Facing the Challenge of Retiree Health Care: Liabilities and Responses of State and Local Governments

Herb Bergson
Former Mayor of Duluth, MN
Health costs bleeding Duluth dry

PAYING FOR RETIRES' CARE

The issue: Duluth is one of many governments nationwide struggling with how to honor agreements to insure the health of retirees.

Worst-case scenario: Bankruptcy — though most agree the city is working proactively enough to reduce its unfunded liability, currently projected to be more than $900 million.

How generous? Duluth pays for everything not covered by Medicare, for as long as the retiree lives, at no cost to the retiree. Also covered is the retiree's spouse, even after the retiree's death.

The justification: Retirees and employees say they've given up a lot of pay and benefits over the years to retain free retiree health care. They also say it's the right thing for the city to do, and they say it should be emulated across the country.

LARRY OAKES

Riders take pride the distance year

JAMES, who now lives in North Carolina, started the driver's Butt Lite as a snipoff of the Iron Butt rally, which covers 12,000 miles in 11 days all over North America and is considered the premier motorcycle endurance event in the world.

"You start off knowing you're going to push yourself," James said.

"You're in a competitive frame of mind for 11 days. Every minute of the 11 days you have to be doing something right, even when you're sleeping."
Duluth Mayor Herb Bergson’s administration has developed a six-step plan to reduce this unfunded liability. It’s a combination of new investments, the creation of an irrevocable trust fund and concessions from current employees.

1 Create irrevocable trust. The city of Duluth will be allowed to establish an irrevocable trust for the purpose of setting money aside to cover the liability. This is a trust that cannot be used for ANYTHING other than paying for retiree health care expenses. The city needs the consent of the state legislature to create such a fund. Because of the large amount of Duluth’s liability, and lost opportunities to invest available funding at higher rates of return, Duluth urges the legislature to enact a “Duluth only” bill early in the 2007 session.

2 Start with $12 million. The city would initially fund the trust with $10 million from our Community Investment Trust Fund (CIT), or the “casino money,” and $2 million from our health care fund balance. Presently, the interest from the casino money pays for the street improvement fund’s debt service. The CIT currently has a principal balance of $60 million, but for this purpose, it would be reduced to about $50 million, and the interest earnings available to pay for streets would be reduced.

3 Invest with the State Board of Investment. The trust’s funds can be invested with the State Board of Investments (SBI), the same board that handles state pension funds. The SBI has a long track record of high rates of return—about 9.5-10%. There is actually a fee paid to the SBI for managing the funds, so it is really a “win-win.”

4 Reinvest remaining Community Investment Trust money. The balance of the CIT fund would be invested with the SBI as well. This would generate a higher rate of interest, and offset the loss in interest from pulling the $10 million from principal. Currently, CIT money earns about a 4.6% rate of return.

5 Earmark revenue from TIF districts. Duluth has three Tax Increment Financing (TIF) districts that are about to close. One of them sunsets in 2007, and two sunset in 2009. The city’s share of this new tax revenue is approximately $1.1 million annually. This revenue will be assigned to the irrevocable trust, as well as funds from modest utility rate increases.

6 Union concessions. These steps do not lessen the important role our employee bargaining units have in solving this problem. We will continue to seek concessions from active employees and retirees. And so far, we’ve had some success. The city supervisors’ union recently signed a contract that requires they pay more for health care, both now and in the future. We also have tentative agreements with both the fire department and the confidential unit that will make additional concessions to help us get to where we have to go. It’s a great first step.

This plan will help generate hundreds of millions over the next 20-30 years—helping to fund the liability without devastating tax increases for Duluthians.