Rules to Expose Long-Term Cost of Health Plans

By ROBERT PEAR
New York Times • published June 21, 2004

WASHINGTON (June 20) New accounting standards will require state and local governments to acknowledge the full cost of health benefits promised to retirees, putting immense pressure on public employers to reduce their liabilities by scaling back benefits or shifting more of the cost to retirees, government officials and accountants say.

Supporters say the rules will help state and local officials, investors and taxpayers understand the magnitude of these commitments to current and future retirees.

But public employees, civil servants, police officers, firefighters, judges, teachers and state university professors predict that the rules, combined with the soaring cost of health care, will speed the erosion of health insurance in the public sector, as happened at many private companies in the early 1990's.

The rules, developed by the Governmental Accounting Standards Board, an independent nonprofit organization, apply to all state and local governments. They require employers to measure and report the long-term costs of retiree health benefits while employees are still working. Under current practice, most public employers do not report such costs until they pay for the promised benefits, often many years after employees have retired.

"State and local governments have generally been looking at the tip of the iceberg," said Karl D. Johnson, project manager for development of the new rules. "Our standards require them to measure the iceberg. Many public employers have never looked under the water. They just looked at what they could see on the surface, what they have to pay this year for current retirees without measuring the cost of their commitment to provide retiree benefits to large numbers of active workers."

In large states, Mr. Johnson said, such unfunded liabilities for retiree health benefits total billions of dollars.

The standards are set forth in two documents. In April, the seven-member board issued financial reporting standards for health plans that cover state and local government employees. It is scheduled to give final approval this week to a companion document, which sets accounting standards for public employers that sponsor such plans.

The board, formed in 1984, is a private entity, but accountants and auditors accept its pronouncements as authoritative. State and local governments have a strong incentive to follow its standards because compliance helps them borrow money in the bond market at favorable rates.

Most public employers finance retiree health benefits on a pay-as-you-go basis, as bills come due. Experts on employee benefits said the new standards would encourage state and local officials to set aside money in trust funds for the purpose of providing health benefits to retirees.

The cost of such contributions would be a new, immediate expense for state and local governments, many of which are already struggling with severe financial problems.

Labor unions and health plan administrators said the standards could jeopardize health benefits for millions of retired public employees. Moreover, they said, the standards will cause a fiscal shock to state and local government agencies and could harm their bond ratings.

"We are concerned that a lot of our retirees will end up losing their health benefits," said Frederick H. Nesbitt, executive director of the National Conference on Public Employee Retirement Systems.

The Financial Accounting Standards Board, a sister organization, issued similar standards for private employers in 1990. Many companies have cited those standards as a reason for cutting retiree health benefits.

"What's going to happen in the public sector is exactly what happened in the private sector," Mr. Nesbitt said.

Daniel C. Givens, a Florida firefighter who is chairman of the Miami Firefighters Relief and Pension Fund, said: "The new standards will suddenly put a strain on the city for a long-term liability that has been *[continued, over]*

developing for years and years.

Retirees will feel the brunt of the impact. They can expect to see reductions in benefits and increases in costs."

Public employers are more likely than most industries to offer health benefits, but the prevalence of retiree coverage in general has been declining. In a survey of large private and public employers, the Kaiser Family Foundation found that 38 percent offered retiree benefits last year, down from 66 percent in 1988. When coverage is still available, premiums, co-payments and deductibles are increasing.

Melvyn Aaronson, treasurer of the United Federation of Teachers in New York, said, "The new accounting standards will accelerate those trends."

The board sets accounting standards for 80,000 state and local governments, affecting more than 15 million employees. About three-fourths of state governments and more than half of local governments provide health benefits to retirees.

Many of the arrangements were adopted years ago, when costs were relatively low, but "times have changed, and many employers now spend 5 percent to 10 percent of payroll, or more, on retiree health benefits," said Paul Zorn, a consultant at Gabriel, Roeder, Smith & Company, which advises more than 400 state and local government entities.

Under the standards, public employers will have to disclose the assets and long-term liabilities of their health plans. They will also have to calculate the amount of annual contributions that would be needed, over many years, to provide the promised benefits.

Cynthia B. Green, a member of the governmental standards board, said: "Historically, government employees have sacrificed salary increases for promises of enhanced benefits. These governments rarely calculate the price tag. They almost never consider whether the promises are affordable. A retiree may have been promised generous benefits, but if the employer can't honor the promise, what good is it?"

Ms. Green, a former vice president of the Citizens Budget Commission, a watchdog group in New York, said she did not know if the critics' "dire predictions" would come true. "If governments find out they have big liabilities," she said, "some may cut spending, some may raise taxes and others may change the benefit package. Or they could combine these options."

Unions contend that the standards will force public employers to overstate their liabilities for retiree health benefits, because the standards ignore the fact that employers can reduce or eliminate health benefits in the face of fiscal pressures.

But the board refused to let employers take credit for savings that might result from benefit cuts in the future. Such bookkeeping techniques "lack objectivity and would give recognition to changes that have not occurred and may not occur," the board said.

Cathie G. Eitelberg, senior vice president of the Segal Company, a benefits consulting firm, said the new disclosures would draw attention from taxpayers and elected officials.

"When taxpayers see the magnitude of the unfunded liability," Ms. Eitelberg said, "there will be changes in the way benefits are financed and delivered, because ultimately the taxpayer pays the bill."

Things To Come Department

The proposed change in accounting standards is not an innocent technical issue. The Governmental Accounting Standards Board is a private organization funded by...? Cynthia B Green, a member of this board is a former vice-president of the equally private Citizens Budget Commission.

The CBC, last year, explained that all 35 hour per week city government workers should go to a 40 hour work week with no raise in pay, give up pension and health benefits, and generally agree to sacrifices in order to save 600 million dollars a year for New York City. We did not agree, we did not give them their 600 million dollars and, marvel of marvels, Mayor Bloomberg has 600 million dollars available to build a stadium anyway.

Not to worry. When the rich, business, anti-tax, anti-worker types make their arguments, as they are highly paid to do, we respond. We respond well. – ***Bob Croghan***