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March 16, 2010

Ms. Sue Goodrick
Benefits Manager
County of Mendocino
579 Low Gap Road
Ukiah, CA 95482

Subject: County of Mendocino Non-Medicare Eligible Retirees Health Coverage Covered Under the Active Health Plan

Dear Sue:

The County has asked Mercer to comment on the possibility of covering the Non-Medicare eligible retirees (retirees) under the County of Mendocino's Active employee health plan.

It has been argued that the monthly employee only active employee rate for Plan II is very similar to the calculated rate for retirees effective July 1, 2010. The 2010 monthly rate for employee only coverage is $654.55 while the retiree rate is $681.15.

While these rates are very similar, it is important to note that the active rate includes reserve accumulation for IBNR and stabilization reserves. By years end, it is anticipated that the reserves will be fully funded at $5,913,441.

The retiree rate covers cost only. No stabilization reserve is contemplated, while the IBNR reserve ($820,000) is earmarked out of the excess earnings. Transference of the non-Medicare eligible retirees to the active plan would contemplate either 1) the transference of IBNR funds from excess earnings or 2) the payout of IBNR out of excess earning and the subsequent accumulation of IBNR reserve under the active plan in the first plan year.

No stabilization reserve is included in the current projected retiree rates. Stabilization reserve is defined as three months of claim cost. Based on 417 eligible retirees, the stabilization reserve would be approximately $650,000.

Given the reserving element included in the active employee rate, the 2011 renewal would adjust downward 13.4% to cover cost and maintain fully funded reserves. The rate would be $566.84. It is understood that the County will most likely implement a rate which will show 0.0% rate adjustment and accumulate excess reserves (maintain the $654.55 rate for 2011).

The 2011 non-Medicare retiree rate equivalent would be $702.54 to cover plan expenses and IBNR reserve. An additional $145.78 per retiree per month would need to be implemented to provide a stabilization reserve. The County could also elect to fund the non-Medicare retiree stabilization reserve over multiple years as it did with the active plan. This would reduce the $145.78 per retiree per month. The total rate to cover non-Medicare cost, IBNR reserve and stabilization reserve would be $848.22 per retiree per month. This compares to an active rate of $566.84 or $654.55 per employee per month for employee only coverage.

The County could elect to blend the active rate with the non-Medicare eligible rate. This would introduce implied subsidies from the active health plan to the non-Medicare retiree health plan coverage. The total rate to cover health plan costs, IBNR reserve and stabilization reserve on a blended basis would be $638.87 per retiree/employee per month for single coverage. The blended rate would include an implied subsidy of $1,047,592 from the active plan to the non-Medicare eligible retirees.

Please note that this analysis assumes no adverse selection is introduced to the non-Medicare retiree population. It is important to understand that as County contributions to non-Medicare retiree coverage decrease or are eliminated, those non-Medicare eligible retirees that can qualify for less expensive alternative health care coverage, will elect less expensive alternative health care coverage. The remaining non-Medicare retirees will be the less healthy retirees. This adverse selection, will impact cost significantly upon each renewal and could increase the amount of cross subsidies substantially in blended rates.

When considering moving the non-Medicare retirees with the Active employee health plan it is important to understand the underlying costs, reserves elements, potential implied subsidies, and adverse selection. This analysis does not take into consideration the impact on any current County policies and bargained agreements that may exist.

Mercer looks forward to reviewing this with the County. Should you have any questions, please contact me at (916) 286-5403.

Bordan Darm
Principal