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Subject: Proposed contribution to OPEB

Members of the Finance Committee,

As you may be aware, I am out of the office for vacation next week, so I wanted to provide my recommendation for a transfer of unexpended funds within the Insurance 32B line-item of the unclassified budget to the OPEB trust fund. The Insurance 32B line-item funds active and retiree health insurance premiums, as well as the planned contribution toward our OPEB liability.

The OPEB obligation is real, even if the state has yet to mandate full-funding by 2040 as it has with retirement system liabilities. All evidence suggests that this obligation will continue to grow when the next actuarial valuation report is received. The demographics tell the story. Despite negotiated changes in plan design, health care costs will continue to rise between 5-10% per year by all industry estimates. Life expectancy continues to increase. Forecasted rates of return on investments are stable or slightly lower based on the past several years. Unlike the retirement system, where those hired since the mid-1990's contribute 9% + 2% of wages in excess of \$30,000 into the retirement system (practically financing their own benefit), the percentage of employee contributions can't be reduced below 50% under current state law. So there is no relief from cost-shifting as was done with pensions. And it is unlikely that a special commission studying OPEB due to report in December 2012 will recommend any significant changes to reduce long-term liabilities. A similar commission on retirement tinkered with widely reported excesses in the system, and making minimal changes in benefits for those hired after July 1, 2012.

In March 2012, the Finance Committee discussed the past practice of sweeping health insurance premium savings that resulted in a favorable budget variance into the OPEB fund. Because the contributions over the prior few fiscal years had resulted in a trust fund balance in excess of the annual recommended contribution (ARC), there was considerable pressure brought by budget activists claiming the OPEB account is "overfunded." Mr. Boschetto argued that the health insurance budget expected to contain excess amounts than that required for active and retired employee premiums, and if the Finance Committee so chose, it could "offset" a significant portion of the FY2013 budget cut with supplemental contributions to OPEB. As a result, Town Meeting was persuaded on a narrow 220-198 vote to eliminate the ARC funding of \$1,313,000 in FY2013. The amendment characterized the contribution as an unnecessary, discretionary contribution to an irrevocable trust the elimination of which would result in a 2% tax reduction. There was no analysis presented showing the impact on the this obligation by eliminating the contribution, nor any explanation offered as to how contributions would be made in FY2014 and beyond without a significant increase in the budgetary base and resulting tax rate. It was a pocket-book decision made without adequate information being provided by proponents. While feel-good votes are the prerogative of Town Meeting, the Finance Committee is charged with taking a longer-term view toward the fiscal well-being of the Town, and I urge you to discount arguments of some that making a FY2012 year-end transfer is in any way related to the decision of Town Meeting to eliminate funding in FY2013.

Simply put, arguments that the OPEB trust is “overfunded” are false and the obligation can be set aside for future citizens to address are irresponsible. It is a prudent management practice to take one-time savings and apply it to non-recurring expenses. These FY2012 funds were earmarked by citizens at Town Meeting for health care expenses. It is entirely appropriate to apply the savings in the 32B line-item to the OPEB liabilities rather than to let these funds otherwise lapse to free cash. Making the transfer will reduce the annual required contribution in future years, and save taxpayers more than the amount transferred due to the return on investment of these assets.

Fred Turkington
Town Administrator