City of Alexandria, Virginia

MEMORANDUM

DATE: APRIL 20, 2009

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: JAMES K. HARTMANN, CITY MANAGER

SUBJECT: BUDGET MEMO # 113 : ELIMINATION OF POST EMPLOYMENT LIFE INSURANCE FOR ACTIVE EMPLOYEES

This memo is in response to a request from Councilman Wilson that City Council be provided additional details on potential savings resulting from the elimination of the City's post employment life insurance benefit for current employees who are first eligible to retire with unreduced benefits on or after July 1, 2014. It should be noted that the estimates contained in this budget memo were conducted by City staff in an effort to conserve both time and money and not done by an actuary. A professional analysis of this question should be professionally conducted by an outside, independent actuary as has long been the practice for the City's retirement plan costing.

Since 2000 the City's practice has been to provide post employment life insurance at two times the value of an employee's final salary. Prior to 2000, the City had long provided life insurance for retirees at one times final salary. The life insurance amounts available to a retiree are reduced by 25% beginning at the first January 1 after the retiree turns 65. The benefit is then reduced by 10% each subsequent year until the January 1 after the retiree turns 70 years of age. After age 70, the retiree will have no further reductions in the life insurance payable. The remaining amount is approximately 25% of the life insurance that was in place at the time the retiree separated from City service. According to a recent study by Watson Wyatt, it was found that this amount of coverage was the highest of all our comparator jurisdictions, and that providing such post employment life insurance benefits were the common practice. The Virginia Retirement System (VRS) provides post employment benefits to State employees, and to most local government employees who are part of the VRS system.

Currently there are about 750 retired employees who receive the City's life insurance benefit as described above. In addition, there are about 2,300 active employees on-board receiving the life insurance benefit. This brings the total number of insured lives to about 3,050.

Of the total number of active employees, about 268 are within 4 years of retirement eligibility within VRS, and are considered highly likely to draw the life insurance benefit. Another 115 lives are within 4 years of retirement eligibility for the Fire and Police pension system. All total, there are 1,133 lives (750+268+115=1,133) that are currently receiving or are eligible to receive within 4 years the City's post employment life insurance benefit.

One suggestion from Councilman Wilson for a cost savings option is to eliminate the post employment life insurance benefit for current employees who are first eligible to retire on or after July 1, 2014. This proposal would reduce benefits for an estimated 1,917 active employees (2,300-268-115=1,917).

A prior actuarial study determined the cost of pre-funding the post employment life insurance liability consistent with Other Post Employment Benefit (OPEB) guidelines is $2.4 million annually (See page 8-17 of the FY 2010 Proposed Budget for additional information). If the $2.4 million in unfunded liability was spread evenly over the 3,050 insured retires and active employees the cost would be $786 per person annually. The annual average of $786 represents the cost at two times salary.

Using the annual benefit base of two times salary, the savings would appear to be $1.5 million (1,917x$786=$1.5 million). However, the average liability for the 1,917 is lower then the 1,133 who would remain insured by the City. There are several factors for this:

- Those employees within the group of 1,917 who have just joined the City workforce or who are mid-career are not nearly as likely to retire from the City and draw a life insurance benefit as those who are closer to retirement.
- Those employees within the group of 1,917 have fewer years of service and therefore represent a disproportionately smaller share of the accrued post employment life insurance liability.
- These employees also represent a disproportionately smaller amount of the cost because employees who are closer to retirement are generally paid more than the average City employee, and life insurance is more expensive for older employees than younger ones.
- The group of 1,917 employees is represented by a greater number of general employees than uniformed officers. This factor disproportionately impacts costs because uniformed employees have higher average salaries than general salary employees, and are comprised of more males, which means they have higher mortality rates and thus higher costs.

Taking these factors into consideration, to presume a savings of $1.5 million may be too high. One half of that amount is probably still too high. We would guess actual savings might be closer to a third of that amount, or $500,000. However, this estimate remains a very rough guesstimate and should be verified through a rigorous analysis by our outside, independent actuary.

City staff does not recommend this reduction in benefits at this time. The savings are too uncertain and the competitive affects are too unknown. Further examination and review of the Watson Wyatt study results will yield an idea of the best total compensation package for City employees and the role life insurance benefits, if any, should play in that package. As a result it would be premature to eliminate this post employment benefit until Council has an opportunity to look at and to establish a comprehensive pay and benefits policy.