To: New Jersey State League of Municipalities
From: New Jersey Pension and Health Benefits Study Commission
Date: February 23, 2016
RE: Questions on Supplemental Report

Thank you for your very thorough February 18, 2016 memoranda, which raise many good questions. As you have pointed out, "fairness" in solving this crisis can be a matter of perspective. This is true both with respect to where the impact falls between employees and taxpayers, and between State and local government. Roughly, half the State budget is devoted to property tax relief funding. Conversely, a third of local spending is paid for with State funds. With this kind of interrelationship, anything done to solve the "State" benefits funding problem is going to have a local impact. The question is what that impact will be.

The possibility that increasing demands for revenue to fund State public employee benefits will crowd out State aid to municipalities and school districts needs to be considered. The current amount of property tax relief, $16.8 billion, already exceeds the amount of income tax revenue, $14.4 billion, dedicated to property tax relief (part of which is already used to pay TPAF pension and retiree health benefits). This means that benefits funding and every other budget line item is in direct competition with property tax relief for the $2.4 billion in non-income tax revenues now needed to merely keep property tax relief funding even, let alone what would be needed to reduce property taxes by increasing school funding[1] or restoring utility tax revenues to municipalities.[2] In contrast, the Commission's comprehensive reform of State pension and health benefits, and local health benefits, would address this problem without a property tax increase.

We also understand your concern over the potential ambiguity of "private sector" benefits. This is why the Commission quantified proposed coverage as an 82% actuarial value gold level plan. The broad experience of large corporations providing this level of coverage suggests that it is workable for both employers and employees. Finally, there are equitable reasons why taxpayers should not be asked to fund benefits substantially better than what they receive themselves.

The private sector benchmark, however, is flexible. The Commission has made clear that "relevant differences between public and private sector employment should be reflected in related coverage terms," 2016 Report, p. 16, and that there may be reasons to continue some benefits, for example, early retiree health benefits for certain public sector positions, even if these benefits would be rare in the private sector. The Commission, while advocating comprehensive reform, has not attempted to solve all of the problems of the current benefits program to every level of detail (why we have not discussed changing retirement ages, for example). Instead, we have sought to bring people to the table by providing a template of minimal reforms necessary to restore fiscal soundness, leaving the details to be worked out when the people who will be most affected by resolution of these issues return to the table.

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[1] http://www.njspotlight.com/stories/16/02/16/christie-s-plan-offers-barely-more-aid-to-schools-but-it-could-be-worse/

[2] http://www.njspotlight.com/stories/16/02/08/lawmakers-push-to-return-utility-tax-funds-to-hard-pressed-municipalities.

Turning to some specific points raised in your memoranda:

The Projected Savings Do Not Assume Any Savings from Local Pension Reform

Many of your comments appear to assume the Commission is proposing to reform local PERS and PFRS pensions. That is no longer the case. Our 2015 Report had proposed municipal pension reform. A more detailed analysis of potential health benefits reforms, however, revealed that there would be more than sufficient savings from reforming school district active employee and municipal active and retiree health benefits to accommodate shifting the teachers' cash balance plan and teachers' retiree health benefits to the local tax base without this shift resulting in an increase of property taxes. As explained in the footnote on the bottom of page 1 of the 2016 Report discussing changes over the past year in the Commission's thinking on the scope of reform, "while reform of local health benefits is essential, subsequent discussions have highlighted reform of local-funded pensions as an issue for further consideration and stakeholder input."

While there are arguments on each side of the local pension reform issue, it is not necessary to resolve that issue now. As a result, the 2016 Report makes no assumption of any savings from local pension reform. All of the local savings claimed in the 2016 Report are derived strictly from health benefits reform.

Amount of Local Costs and Savings

Similarly, your observation that "the total savings are greater than the gross expenditure reported for health savings by the communities" appears to reflect an understandable misconception. When the Commission speaks of health benefits funded by "communities," this includes municipal active employee and retiree health benefits ***and*** the school district active employee health benefits also paid through the local tax base. Looking at the data for Brick, for example:

	Current Employer Cost	Post-Reform Employer Cost	Savings
Municipal Active	$5,979,641	$3,983,936	$1,995,705
Municipal Retirees	$4,704,706	$2,782,986	$1,921,720
District Actives	$27,492,173	$18,316,660	$9,175,513
Total	$38,176,520	$25,083,582	$13,092,938

The total savings of $13 million are greater than the $10.7 million total current *municipal* cost, but not higher than the total current $38 million cost including the active teacher health benefit costs. For reasons of space and clarity, Exhibit 17 shows only total savings and shifted costs, broken down further in Note 85, which shows the source of the savings (municipal active, municipal retiree and school district active). Because the table in Note 85 already extends the full width of the page, the current employer costs were not shown, but are included for your information in Exhibit A of this memorandum.

As for how these costs and savings were determined, as explained in Note 83 to the 2016 Report, for the ten community case study two different approaches were used to calculate post-reform costs for each subscriber group in each community. The first proportionately reduced the employers' current costs for each subscriber group by the same percentage as the reforms are projected to reduce costs in the State-run plans: ~33% for active employees and a blended average of ~41% for early and Medicare retirees (use of a blended average for municipal retiree costs is necessary since municipal User-Friendly Budgets do not report these costs separately). The second approach reduced employers' costs to the same average per-subscriber costs for that subscriber group in the post-reform State-run plans. To be conservative, the projections in the 2016 Report use the higher of a proportionate reduction in costs or the post-reform State-run plan costs, thereby yielding the highest post-reform costs and lowest resulting savings. Expressed differently, the average cost in the State plan was used as a minimum post-reform cost even if a proportionate reduction of a particular local employer's costs suggested lower post-reform costs and thus greater savings.[3]

Finally, we can further confirm your conclusion that the municipal active employee costs in Exhibit 16 are in "basic agreement" with the figures you found in your review of user-friendly budgets. In three communities (Dover, Glassboro and Randolph), the differences are merely due to rounding. In three more (Brick, Montclair and Pennsauken), the minimal differences are likely due to the Commission including in the "employee" headcount and cost totals elected officials receiving health benefits. In the four remaining communities where the differences are somewhat greater (Burlington Twp., Hamilton, Hillside and Sparta) this is due to those four municipalities not having reported receiving any employee premium contributions (Burlington Tp., Hamilton and Hillside also have elected officials receiving benefits). As set forth in Note 82, in these municipalities, the Commission's projections, to be conservative, assume the reported current costs are total premium costs towards which employees contribute, on average, 17.7% of premium costs. If the reported figures actually reflect the employer-only cost, the savings resulting from the shift for these communities would be greater.

[3] In preparing this response, we noted that the average State-plan cost for active employees, $11,010, was in error entered as the blended average post-reform cost for retirees. As the actual post-return blended cost is $10,460, the error is *de minimis* as it resulted in a slight *understatement* of potential savings for Glassboro, Hillside, Montclair and Sparta.

Municipal Active Employees

Community	Current Cost	Post-Reform Costs	Savings
Brick Tp.	$5,979,641	$3,897,540	$2,082,101
Burlington	$2,392,964	$1,332,210	$1,060,754
Dover	$1,530,366	$924,840	$605,526
Glassboro	$2,225,998	$1,299,180	$926,818
Hamilton	$7,525,975	$5,372,880	$2,153,095
Hillside Tp.	$2,230,058	$1,673,520	$556,538
Montclair	$4,306,838	$3,303,000	$1,003,838
Pennsauken	$3,538,706	$1,959,780	$1,578,926
Randolph	$2,017,011	$1,200,090	$816,921
Sparta	$1,835,484	$990,900	$844,584

Municipal Retirees

Community	Current Cost	Post-Reform Costs	Savings
Brick Tp.	$4,704,706	$2,782,986	$1,921,720
Burlington	$888,617	$525,646	$362,971
Dover	$1,878,480	$1,111,182	$767,298
Glassboro	$1,270,773	$803,730	$467,043
Hamilton	$8,001,672	$4,733,248	$3,268,424
Hillside Tp.	$2,026,377	$1,607,460	$418,917
Montclair	$926,538	$924,840	$1,698
Pennsauken	$2,623,472	$1,551,869	$1,071,603
Randolph	$1,952,416	$1,154,917	$797,499
Sparta	$896,383	$627,570	$268,813

School District Active Employees

Community	Current Cost	Post-Reform Costs	Savings
Brick Tp.	$27,492,173	$18,316,660	$9,175,513
Burlington	$8,298,808	$5,529,081	$2,769,727
Dover	$5,427,902	$3,616,340	$1,811,562
Glassboro	$5,468,330	$3,643,275	$1,825,055
Hamilton	$29,202,277	$20,379,510	$8,822,767
Hillside Tp.	$6,678,073	$4,459,050	$2,219,023
Montclair	$13,592,643	$10,459,500	$3,133,143
Pennsauken	$17,941,254	$11,953,360	$5,987,894
Randolph	$11,882,988	$7,917,041	$3,965,947
Sparta	$7,757,777	$5,168,619	$2,589,158