plan immediately upon retirement to preserve their future eligibility for the plan. A clearly beneficial rule change would be to add a "one-time opt-out/opt-in" provision to the plan. Because there are a significant number of retirements prior to age 65, allowing a retiree to defer participation could help reduce the University's costs, while allowing the retiree to participate in another health insurance plan that might provide better benefits or lower costs (e.g., a plan offered through his or her spouse's employer).

Recommendation: The Committee proposes a new arrangement for sharing the cost of retiree medical coverage between the University and employees who were hired prior to 1/1/2008 and become eligible to retire on or after 1/1/2014 (or 5 years after adoption if later):

- *The University provided subsidy of between 55-85% of retiree medical premiums should be based on age at commencement of retiree medical benefits and years of service at separation*
- *The percentage of subsidy is determined upon benefit commencement, and does not change until the retiree reaches Medicare age (65), at which time the OU subsidy will increase by an additional 10% of the premium*
- *Employees are eligible to retire with 25 years of service, but do not become eligible for the OU subsidy until reaching age 55*
- *Employees can defer participation in the OU plan at retirement, with a one-time opportunity to re-enter upon loss of other health plan coverage or upon attaining age 65 whichever is sooner*

It is projected that adding the employee cost sharing above will reduce OU's future obligation for providing retiree medical benefit coverage by \$41.1 million

Additionally, the Committee proposes that employees hired before 1/1/2008 and become eligible to retire on or after 1/1/2019 (or 10 years of service if later) be subject to a "cap" that limits the maximum University annual contribution toward their cost of

retiree medical benefits to two times (2X) the premium subsidy provided in the year this provision is adopted.

It is projected that adding the cap on OU's subsidy will reduce OU's future obligation for providing retiree medical benefit coverage by \$73.5 million

Question: What University sponsored retiree medical program should be implemented for employees hired on or after 1/1/2008, to support the University's employee attraction and retention goals?

The University of Oklahoma Board of Regents approved in December 2007 the exclusion from participation in University subsidized retiree medical benefit plans of those employees hired on or after January 1, 2008. Employees hired after 1/1/2008 may qualify to participate in group medical insurance programs sponsored by the University after they retire and benefit from group rates at their own expense. President Boren indicated in recommending this action to the Regents, that this action was required to help limit the growth of the University's post retirement benefit obligation. While the Committee supports limiting the participation of these current and future OU employees in the retiree medical programs currently offered that are highly subsidized by the University, there is strong support for further study to determine how the University can help these employees prepare financially for the cost of retiree medical coverage. Although the evaluation of options for supporting the retiree medical benefits for these employees could not be addressed during the current review, this issue should be addressed in the near future.

Recommendation: *The Committee recommends that a subsequent review be conducted to determine what type of University sponsored retiree medical insurance support should be provided for employees hired on or after 1/1/2008.*

Note that this will not reduce OU's future obligation of \$589 million as only employees hired prior to 1/1/2008 were included in the measurement..

Closing Comments

The Committee engaged in very thoughtful and vigorous discussion and debate in conducting the analysis and establishing the set of preliminary recommendations included in this report. Many factors, such as faculty and staff attraction and retention, University financial resources, and providing secure benefits to retirees who service the University had to be considered. There were no solutions identified that could shield all stakeholders from the significant financial impact that continued increases in the cost of retiree health insurance expenditures will create.

As you all know, the cost of health insurance coverage is the subject of a major national debate. Nationally, some change in Medicare and other health insurance programs is expected to occur in the future because the present structure is too expensive and cannot be sustained. However, the timing and nature of changes cannot be anticipated, and actions to modify the University's retiree medical programs are required now. Difficult decisions will be required, because the growth in retiree medical costs is occurring at a time when the University is experiencing financial challenges due to limited growth and, sometimes, reductions in state appropriations. Expenditures for retiree medical expenses in the future, if not managed and planned for, will compete for financial resources against programs that are critical to meeting the University's educational and service missions.

The Committee has sought to provide recommendations that offer OU employees a competitive and valuable level of retiree medical benefits that are still affordable to both our retirees and the University. In doing so, we have proposed approaches that shield current retirees and those nearing retirement from the major financial impact that others further from retirement will unfortunately need to face. Necessarily, this introduces the complexity of offering different benefits for different groups of employees depending upon when they meet the requirements to retire. Not only will this be difficult to communicate, it also will be more complex to administer. Nonetheless, we believe that by working together we can meet this challenge, and achieve a sustainable structure for this very important benefit.

The Committee looks forward to your careful review of our report, and your suggestions or comments in advance of our finalizing recommendations to submit to President Boren.

Contribution Strategy and Health Insurance Options Committee

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 - Norm Jacobson
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Special thanks to Nick Kelly, Assistant Human Resources Director – Employee Benefits, who provided significant staff support to the Committee

Retiree Medical Redesign Cost Implications: January 1, 2008 Valuation

PROPOSED PLAN CHANGES
Groups 1 and 2 : No Change
Group 3: Add \$300 deductible, Medicare carve-out with a \$2,000 Out-of-Pocket Maximum and contributions
Group 4: Add \$300 deductible, Medicare carve-out with a \$2,000 Out-of-Pocket Maximum & 2x cost cap

Scenario	Baseline	Preliminary Recommendation
Total Present Value as of January 1, 2008 of Future OU Benefit Payments (in Millions)		
• Group 1: Retirees as of 1/1/2008	\$106.8	\$106.8
• Group 2: Actives currently eligible and actives who will be eligible by 1/1/2014	172.3	172.3
• Group 3: Actives not eligible by 1/1/2014 but will be eligible by 1/1/2019	108.8	62.8
• Group 4: All other actives hired prior to 1/1/2008	201.2	43.7
<i>Total Actives</i>	\$482.3	\$278.8
Total Present Value of Benefits	\$589.1	385.6
Change in liability due to adding a \$300 deductible		\$(15.0)
Additional change due to switching to Carve-out		(73.9)
Additional change due to adding the Contribution Matrix		(41.1)
Additional change due to adding 2x Cap		(73.5)
Total Reduction in Liability		\$(203.5)

Preliminary Retiree Contribution Matrix

PROPOSED AGE/SERVICE CHART SHOWING OU CONTRIBUTION

Age at Benefit Commencement Years of Service At Termination	10 – 14	15-19	20 – 24	25+
Under 55	Employees are eligible to retire with 25 years of service. No OU subsidy until age 55.			
55 – 61	Not eligible	55%	65%	75%
62 – 64	55%	65%	75%	85%
65+	65%	75%	85%	95%

- Employees must have a minimum of 10 years continuous service in all cases.
- Employee can defer participation in the OU plan at retirement, with a one-time opportunity to re-enter the plan later upon loss of coverage.
- For retirements prior to age 65, OU's contribution locks in at the percentage indicated above, which is based upon the employee's years of service at separation and the age at the time participation begins under the OU Plan.
- **When the retiree reaches Medicare age (65) OU's subsidy increases by an additional 10%.**

Some examples:

- Employee retires at age 52 with 27 years of service and elects to begin coverage under the OU Plan at 59, OU will subsidize 75% of the cost prior to age 65 and at age 65 and later OU will subsidize 85%
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- Employee retires at age 58 with 22 years of service and elects to begin participation in OU's plan at age 62. OU will subsidize 75% between 62-64 and 85% for age 65 and beyond.

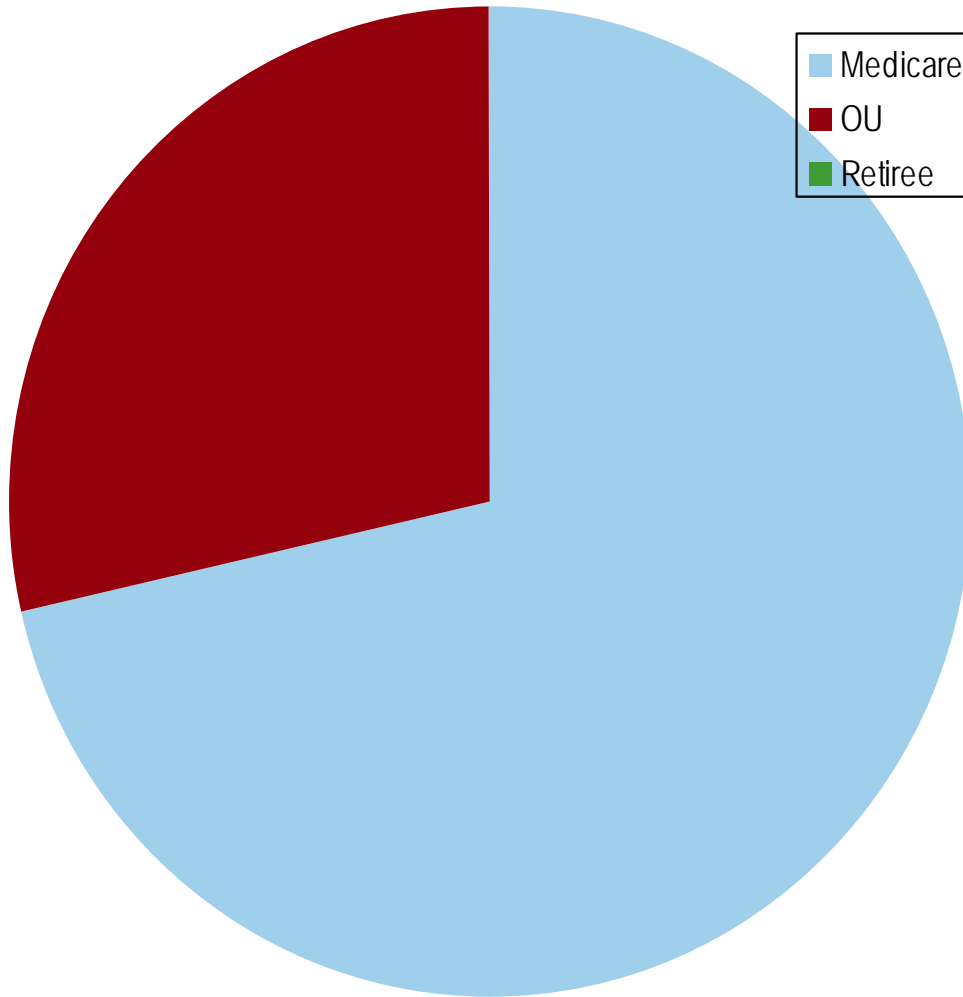
How does OU's Plan Coordinate with Medicare

- › When someone retires and is eligible for OU continued medical coverage and is eligible for Medicare, they receive medical coverage from both OU and Medicare. When claims are incurred, Medicare will pay for the cost of the service 1st, then OU determines what portion of the remaining balance, if any, is payable from our plan. The amount payable depends on the Medicare Coordination approach that we apply.

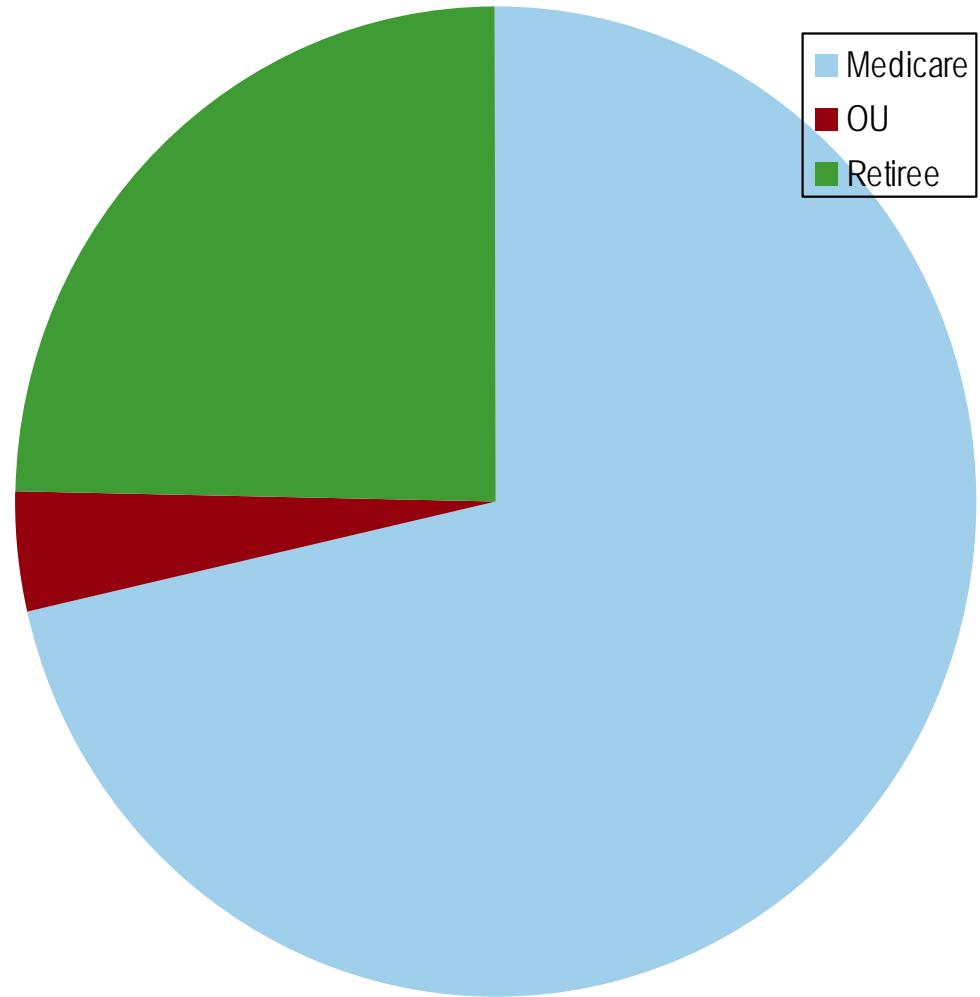
We are currently using the Coordination of Benefits method when determining OU's payment from the plan. For future retirees who will meet the plans eligibility requirements after December 31, 2013 (or 5 years after adoption if later) we are recommending switching to the Carve-out approach. **The pages that follow describe how these two methods would apply.**

How Does OU's Post-65 Program Integrate with Medicare

Medicare Coordination: Current Plan



Medicare Coordination: Proposed



Medicare Coordination Methods

There are three traditional ways that an institution's retiree medical plan will integrate with Medicare, each of which varies in how they calculate the plan payment:

1. **Standard Coordination of Benefits (COB)**
 - The principle behind COB is for the plan to pay the full amount not paid by Medicare, but no more than it would pay if Medicare had not paid anything
2. **Exclusion (also referred to as Maintenance of Benefits)**
 - The principle behind Exclusion is to treat the claim as the balance after Medicare, then apply the plan deductible and coinsurance to this balance
3. **Carve-Out (also referred to as Benefit Reduction or Benefits Less Benefits)**
 - The principle behind Carve-Out is that the retiree has the same out of pocket expense as that retiree would have had if Medicare had not paid anything

Medicare Cost Sharing (2008)		Employer Plan	
Part A Deductible	\$1,024	Deductible	\$300
Part B Deductible	\$135	Out-of-Pocket Maximum (excluding deductible)	\$2,000
Part Coinsurance	B 20%	Coinsurance	20%

Medicare Integration Example – Low Utilizer

Medicare Payment Calculation					
Charges	Total	Medicare Pays		Participant Pays	
		Part A	Part B	Part A	Part B
Hospital	\$0	\$0		\$0	
Doctor	\$1,000		\$692		\$308
Total	\$1,000	\$0	\$692	\$0	\$308
	Total \$1,000	Medicare \$692		Participant \$308	

Coordination of Benefits	
Plan Benefit Calculation	
1. Total Claim	\$1,000
2. Deductible	300
3. Balance (1) – (2)	700
4. Coinsurance (20% x (3) to max of \$2,000)	140
5. Balance Payable by Plan (3) – (4)	560
COB Calculation	
1. Total Claim	1,000
2. Medicare Paid Expense	692
3. Participant Balance Under Medicare (1) – (2)	308
4. Plan Pays Smaller of: (5 Above) - Active Plan Payment or (3) - Medicare Balance Plan Payment	560 308 \$308
5. Retiree Pays Balance (3) – (4)	\$0

Carve-Out	
1. Total Claim	\$1,000
2. Deductible	300
3. Balance (1) – (2)	700
4. Coinsurance (20% x (3) to max of \$2,000)	140
5. Balance (3) – (4)	560
6. Medicare	692
7. Plan Payment (5) – (6) (minimum \$0)	\$0
8. Retiree Pay (1) – (6) – (7)	\$308

Medicare Integration Example – Medium Utilizer

Medicare Payment Calculation					
Charges	Total	Medicare Pays		Participant Pays	
		Part A	Part B	Part A	Part B
Hospital	\$3,500	\$2,476		\$1,024	
Doctor	\$1,500		\$1,092		\$408
Total	\$5,000	\$2,476	\$1,092	\$1,024	\$408
	Total \$5,000	Medicare \$3,568		Participant \$1,432	

Coordination of Benefits	
Plan Benefit Calculation	
1. Total Claim	\$5,000
2. Deductible	300
3. Balance (1) – (2)	4,700
4. Coinsurance (20% x (3) to max of \$2,000)	940
5. Balance Payable by Plan (3) – (4)	3,760
COB Calculation	
1. Total Claim	5,000
2. Medicare Paid Expense	3,568
3. Participant Balance Under Medicare (1) – (2)	1,432
4. Plan Pays Smaller of: (5 Above) - Active Plan Payment or (3) - Medicare Balance Plan Payment	3,760 1,432 \$1,432
5. Retiree Pays Balance (3) – (4)	\$0

Carve-Out	
1. Total Claim	\$5,000
2. Deductible	300
3. Balance (1) – (2)	4,700
4. Coinsurance (20% x (3) to max of \$2,000)	940
5. Balance (3) – (4)	3,760
6. Medicare	3,568
7. Plan Payment (5) – (6) (minimum \$0)	\$192
8. Retiree Pay (1) – (6) – (7)	\$1,240

Medicare Integration Example – High Utilizer

Medicare Payment Calculation					
Charges	Total	Medicare Pays		Participant Pays	
		Part A	Part B	Part A	Part B
Hospital	\$25,000	\$23,976		\$1,024	
Doctor	\$15,000		\$11,892		\$3,108
Total	\$40,000	\$23,976	\$11,892	\$1,024	\$3,108
	Total \$40,000	Medicare \$35,868		Participant \$4,132	

Coordination of Benefits	
Plan Benefit Calculation	
1. Total Claim	\$40,000
2. Deductible	300
3. Balance (1) – (2)	39,700
4. Coinsurance (20% x (3) to max of \$2,000)	2,000
5. Balance Payable by Plan (3) – (4)	37,700
COB Calculation	
1. Total Claim	40,000
2. Medicare Paid Expense	35,868
3. Participant Balance Under Medicare (1) – (2)	4,132
4. Plan Pays Smaller of: (5 Above) - Active Plan Payment or (3) - Medicare Balance Plan Payment	36,700 4,132 \$4,132
5. Retiree Pays Balance (3) – (4)	\$0

Carve-Out	
1. Total Claim	\$40,000
2. Deductible	300
3. Balance (1) – (2)	39,700
4. Coinsurance (20% x (3) to max of \$2,000)	2,000
5. Balance (3) – (4)	37,700
6. Medicare	35,868
7. Plan Payment (5) – (6) (minimum \$0)	\$1,832
8. Retiree Pay (1) – (6) – (7)	\$2,300

Medicare Integration Examples Summary

	Low Utilizer			Medium Utilizer			High Utilizer		
	No Medicare	COB	Carve-Out	No Medicare	COB	Carve-Out	No Medicare	COB	Carve-Out
Total Charges									
Hospital	\$0			\$3,500			\$25,000		
Doctor	\$1,000			\$1,500			\$15,000		
Total	\$1,000			\$5,000			\$40,000		
Payments									
Medicare	\$0	\$692	\$692	\$0	\$3,568	\$3,568	\$0	\$35,868	\$35,868
Plan	\$560	\$308	\$0	\$3,760	\$1,432	\$192	\$37,700	\$4,132	\$1,832
Retiree	\$440	\$0	\$308	\$1,240	\$0	\$1,240	\$2,300	\$0	\$2,300