Program Evaluation Division
North Carolina General Assembly

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Unfunded Actuarial Liability for Retiree Health is Large, but State Could Save Up to $64 Million Annually by Shifting Costs to Medicare Advantage Plans

Summary

The Joint Legislative Program Evaluation Oversight Committee's 2013–15 Work Plan directed the Program Evaluation Division to examine the funding status of North Carolina's Retiree Health Benefit Fund. The fund contributes the State's share of retiree premiums to the State Health Plan, which provides several health plan options to non-Medicare-eligible (younger than 65) and Medicare-eligible (65 and older) retirees. In 2004, the Governmental Accounting Standards Board began including in its standards that state governments report liabilities for retiree health benefits on an accrual basis.

North Carolina's unfunded actuarial liability for the Retiree Health Benefit Fund is $25.5 billion. Several factors explain the large unfunded liability: benefits are funded on a pay-as-you-go basis (meaning benefits are funded when they are provided rather than prefunded during an employee's active employment); retirees with sufficient contributory service are eligible for a non-contributory benefit (meaning the State pays 100% of their premium); and benefits are available to essentially all retirees with the requisite number of years of service.

North Carolina is not a strong performer on any of the measures used to compare the funded status of states. In Fiscal Year 2012–13, North Carolina ranked 41st in unfunded liability per state resident for retiree health benefits, with only eight states performing worse. It was one of 38 states with a funded ratio of 10% or less for its retiree health benefits and one of 26 states that paid less than 50% of its annual required contribution.

The General Assembly could consider the following options to reduce the unfunded liability of the Retiree Health Benefit Fund: (1) increase the appropriation to the fund, (2) shift more costs to the federal government, (3) transition to a defined contribution model, (4) reduce the number of individuals eligible for the benefit, (5) require active employees to contribute to the fund, and (6) increase the amount retirees pay for the benefit by increasing premiums and out-of-pocket costs.

To address the unfunded liability, the General Assembly

- should direct the State Treasurer and State Health Plan Board of Trustees to shift costs to the federal government by requiring eligible retirees to be on Medicare Advantage plans, generating an estimated savings of up to $64 million annually, and
- could appoint a joint committee to determine which of the report's other options to pursue in light of the financial and legal implications discussed in this report.