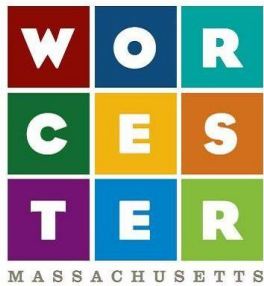


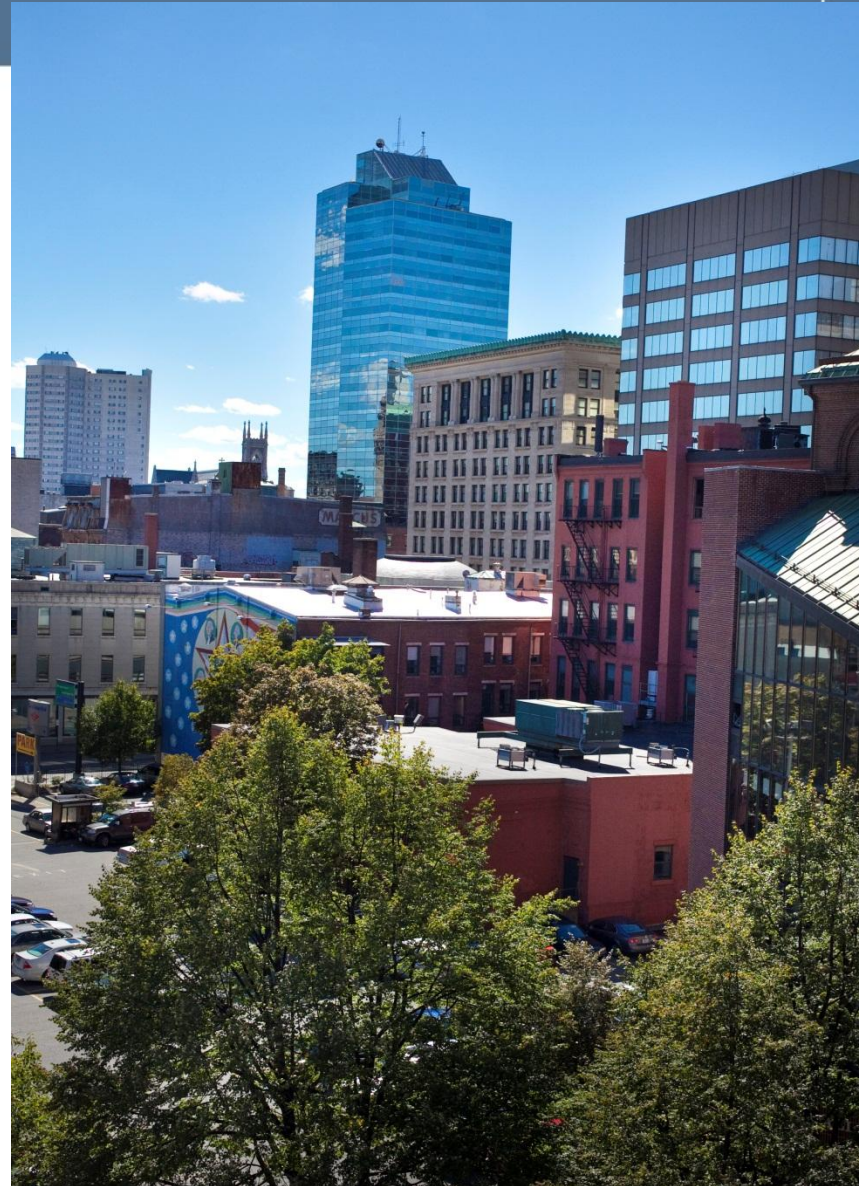


Municipal OPEB Obligations: The Clock is Ticking

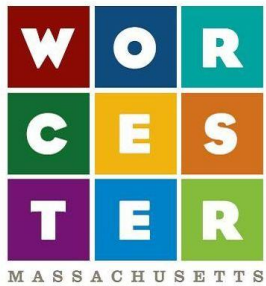
Michael V. O'Brien, City Manager
City of Worcester, Massachusetts



Introduction



- Second Largest City in New England; population of 181,000
- Strong Economic Base – Health Care, Education, Advanced Manufacturing, Financial Services
- Educated Workforce
- Vibrant Economic Development
- #4 for Job Growth (*WSJ*)
- #9 Most Recession Proof City (*Daily Beast*)
- #9 Most Livable City in U.S. (*Forbes*)



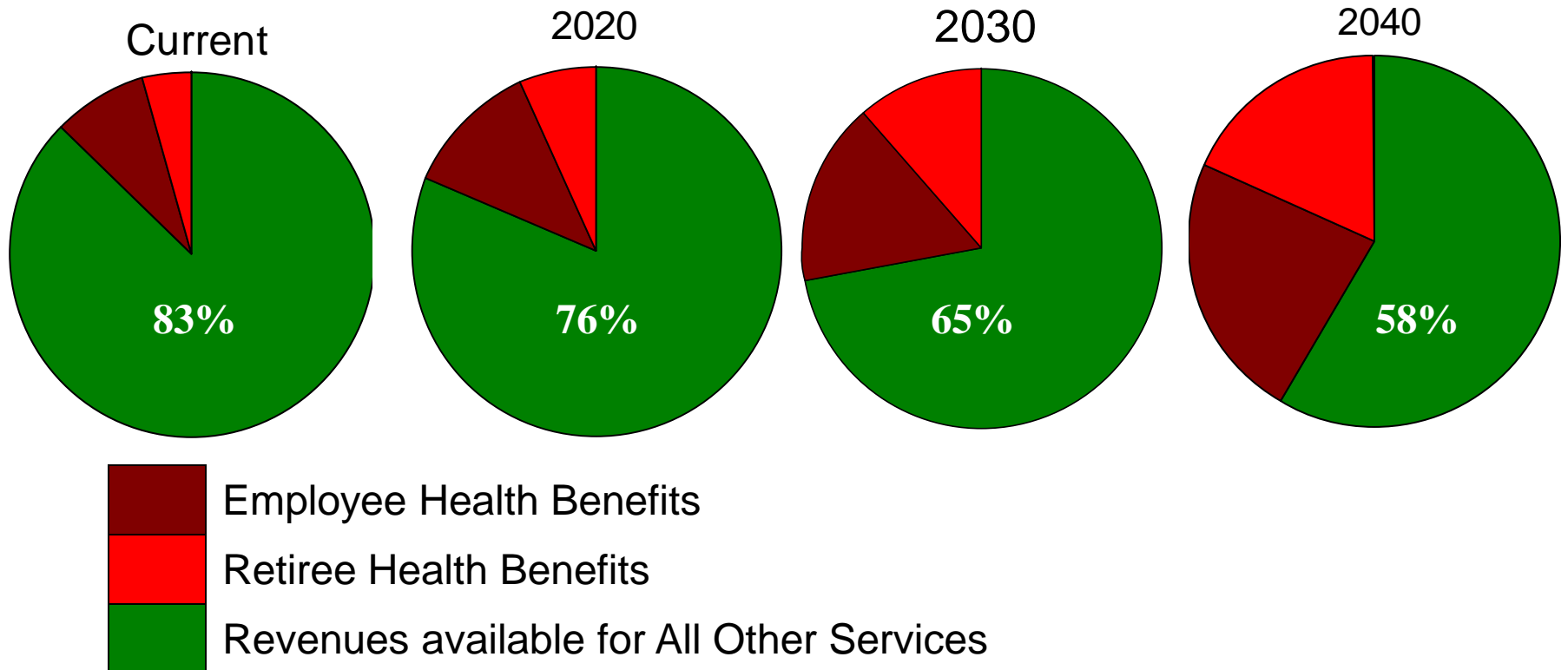
Municipal Government

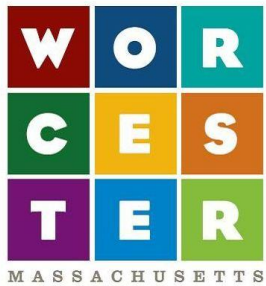
- Total Budget = \$606M; Public Schools = \$313M
- 4,500 Employees; 4,800 Retirees (*First Time Surpassed Active Employees*)
- Downsized City Government – Loss of 225+ Positions in Three Fiscal Years; 15% Workforce Reduction; Early Retirement Incentive Given to 55.
- Revenue Growth Not Keeping Up With Rising Fixed Costs
- Unrestricted State Aid Cut by \$20M Annually; Local Receipts Down By Almost 17%
- \$1B in Total Unfunded Benefit Liabilities



Bottom Line

If Revenues Continue to Grow at 3% Annually, and Retiree Benefits Continue to Grow at 9%, Revenues for All Other Services Decline.





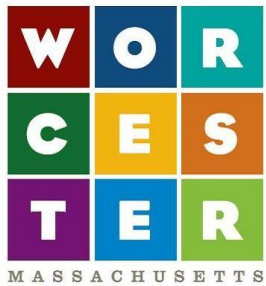
Unfunded Liabilities: Worcester's Approach

- Two Significant Unfunded Liabilities
- Fund Pension Liability (~\$300 M)
 - 70% Funded
 - City Meets Annual Required Contribution
 - In FY13, Total \$32.7 M
- Reduce OPEB Liability (~\$765 M)
 - Pay As We Go, Set Aside \$0, No Trust Fund
 - If We Were to Fund this Liability Over a 30-year Term, We Would Have Had to Set Aside \$53.7 M in FY2012 to Pay Current Benefits and Properly Begin to Fund Future Obligations; Annual Budgeted Contribution in FY12 was \$21.8 M
 - We Are Appropriating Nearly \$32 M Less Than our Obligation Requires
 - Enacted and Implemented Reasonable, Retiree Health Care Reforms Reduced Our Once Over \$1.1 B Liability By Almost a Third, to a Now Staggering \$665 M



Progressive Reform

- Enacted and Implemented Reasonable, Retiree Health Care Reforms
 - Increased Employee/ Retiree Contribution Rates (from 10% to 25%)
 - Adopted Section 18; Required Retirees to Transition to Medicare
 - Implemented GIC-Like Health Plans; Increased Co-payments
 - Transitioned All Active Employees and Retirees to GIC-Like Health Plans
- **Good News:** Reduced Our Once Over \$1.1 B Liability By Almost a Third, to a Now Staggering \$665 M
- **Bad News:** Remaining Liability is Unaffordable and Unsustainable, Threatening Our Ability to Provide Basic Municipal Services Long-Term
- Incremental Year-to-Year Increases in our Appropriations Will Be Outstripped 2-to-1 by Actual Costs of these Benefits in the Years Ahead.



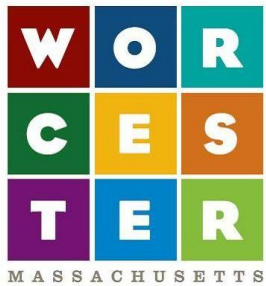
Pension and OPEB Liability Funding Strategies

- **Pensions**

- Liability Calculation is More Stable, Variables Less Volatile
- Includes an Employee Contribution into Benefit Funding
- Does Not Include Teachers for Cities
- Have Graduated Benefits Based on Years of Service
- Have Variable Benefits Based on Salary Level

- **Health Insurance (OPEB)**

- Liability Must Account for Health Cost inflation—Who Really Knows?
- Includes all City and School Employees
- Grants the Same Benefit Regardless of Years of Service or Salary Level
- Actual Cost of Benefit is Subject to Great Variation—Who Knows Health Care Cost Inflation Rate in FY20?



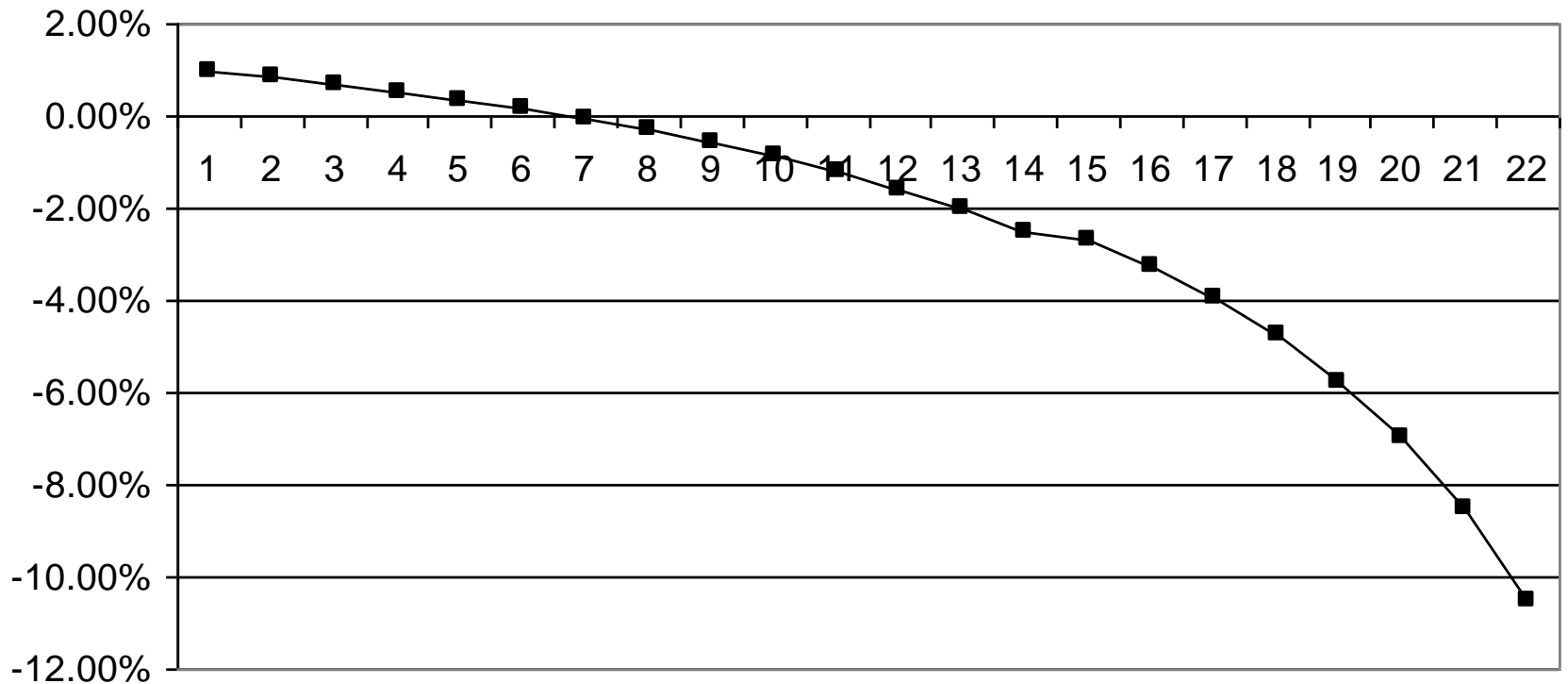
What Does the Future Hold in a World Without Reform

- Growing OPEB Costs Will Continue to Consume A Greater Percentage of Funds for Core Services
- Service Erosion from OPEB Costs Can Be Assumed Without a Funding Source and Without Reform
- Is Prefunding Realistic for Most Cities? No. Adequate Pre-funding is Out of Reach for Most Municipalities.
- Adequate Pre-funding in FY12 for Worcester Would Have Created a Deficit of More than \$30 M.



What Can We Expect for Growth in Other Services?

Annual % Growth/ Gross Cuts in funds for all other services: Excluding Health and Pension Costs





MASSACHUSETTS



What Should Be Done?

For Consideration of the Committee—

- Reform is Needed Now for Future Employees and Retirees
- MTF Recommendations Should Be Considered
 - Pro-rate Benefit Amount for Years of Service (Similar to Pensions)
 - Raise Eligibility Age for Retiree Health Care Benefits
 - Increase Eligibility Hours and Pro-rate Benefits for Part-time Employees
 - Reduce Municipal Share of Premium Costs
 - Terminate Dependent Coverage