



ADVISORY & FINANCE COMMITTEE

The following meeting of the Advisory & Finance Committee has been posted and will be held

At: Plymouth Town Hall
11 Lincoln Street
Mayflower II Meeting Room
Plymouth, MA 02360

On: Wednesday, January 21, 2015 at 7:00PM

Items on the agenda will include but are not limited to the following. Other discussion may include items that were not reasonably anticipated by the Chairman 48-hours in advance of the meeting posting.

AGENDA ITEMS:

- Article 20: New Bylaw – Regulations: Swear in Appointees Larry Pizer
Town Clerk

- Retiree Health Care Carolyn Ryan
Massachusetts Taxpayers Foundation

Public Comment

Old/New/Other Business

Meeting Minutes

Next Meeting: Wednesday, January 28, 2014 - Mayflower II Room – Town Hall

Memo

To: Advisory and Finance Committee
From: Laurence R. Pizer, Town Clerk
Date: January 12, 2015
Re: Proposed Bylaw Regulating the Swearing-In Process

"All elected and appointed officials shall be qualified by the Town Clerk within 30 days of their appointment or reappointment except where a different period is specified in the General Laws. If an appointed official is not qualified in this period, his appointment shall terminate and the appointing authority shall be so notified by the Town Clerk."

Article 20 proposes to add Chapter 123, "Oath of Office" to the General Bylaws and to include the language as Section 1.

Although there has been an improvement in convincing appointees to take the required oath before performing committee responsibilities, Plymouth has not come close to universal success. *Chapter 41 §107, of the Massachusetts General Laws states, "Every other elected member and every appointed member of every board or commission of a town, and every other elected officer and every appointed officer of a town, shall also, before entering upon his official duties, be sworn to the faithful performance thereof."* Thus, it mandates that appointees take their oath before serving. Failure to do so exposes the Town to liability if a complainant took exception to the action of a committee with members serving without legal authority.

Similar bylaws or ordinances are in effect in the Town of Blackstone and the City of Woburn.

Memo

To: Advisory & Finance Committee
From: John Moody, Chairman
Date: January 13, 2015
Re: Other Post-Employment Benefits (OPEB) Materials

The following materials are being distributed as background information for the presentation on OPEB from Carolyn Ryan arranged by Harry Salerno for our January 21 meeting. These are not part of Ms. Ryan's presentation, per se, but provide a background for that presentation.

Upon hearing that we would be discussing OPEB, Tom Kelly, Chairman of the Plymouth Retirement Board, requested that some of these materials (*Mass. Retires Response* and *Retiree Health Care Costs Straining Budgets*) be distributed to the Committee to provide the retiree perspective on the issue. I added to these materials the original report (*The Brick That Broke*), which is referenced in Mr. Kelly's requested materials.

Please review these materials in advance of the January 21 meeting so that we may have a more effective dialogue about this complex matter.

Thanks.



MASS RETIREES

Be the voice of the Massachusetts Retiree

Retiree Healthcare Siege Continues

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MTF Report Misleading

OCTOBER 1, 2014: Last week, the Mass. Taxpayers Foundation (MTF) released its latest report on municipal retiree health insurance. As expected the report finds that the cost of municipal health insurance plans is unsustainable, and as such, benefit reductions are called for. Click here to view the report.

Unfortunately, the MTF report has drawn undue attention from the Boston media. Just last Saturday the [Boston Herald editorialized](#) (see "[The Retiree Dilemma](#)") on the subject, largely echoing the MTF recommendations.

We believe this typical MTF report uses selective data to produce results that reflect their agenda – a flawed methodology that most reputable professional research entities would not utilize in trying to compile an objective analysis.

Specifically, limiting the use of property tax levy in the 10 "poorest" communities as the focal point for the report's findings is not really an objective measuring stick. State aid and other revenues, generally doubling the property tax levy, must be included in the equation to objectively analyze a community's ability to pay.

In addition to poor methodology, the report intentionally neglects to state the \$250M in health care savings that resulted from the Governor and legislature passing municipal Health Care Reform in 2011. Ironically, the report omits the City of Fall River from its findings and the Health Care Reform savings to the taxpayer in that city was over \$8M in FY14 and a total of \$12.104 million since FY13!!

Further, several of the communities profiled by the latest MTF report have not enacted the reforms already passed by the Legislature over the past five years. Simply put, the tools are already available for municipalities to gain control over local healthcare costs.

Four of the profiled communities have reported a collective savings of \$16.468 million as a result of instituting municipal insurance reforms. However, the MTF fails to mention this data in their report.

- **Amherst \$1.683 million**
- **Chelsea \$1.405 million**
- **Fall River \$12.104 million (FY12-14)**
- **Fitchburg \$1.190 million**

We understand that further health care reforms will have to be discussed, but shifting even more costs on public retirees and employees is not the solution. And taking health coverage away from non-Medicare eligible retirees is definitely not the way to go!

Our Association remains committed to working with the legislature, policy makers and the incoming administrations to resolve these important issues.

Report on the City of Fall River's savings from the Health Care Reform



Bulletin

September 22, 2014

Retiree Health Care Costs are Straining Budgets in the State's Poorest Cities

In 2011, the Foundation published *Retiree Health Care: The Brick That Broke Municipalities' Backs*, a groundbreaking report that detailed the enormous liabilities for retiree health care facing municipalities in Massachusetts. Cities and towns in the state are estimated to have a total of \$30 billion in unfunded retiree health care liabilities, and funding those obligations would crush municipal budgets and taxpayers.

Following the Foundation's report, the state formed an Other Post-Employment Benefits (OPEB) Commission in 2012 to study what drives the liabilities and to make recommendations for reform. These recommendations were the basis for the Governor's reform proposal in 2013 to toughen eligibility standards and link benefits to length of service. The Legislature has taken no action on his or any other proposal for OPEB reform.

Facing liabilities that are simply unaffordable and beyond their capacity to fund in advance, municipalities instead use a "pay-as-you-go" approach (referred to as "paygo") in which they fund only their share of health care premiums for that year's retirees. Under such an approach, municipalities set nothing aside for the costs of benefits that current employees will receive upon retirement. Instead, those obligations are pushed into the future and added to existing liabilities.

However, relying on paygo to meet obligations has serious consequences. As annual spending on retiree health care grows, the fiscal squeeze already pressuring municipalities tightens further and forces cuts in basic services. Even if municipalities ignore their long-term obligations and do not pay down their retiree health care liabilities, they cannot escape the fact that those costs are rising and eroding the resources available for important services like education and public safety.

This bulletin analyzes retiree health care spending in nine of the 10 municipalities with the lowest per capita incomes in the state and populations of at least 10,000. It includes data for Amherst, Chelsea, Everett, Fitchburg, Holyoke, Lawrence, New Bedford, North Adams, and Springfield.¹ The bulletin examines two measures of retiree health care costs: the increase in retiree health care spending relative to the increase in property tax revenues between fiscal 2009 and fiscal 2013, and retiree health care spending as a share of total property tax revenues in fiscal 2013.

¹ Per capita income data is as reported by the Division of Local Services. Fall River, which has one of the 10 lowest per capita incomes and population greater than 10,000, did not begin reporting its retiree health care costs until fiscal 2012 so it is excluded from this analysis. Data from 2013 is included in Tables 2 and 3 for reference.

Municipalities have few options for controlling paygo costs because benefit eligibility is determined almost entirely by state law. An employee needs only 10 years of service to receive full benefits for life beginning as early as age 55.² In many municipalities, part-time employees qualify for the same benefits as full-time employees. Furthermore, nearly all municipalities contribute at least 50 percent towards the cost of premiums, though many contribute more than that. With such generous benefits, it is not difficult to understand why the costs of retiree health care are growing much faster than property taxes.

Retiree Health Care Costs Outpacing Growth in Property Taxes

Between fiscal 2009 and fiscal 2013, the total costs for retiree health care coverage in the nine municipalities rose from \$71.8 million to \$88.8 million, an increase of 24 percent, while property taxes grew at half that rate, a modest 12.1 percent.

The surge in retiree health care costs, ranging as high as 44 percent growth in Amherst, means that a large share of increased property tax revenues was dedicated to paying for these benefits rather than addressing other needs. In fact, the increase in retiree health care costs consumed 26 percent of the growth in property taxes in the nine communities between fiscal 2009 and 2013, as Table 1 on page 3 shows.³

The jump in retiree health care spending is especially striking when considered in the context of the tiny two percent growth in the total budgets of these nine communities between 2009 and 2013. As a result of the fiscal squeeze, they reported nearly 1,000 fewer full-time employees in fiscal 2013 than in fiscal 2009 as they held wage and salary growth to \$8.7 million, or one percent—half the \$17 million increase in retiree health care costs.

The Challenge of Finding Municipal Financial Data

Historically, there was little reporting required on retiree health care costs. That changed with the implementation of new standards from the Governmental Accounting Standards Board (GASB), effective for most Massachusetts municipalities beginning in fiscal 2009.

However, despite the reporting requirement, there remains a significant lack of transparency on retiree health care costs—and, for that matter, finances in general—in many communities. As noted in this bulletin, Fall River only began reporting retiree health care liabilities in fiscal 2012, a full three years after the GASB deadline. Furthermore, the current requirements are just the beginning—GASB has already expanded pension reporting requirements and, over the next several years, will expand retiree health care reporting requirements as well.

The lack of financial accountability and transparency speaks to a larger issue that the state and municipalities must address. Only five of the 10 poorest communities had a financial statement from the most recent fiscal year readily available online. In some cases, the annual budgets are little more than a listing of various accounts without any discussion of revenue or expenditure changes, trends, or other factors that affect budgets. Only in rare cases do budgets provide a separate line item for annual retiree health care spending.

Clear, accurate financial information is crucial to understanding the scope of these enormous burdens. In addition, residents are entitled to understand how a municipality spends its revenues, and should have easy access to current and historical data that is presented in a useful manner. Technology makes it easier than ever for municipalities to provide this information to residents.

² For employees hired after April 2, 2012, the eligibility age increased by five years for each pension classification. Most hires (Group 1) are still eligible for benefits as early as age 60 and public safety groups are eligible as early as age 55.

³ Some of the increases in retiree health care spending may include modest contributions to OPEB trust funds, but those are only a fraction of what municipalities should be setting aside to pay for benefits. Property tax revenues include not only the increased property taxes on existing property owners but also the revenues resulting from newly constructed property.

Table 1: Growth in Retiree Health Care Costs Compared to Growth in Total Property Taxes, 2009-2013

Municipality	Retiree Health Care, 2009	Retiree Health Care, 2013	Difference, Retiree Health Care 2009-2013	Total Property Tax Levy, 2009	Total Property Tax Levy, 2013	Difference, Property Tax Levy, 2009-2013	Retiree Health Care Cost Growth as a % of Property Tax Growth
Amherst	\$2,139,934	\$3,075,000	\$935,066	\$34,871,426	\$41,799,726	\$6,928,300	13%
Chelsea	3,375,643	4,111,897	736,254	33,263,028	41,208,288	7,945,260	9%
Everett	5,183,195	6,349,879	1,166,684	73,489,134	87,262,044	13,772,910	8%
Fitchburg	5,443,728	5,942,982	499,254	36,531,102	42,312,177	5,781,075	9%
Holyoke	7,439,577	9,077,923	1,638,346	44,639,085	51,281,090	6,642,005	25%
Lawrence	7,843,000	10,328,000	2,485,000	45,012,874	54,761,398	9,748,524	25%
New Bedford	12,537,241	15,806,016	3,268,775	88,797,309	95,218,502	6,421,193	51%
North Adams	2,861,058	2,943,932	82,874	11,052,149	13,686,384	2,634,235	3%
Springfield	25,004,396	31,172,202	6,167,806	163,078,974	167,403,337	4,324,363	143%
Total	71,827,772	88,807,831	16,980,059	530,735,081	594,932,946	64,197,865	26%

Sources:

Retiree health care costs and premium contribution rates are as reported in annual financial statements, fiscal years 2009 and 2013. Chelsea's 2009 retiree health care cost as reported in the 2009 financial statement did not include retired teachers so the city provided revised 2009 data. Property tax data is from the state's Division of Local Services.

In Springfield, retiree health care costs jumped from \$25 million to \$31.2 million between fiscal 2009 and 2013, almost 50 percent greater than the \$4.3 million increase in property taxes over the same period. Clearly, it becomes impossible to fund basic services when retiree health costs are consuming more than the entire growth in property tax revenues. For example, had Springfield's retiree health care costs held steady instead of increasing by \$6.2 million, the city could have funded some 75 additional teachers.⁴

New Bedford faces a similar squeeze as the growth in retiree health care costs consumed half of the growth in property tax revenues, rising from \$12.5 million in fiscal 2009 to \$15.8 million in fiscal 2013. That 26 percent increase in retiree health care was more than three times the 7.2 percent growth in property tax revenues.

Notably, these increases occurred despite steps taken by several municipalities to control costs, such as requiring eligible retirees to enroll in Medicare, adopting municipal health reform, or reducing contribution levels.

Retiree Health Care Consumes a Large Share of Property Tax Revenues

Even in the communities in which retiree health care grew at a slower rate, those costs consume a large share of property tax revenues. As Table 2 details, in fiscal 2013 retiree health care costs were equal to 15 percent of total property tax revenues in the nine municipalities, ranging from seven percent in Amherst and Fitchburg to 22 percent in North Adams.

Table 2: Retiree Health Care Costs as a Percentage of Property Taxes, Fiscal 2013

Municipality	Retiree Health Care, 2013	Total Property Tax Levy, 2013	Retiree Health Care Costs as a % of Property Tax Levy	Average Single Family Tax Bill, \$ Amount to Retiree Health Care
Amherst	\$3,075,000	\$41,799,726	7%	\$479
Chelsea	4,111,897	41,208,288	10%	N/A
Everett	6,349,879	87,262,044	7%	N/A
Fitchburg	5,942,982	42,312,177	14%	419
Holyoke	9,077,923	51,281,090	18%	589
Lawrence	10,328,000	54,761,398	19%	477
New Bedford	15,806,016	95,218,502	17%	459
North Adams	2,943,932	13,686,384	22%	445
Springfield	31,172,202	167,403,337	19%	467
Total	88,807,831	594,932,946	15%	N/A
<i>Fall River</i>	<i>18,445,638</i>	<i>79,433,714</i>	<i>23%</i>	<i>582</i>

⁴ The Department of Elementary and Secondary Education reports the average teacher salary for Springfield in 2013 was \$58,693. The estimate adds a 33 percent benefit factor to that salary amount to account for the costs of health insurance and other benefits.

In North Adams, \$445 of the average single family homeowner’s property tax bill was dedicated to retiree health care in fiscal 2013. For the average single family homeowner in Holyoke, the retiree health care costs consume more than \$500 of the annual tax bill. In each municipality, the average single family homeowner pays more than \$400 per year to fund the costs of retiree health care.⁵

Not only are property taxpayers funding retiree health care at the expense of other services, they are also funding a benefit that most of them do not receive. Few residents have access to any retiree health care benefits themselves, let alone the generous ones provided by municipalities. According to the Agency for Health Care Quality and Research, in 2013 only 7.3 percent of Massachusetts private sector establishments offer health insurance to retirees over age 65, and only 8.8 percent offer it to retirees prior to age 65. This includes employers that require retirees to pay the entire share of premiums. By contrast, all but one of the nine municipalities contribute 75 percent or more of the cost of premiums (Table 3).

Table 3: Municipal Contribution Rates for Retiree Health Care Premiums

Municipality	Municipal Share of Premium
Amherst	75% to 90%
Chelsea	75% to 82.5%, includes part B
Everett	85% to 90%
Fitchburg	70 to 75%
Holyoke	50%
Lawrence ⁶	80%
New Bedford	75%
North Adams	75%
Springfield ⁷	75%
<i>Fall River</i>	75%

The state’s municipalities, and particularly the poorest cities and towns, are facing a long-term fiscal squeeze with retiree health care consuming an ever larger share of limited growth in local budgets. Massachusetts cities and towns simply cannot afford the exceedingly generous benefits that they currently provide.

As costs and liabilities grow each year, it becomes more urgent for the Legislature to implement reforms. The reforms must increase the eligibility from 10 years of service to at least 20 years,

⁵ The cost per average single family tax bill is not calculated for Chelsea and Everett. These two municipalities are among the 13 statewide that provide residential property tax exemptions; the Division of Local Services does not report the average single family tax bill data for such communities.

⁶ In its fiscal 2013 financial statement, Lawrence reports that it contributes 75 percent towards retiree health care premiums. However, the city’s contribution is listed as between 80 percent and 90 percent, depending on the date of retirement, on the rate sheet provided by the GIC, of which Lawrence is a member. The city contributes 75 percent towards the health care premiums of active employees.

⁷ Springfield contributes 78 percent towards Medicare premiums for retirees whose pensions were less than \$30,000 as of June 30, 2006.

tie benefits to years of service, pro-rate benefits for part-time employees, and eliminate expensive pre-Medicare coverage. In order to address these huge unfunded liabilities, the reforms must apply to a broader group than new hires.

The Massachusetts Taxpayers Foundation is a nationally recognized, independent, nonprofit research organization whose purpose is to promote the most effective use of tax dollars, improve the operations of state and local governments, and foster positive economic policies. Over the past 20 years the Foundation has won 16 national awards for its work on health care access and costs, transportation reform, business costs, capital spending, state finances, MBTA restructuring, state government reform, and municipal health reform.



Massachusetts Taxpayers Foundation

Retiree Health Care:
*The Brick That Broke
Municipalities' Backs*

FEBRUARY 2011

MTF

The Massachusetts Taxpayers Foundation is a nationally recognized, nonprofit research organization whose purpose is to promote the most effective use of tax dollars, improve the operations of state and local governments, and foster positive economic policies. Our credibility is based upon independent, objective, and accurate analysis of state and local spending, taxes, and the economy. Over the past decade the Foundation has won fourteen national awards for our work on transportation reform, business costs, capital spending, state finances, MBTA restructuring, state government reform, and health care.

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Retiree Health Care:
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MASSACHUSETTS TAXPAYERS FOUNDATION

FEBRUARY 2011

We would like to recognize
MTF Policy Analyst Carolyn Ryan as
the principal author of this report.

Retiree Health Care: The Brick That Broke Municipalities' Backs

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Retiree Health Care: The Brick That Broke Municipalities' Backs

Taxpayers have long understood government pension liabilities and the impact on local budgets, but government obligations for other post-employment benefits provided to employees (OPEB), namely retiree health insurance, have only recently started to receive similar attention. New reporting requirements force governments to disclose their OPEB liabilities, and the numbers show that retiree health benefits are no longer the marginal annual budget items they were when initially offered to employees. Instead, the rapid acceleration of health care costs combined with overly generous benefits have created staggering OPEB liabilities which exceed unfunded pension liabilities in almost all Massachusetts communities. Without action, these OPEB liabilities will continue to escalate with enormous consequences for cities and towns.

While a handful of Massachusetts communities have begun to fund their OPEB liabilities with modest contributions, the aggregate liability is more than 99 percent unfunded. Enormous OPEB liabilities, combined with existing pension obligations, threaten the long-term stability of local government finances and are already crippling municipalities' ability to provide basic services, including public education.

What is OPEB?

The term OPEB refers to all benefits, other than pensions, that retirees receive. For public employees in Massachusetts, OPEB largely consists of retiree health insurance but also includes life insurance. As with pension benefits, employees are entitled to these benefits after meeting certain eligibility requirements, such as a vesting period and minimum retirement age.

The increased focus on government OPEB obligations comes partly as a result of

requirements issued by the Governmental Accounting and Standards Board (GASB) in June 2004. Referred to as GASB 45, these standards require all government entities to report their annual OPEB obligations, unfunded liabilities, and various assumptions in annual financial statements. GASB 45 brought governments in line with private sector reporting requirements that have existed for 20 years.

Under GASB 45, governments must disclose the present value of their incurred OPEB costs for both current retirees and active employees already eligible for benefits. The liability defines how much the governments need to set aside today in order to continue to provide these benefits over time, based on a variety of assumptions. Such reporting also helps to gauge the true cost of employee compensation by forcing governments to quantify the present value of a future retirement benefit, even though an employee may not receive that benefit for many years.

Like the earlier pension statements issued by GASB, Statement 45 outlines technical and reporting requirements but does not set policies for governments to address liabilities. As a technical rulemaking board, this is typical for GASB. Although there is no requirement to pre-fund these liabilities, those governments that choose pay-as-you-go over pre-funding place a heavier burden on future taxpayers.

GASB 45 included a three-year phase-in of reporting requirements, with the largest governments being the first to implement the policy. Fiscal year 2009 was the first in which all 351 Massachusetts communities were required to disclose OPEB liabilities.

OPEB has historically received less attention than public sector pensions and employee health insurance, but it is an

important component of employee costs. Although GASB 45 forced disclosure, the total liabilities remain a buried note at the back of financial statements. In theory, OPEB data should be readily available, but in reality it is often difficult to find. Decentralized reporting and the lack of funding requirements lead to haphazard availability of local government OPEB data.

To fill the void and provide a clearer picture of the impact on taxpayers, the Taxpayers Foundation researched and analyzed data from the 50 largest communities in the state, based on population, providing the first broad look at municipal OPEB liabilities in Massachusetts.

Huge Liabilities

The total OPEB liability for the top 50 communities is a breathtaking \$20 billion—nearly \$5 billion larger than earlier estimates of the total liability for all 351 communities in the state.¹ The OPEB liability for the remaining 300 communities, plus regional school districts, will likely add at least \$5 to \$10 billion to this burden. The retiree health care problem threatens to wreak havoc with local government budgets, and no individual community is immune. Governments already owe this, and the liability is rising every year.

Retiree health care liabilities² are driven by several factors which can vary from community to community. Table 1 and Appendix A provide details on the liabilities for all 50 municipalities, which range from \$59 million in Dartmouth to more than \$4.5 billion in Boston. Each community

calculates its own liability and chooses its own assumptions for investment performance and health care cost growth. A higher assumed rate of return and a lower cost growth assumption would reduce the liability. The health plan design, number of people covered, and employees' share of contributions all also affect the liability.

The \$20 Billion Liability

Table 1 shows a total liability of approximately \$18 billion, but we use a \$20 billion liability throughout this report for several reasons:

- Two communities did not have any data available. Based on liabilities in similar communities, we estimate that the liabilities in Fall River and Woburn would add \$500 to \$750 million to the aggregate liability.
- GASB guidelines require that entities relying on pay-as-you-go use a short-term interest rate assumption, but Weymouth and Lynn use an 8 percent return assumption. If these communities had followed GASB guidelines, we estimate it would add \$500 to \$650 million to the aggregate liability.
- Many communities are relying on old data to report their liabilities. For 34 communities, the most recent actuarial valuations were conducted prior to 2009. In most cases, unfunded liabilities will have grown because of communities' failure to begin to address the problem.

¹ Two of the top 50 communities, Fall River and Woburn, do not have any OPEB data available despite the requirement to do so. As discussed later, this liability is almost totally unfunded.

² Since OPEB is almost entirely retiree health care, we use the two terms interchangeably.

Table 1
Municipal OPEB and Pension Liabilities (in thousands)

Pop. Rank	Municipality	Unfunded Pension Liability		OPEB + Pension Total	
		OPEB Liability	Unfunded	Total	Unfunded Liability
1	Boston	4,553,816	2,920,165	7,212,669	7,473,981
2	Worcester*	765,312	297,675	929,569	1,062,987
3	Springfield	761,576	402,504	699,026	1,164,080
4	Cambridge	598,995	67,004	833,034	665,999
5	Lowell	432,752	150,668	413,775	583,419
6	Brockton	635,224	32,623	410,270	667,847
7	New Bedford	478,609	319,667	516,133	798,276
8	Quincy	435,548	165,187	472,269	600,735
9	Fall River	N/A	N/A	N/A	N/A
10	Lynn	450,682	214,078	412,239	664,760
11	Newton	531,675	137,886	419,001	669,561
12	Somerville	570,929	96,631	280,400	667,559
13	Lawrence	323,977	146,233	285,982	470,210
14	Framingham	389,843	64,895	262,770	454,738
15	Haverhill	299,042	138,230	282,522	437,272
16	Waltham	517,000	89,420	251,354	606,420
17	Plymouth	264,991	54,787	175,119	319,778
18	Brookline	323,000	108,623	332,222	431,623
19	Malden	164,766	57,893	216,498	222,659
20	Chicopee	165,267	94,628	247,050	259,895
21	Taunton	335,113	89,769	281,787	424,883
22	Medford	247,639	66,794	216,374	314,433
23	Weymouth	131,756	53,587	190,920	185,343
24	Peabody	419,806	78,341	197,189	498,146
25	Revere	160,287	66,438	163,452	226,725
26	Barnstable	159,322	54,693	**	214,015
27	Methuen	209,816	67,016	154,332	276,833
28	Attleboro	274,301	29,194	118,944	303,495
29	Pittsfield	224,749	105,976	186,547	330,725
30	Leominster	154,772	19,511	118,516	174,283
31	Fitchburg	177,764	75,856	167,874	253,620
32	Westfield	178,430	70,609	193,420	249,039
33	Arlington	139,440	47,385	192,195	186,825
34	Salem	159,946	79,394	179,382	239,339
35	Holyoke	300,166	90,362	265,688	390,528
36	Billerica	233,836	73,500	**	307,336
37	Beverly	209,173	56,430	143,368	265,603
38	Woburn	N/A	N/A	N/A	N/A
39	Marlborough	111,574	56,153	151,387	167,727
40	Everett	137,107	99,111	156,991	236,218
41	Chelsea	184,806	68,366	130,398	253,172
42	Amherst	68,990	**	**	N/A
43	Braintree	158,006	47,920	189,266	205,926
44	Dartmouth	59,273	36,744	**	96,017
45	Chelmsford	162,400	52,175	**	214,575
46	Shrewsbury	85,122	19,592	85,257	104,714
47	Andover	245,108	36,946	136,899	282,054
48	Watertown	118,381	43,511	140,549	161,892
49	Falmouth	108,886	40,786	125,751	149,672
50	Natick	111,744	40,383	131,268	152,127
	Total	17,930,716	7,225,337	18,669,656	25,087,064

* Worcester also has approximately \$168 million in outstanding pension obligation bonds.

** The Foundation does not have complete data for the communities in regional pension plans.

Just how big is this burden? For these 50 communities, the unfunded liability is two-and-a-half times larger than the total unfunded pension liability. Every community has a larger unfunded OPEB liability than unfunded pension liability. In Peabody, for example, the unfunded OPEB liability is more than five times larger than its unfunded pension liability.

This trend is particularly troubling among communities that are already suffering from large unfunded pension obligations. Lynn, Chelsea, and Pittsfield all have pension systems that are less than 50 percent funded and have unfunded OPEB liabilities that are more than twice as much as their unfunded pension liabilities. In more than half of the 50 communities, excluding those in regional pension plans, the *total* OPEB liability is greater than the *total* pension liability. Attleboro, Peabody, Waltham, and Somerville each has a total OPEB liability that is more than double its total pension liability.

With pension obligations already weighing down municipal budgets, communities cannot realistically expect to satisfy both their retiree health care and pension liabilities. If municipalities continue business as usual with retiree health care, many can expect to be paying more to provide a year of retiree health benefits than the average retiree receives in pension benefits. Once a supplemental benefit, retiree health care is becoming the most costly aspect of retirement compensation.

As breathtaking as these liabilities are, they almost certainly are understated because most of the communities have used artificially low assumptions about the growth of health care costs in liability calculations. All but five of the 50 municipalities assume that health cost

growth will drop to five percent annually, most commonly within five years, which seems highly unlikely. As shown in Table 2 and Appendix B, this does not reflect actual experiences over the last decade.

Table 2
Cost Growth Assumptions versus Actual Health Insurance Expenditures³
Select Communities

Municipality	Assumed Long-Term Growth (%)	Average Annual Growth Since 2001 (%)
Methuen	5.0	12.7
Brookline	5.0	11.6
Framingham	5.0	11.1
Medford	5.0	10.1
Marlborough	5.0	9.8
Everett	5.0	8.2

Annual Obligations

The annual costs to tackle OPEB liabilities are daunting. To pay for this \$20 billion liability over the next 30 years would require an annual contribution (ARC) of at least \$1.2 billion for just these 50 cities and towns, compared to the \$500 million they currently spend on a pay-as-you-go basis.⁴

The \$1.2 billion ARC includes two parts: an amortization payment and the “normal cost” payment. The amortization payment, which increases each year, is the annual cost to reduce the existing unfunded liability over a period of time, in this case 30 years. Since the future costs for current retirees are incorporated into the unfunded liability, the amortization payment includes those expenses. The normal cost is the amount a municipality must set aside to fund all of the

³ As reported to the Massachusetts Department of Revenue.

⁴ Excludes Fall River and Woburn.

OPEB obligations payable in the future that were incurred for active employees during that year.

Municipalities have two ways to fund liabilities: pay-as-you-go or paying the ARC. All 50 communities currently fund OPEB on a pay-as-you-go basis and calculate the ARC mainly to comply with GASB 45. However, every year that a community does not meet its ARC, it defers that obligation to the future and increases its unfunded liability. With current pay-as-you-go funding at \$500 million and the ARC at \$1.2 billion, these 50 communities face two paths that both lead to the same disastrous result.

By deferring \$700 million in contributions each year, municipalities lose the income they would have earned on that money, which adds to their obligation. That lost interest compounds every year they continue to defer payment and builds dramatically over time.

Based on a four percent rate of return, these municipalities lose \$28 million of interest earnings by not paying the \$700 million for one year.⁵ By deferring the \$700 million each year for five years, the municipalities would sacrifice more than \$400 million in interest income. Skipping the \$700 million payment each year for 30 years would lead to an astonishing \$19.8 billion in lost interest income (Appendix C).

Of the 50 communities, only Arlington has designated a special OPEB trust, which holds \$2.9 million or about two percent of the town's total liability. A handful of other communities have made small contributions to special funds for OPEB, but those contributions were not placed into

⁵ The median assumed rate of return in actuarial valuations for the top 50 communities is four percent.

irrevocable trusts at the time of their most recent valuations.⁶ With such an enormous and growing gap between current payments and the ARC, these communities have no way to meet the ARC now or in the future.

On the other hand, if municipalities continue pay-as-you-go funding, the liabilities do not disappear and paying for annual costs will become more and more unmanageable. Health care costs will continue to grow and consume an ever larger share of limited revenues. While municipalities operate under the illusion that pay-as-you-go adequately meets their obligations, they are digging deeper and deeper holes that taxpayers must fill in the future.

Whether communities choose the path of pre-funding or pay-as-you-go, retiree health care costs are simply unaffordable. Employee benefits have already eroded local budgets and forced cuts to basic services—and municipalities have not even begun to fund OPEB liabilities. This hemorrhaging will intensify as the soaring costs of retiree health care and other employee benefits force more severe cuts than municipalities have already implemented.

The Legislature and municipalities face a clear and critical choice: cut back retiree health care benefits to an affordable and sustainable level or see cities and towns sink farther and farther into debt while decimating local services.

⁶ GASB requires that contributions be irrevocable and placed in a specially designated trust that is protected from creditors. Since these communities did not establish irrevocable trusts—and therefore funds could be tapped for other purposes at any time—these assets are not counted in actuarial valuations. Boston and Brookline established irrevocable trusts after their most recent valuations.

Table 3
Increase in Average Single Family Tax Bills to Meet OPEB Obligations
Communities with increases over 50 percent

City/Town	Average Single Family Tax Bill (FY10)	Increase Needed, per Single Family Parcel	Tax Bill Increase	Total 30-yr Payment, Average Single Family Homeowner
Lawrence	2,374	6,053	255%	181,604
Boston	2,762*	3,261	118%	97,827
Holyoke	2,764	2,433	88%	72,989
Attleboro	3,153	2,614	83%	78,434
Brockton	2,713	1,858	68%	55,740
Worcester	3,129	2,049	65%	61,478
Lowell	3,072	1,971	64%	59,118
Taunton	2,612	1,571	60%	47,135
Revere	3,347	1,964	59%	58,933
New Bedford	2,838	1,577	56%	47,308

*Boston's average family tax bill is for FY 2009 and includes the residential exemption.

Overwhelming Burden on Taxpayers

Another way of understanding these massive liabilities is to measure the potential impact on taxpayers, and the burden would be overwhelming.⁷

As shown in Table 3 and Appendix D, 10 communities would need to increase the average single family tax bill by more than 50 percent and maintain that increase for 30 years to pay for the full ARC. Lawrence homeowners would see an astonishing 255 percent increase and Boston a 118 percent increase in their bills.

In 29 of the 40 communities, tax bills would need to jump by 20 percent or more to pay the ARC. Even at the lowest end, Falmouth

homeowners would see an 8 percent increase in property taxes.

Over 30 years, the average single family homeowner in Boston would pay nearly \$100,000 in *additional* taxes to meet the city's annual OPEB obligations. In eight other communities—Worcester, Lowell, Brockton, Newton, Lawrence, Revere, Attleboro, and Holyoke—the average homeowner would pay more than \$50,000 in additional taxes over 30 years.⁸

It is absolutely inconceivable that taxpayers would, or should, be asked to pay such extraordinary and unaffordable amounts—yet that is the obligation on the backs of taxpayers if the benefits are not changed.

⁷ The Foundation used the Department of Revenue's data on residential parcels and tax bills to analyze the implications of paying the full ARC for taxpayers in 40 of the 50 communities. Residential tax bill data was not available for Barnstable, Brookline, Chelsea, Everett, Malden, Marlborough, Somerville, and Watertown, in addition to Fall River and Woburn.

⁸ Municipalities increase the amortization portion of their ARC each year (usually by 4.5 percent), but the Foundation assumed the entire ARC remained level for 30 years because several communities do not provide details of the amortization portion. As a result, the total 30-year payments may be low estimates for some communities.

A Disappearing Benefit

Massachusetts municipalities already stand apart from the great majority of employers by offering retiree health care at all, but the richness of benefits—extraordinary plans, substantial employer contributions, and low eligibility barriers—places them among the most generous employers in the nation.

In the private sector, retiree health care is rapidly becoming a thing of the past. Only 28 percent of private sector employers with at least 500 employees offered health care benefits to early retirees in 2009, down from 46 percent in 1993, while just 21 percent of these employers provided supplemental health care coverage for Medicare-eligible retirees compared to 40 percent in 1993.⁹ These percentages include employers that require retirees to pay the full premium cost, so an even smaller fraction actually contribute anything to the cost of premiums.¹⁰

In Massachusetts, employer-provided retiree health care is also a rarity. According to the state's 2009 survey, only 9.6 percent of all employers offered early retiree health care. Slightly more—12 percent of all employers—provided supplemental coverage to Medicare-eligible retirees. A survey by Associated Industries of Massachusetts (AIM) found similar results: in 2010, only eight percent of employers offered retiree health care coverage. These

numbers also include employers that do not contribute anything to the cost of premiums.

Even in the public sector, retiree health care is more the exception than the rule. According to a national survey by Cobalt Community Research, just 28 percent of local governments provided retiree health care in 2010.¹¹ The Department of Health and Human Services found similar results in a 2009 national survey—36.4 percent of state and local governments offered health care to early retirees and 25.4 percent offered supplemental health care to retirees 65 and older. As with the private sector data, these numbers include governments that do not contribute anything to the cost of premiums.

The 100 largest government entities in Oregon have a total OPEB liability of only \$3 billion. That includes Oregon state government, which reduced its already modest retiree health care subsidy for new hires in 2003. Among local governments in the U.S., Boston has the fourth largest unfunded OPEB liability, behind only New York City, Los Angeles County, and Detroit.¹²

Several factors explain the extraordinarily large municipal liabilities in Massachusetts. The state's cities and towns offer exceedingly generous health benefits, including such relics as \$5 co-pays and no deductibles. Many municipal retirees are not required to enroll in Medicare, leaving municipalities to pay for the more expensive non-Medicare plans. Finally, the eligibility

⁹ Frontstin, Paul. "Issue Brief: Implications of Health Reform for Retiree Health Benefits." Employee Benefit Research Institute (EBRI), January 2010.

¹⁰ Employers who provide only access to employer health care, and make no contribution, still have a liability if retirees are included in the same health plan(s) as active employees. Using a single rate for both retirees and actives results in retiree premiums lower than they would otherwise be in a retiree-only plan, and active employee premiums are slightly higher than if retirees were excluded. This is known as the implicit rate subsidy.

¹¹ "Health & OPEB Funding Strategies, 2010 National Survey of Local Governments." Cobalt Community Research.

¹² U. S. Government Accountability Office. "State and Local Retiree Health Benefits: Liabilities are Largely Unfunded but Some Governments are Taking Action." November 2009.

requirements for retiree health care have few restrictions.

As a rule, municipal health plans in Massachusetts are significantly richer than plans offered by other employers, including the state and federal governments.¹³ While these other employers have responded to the reality of escalating health care costs, municipalities have lagged in adjusting plan benefits because all changes are subject to collective bargaining. Retirees are included in these same expensive plans with the same generous benefits. And, unlike other public and private entities, Massachusetts municipalities have no dollar cap on their contribution for retiree health care.

Adding to the problem, thousands of Medicare-eligible retirees are not enrolled in Medicare, even though the municipality and employee have already paid for it.

Municipalities also have eligibility requirements that are remarkably expansive. Between current retirees and active employees already eligible for benefits, these 50 municipalities must provide lifetime health care to 150,000 people.

- After only 10 years of service, employees are entitled to lifetime health care benefits upon retirement. By contrast, the pension system tailors benefits to years of service so an individual who works for 30 years receives a much greater benefit than one with 10 years of service.
- Retirees are eligible for health care benefits as early as age 55, 10 years before they qualify for Medicare.

- The state mandates that municipal employees must work only 20 hours per week to be eligible for the same benefits as full-time employees. Such part-time employees also need to have only 10 years of service to receive retiree benefits, so a part-time employee must work the equivalent of only five years of full-time service to obtain lifetime retiree health care benefits.
- State law requires that retiree health benefits include spouse and dependent coverage which costs more than twice as much as individual coverage. At local option, spouses retain lifetime coverage upon the death of a retiree.

¹³ The Foundation will be releasing a study which compares the benefits offered by a sample of municipal plans with other public and private sector plans.

Recommendations

It is urgent that municipalities and the Legislature take steps to rein in these huge and growing liabilities. Delay will only require more difficult and sweeping action later.

There is a serious question whether many communities can afford to continue to provide any sort of retiree health care, particularly in combination with their pension obligations and the escalating costs of employee health care. At a minimum, the extraordinarily generous retiree benefits must be scaled back, and the sooner communities act the more likely they will be able to preserve some form of those benefits.

Unfortunately, communities have limited flexibility to address this problem since so many of the benefits are mandated by state law. Nevertheless, cities and towns have some opportunities to make changes on their own, which they should seize.

This report makes a series of recommendations to address this problem, divided into those that require legislative action and those that municipalities can implement under current law.

Because of the severity of the problem, the changes in benefits need to apply to current employees, and in some cases to current retirees, rather than only for new hires, as in the case of pension changes.¹⁴ It is important to emphasize that even if all the recommendations were adopted, municipalities would still be providing their retirees with far more generous health benefits than all but a tiny fraction of Massachusetts employers.

¹⁴ Retiree health care benefits do not have the same legal protections as pensions.

Legislative Recommendations

Provide Local Officials the Authority to Adjust Plan Design

One of the most important steps to control the costs of municipal health care for both employees and retirees is to give local officials the authority to change plan design outside of collective bargaining. Unlike the state and private sector employers, municipal officials' hands are tied by having to go through collective bargaining to make even minor plan changes. The result is overly rich plans, and since retirees are enrolled in the same health plans as active employees, this also drives up OPEB liabilities. Making modest changes, but still keeping benefits at least on par with the state's Group Insurance Commission, would have the dual impact of immediate and large savings in operating budgets while taking a significant bite out of OPEB liabilities.

Contribute Set Dollar Amounts and Cap Municipal Contributions

A key strategy for communities to control their OPEB liabilities, which would require legislative action, would be to contribute a set dollar amount toward premiums and to place a cap on their contributions. Municipalities currently tie their contributions to a percentage of a plan's cost with a minimum 50 percent required by state law. The dollar approach would reduce liabilities by helping to protect the municipality from the relentless growth in health care costs and encourage retirees to choose less expensive health care plans. For example, Gainesville, Florida switched from percentage to dollar contributions in 2009 and reduced its liability by 12 percent.¹⁵

¹⁵ U. S. Government Accountability Office. "State and Local Retiree Health Benefits: Liabilities are Largely Unfunded but Some Governments are Taking Action." November 2009.

Massachusetts municipalities are not permitted to cap their benefits, but contribution limits are prevalent in both the private and public sectors. For example, a local Fortune 100 company—one of the few private employers still providing retiree health care—caps its contribution at 100 percent of 2005 costs. Colorado caps its monthly contributions for early and Medicare-eligible retirees at \$230 and \$115 respectively, and Florida offers a maximum health insurance subsidy of \$150 per month to state employees.

Require Medicare Enrollment

Current state law requires that all state retirees enroll in Medicare as their primary coverage. However, there is no such requirement for municipalities—only a local option. The additional costs of covering Medicare-eligible retirees in non-Medicare plans adds substantially to OPEB liabilities. For example, if just one-third of the Medicare-eligible retirees in Newton who are currently not enrolled in Medicare made the switch, the city’s liability would drop by almost \$15 million. If all 150 made the switch, the liability would drop by about \$45 million, or 8.5 percent.

The majority of communities have imposed the Medicare requirement, and in those that do not have a formal requirement many retirees have chosen Medicare as their primary coverage. Nevertheless, there are thousands of retirees statewide who are not enrolled despite the fact that both the municipality and the employee have paid into the Medicare system. As recently proposed by the Governor, the state should mandate that all Medicare-eligible municipal retirees enroll in Medicare.

Tie Benefits to Years of Service

Instead of allowing all retirees to be eligible for full retiree health care after just 10 years

of service, the Foundation recommends the Legislature make retiree health care benefits commensurate with length of service, as the pension system already does.

There are a number of ways this could be accomplished. Under one option, employees would receive the municipality’s maximum subsidy at 35 years of service, with the contribution reduced proportionately for shorter tenures. For example, if a municipality’s maximum retiree health care contribution is 75 percent of the premium, contributions could be scaled downward as follows:

Years of Service	Percent of Full Municipal Contribution	Municipal Contribution, Based on a 75% Maximum
35 or more	100%	75%
30 to <35	85%	63.75%
25 to <30	70%	52.5%
20 to <25	55%	41.25%
15 to <20	40%	30%
10 to <15	25%	18.75%

A slightly more complicated version would tie the scale to the pension benefit, which includes age as a factor. Only employees receiving the maximum pension benefit of 80 percent of final average salary would receive the maximum premium contribution. Alternatively, municipalities could contribute a flat dollar amount per year of service towards monthly health care premiums for eligible retirees.

Raise the Retiree Health Care Eligibility Age

The Foundation recommends the Legislature increase the retiree health care eligibility age from 55 to 62. This substantially shortens the time frame for which a municipality would have to pay pre-Medicare premiums

and be responsible for the overlapping health care costs of both the retiree and the retiree's replacement. Increasing the eligibility age may also encourage some employees to defer retirement, allowing the community to benefit longer from their knowledge and years of experience.¹⁶

Several state governments have raised the eligibility age for retiree health benefits. In 2008, Rhode Island raised eligibility to 59. New York state raised the minimum retirement age—which dictates the retiree health care eligibility age—from 55 to 62 for new hires.

Increase Eligibility Hours and Prorate Benefits for Part-Time Employees

Under state law employees must work only 20 hours per week to be eligible for retiree health care. Thus, an employee who works 20 hours per week for 10 years is entitled to the same retiree health benefit as an employee who works 40 hours per week for 35 years.

The Foundation recommends that the Legislature raise the eligibility for retiree health benefits to 1,400 hours or approximately 27 hours per week for part-time employees. In addition, the benefit should be tied to the number of hours an employee works. For example, an employee working three-fourths of a full-time schedule would be entitled to 75 percent of the benefits of a full-time employee with the same years of service.

End Spousal/Dependent Coverage

Providing spousal/dependent coverage to retirees is an expensive obligation imposed on municipalities and is unusually generous

even among the dwindling ranks of employers still offering retiree health care. The Foundation recommends that the Legislature eliminate the requirement that municipalities offer spousal/dependent coverage to all future retirees who are eligible for health benefits.

Costs for spousal/dependent coverage are at least twice as much as individual coverage. For example, in Somerville's least expensive plan, the city pays \$17,610, or over \$11,000 more, for an early retiree who elects family coverage instead of individual coverage. For supplemental Medicare plans, the city pays twice as much for retiree-plus-spouse coverage as it does for retiree-only coverage.

Municipal Recommendations

Decrease the Municipal Share of the Premium Contribution

State law requires municipalities to contribute a minimum of 50 percent toward retiree health care premiums, and in the 50 communities the average municipal contribution is 75 percent.

Municipalities currently contributing more than 50 percent can reduce their contributions without needing a legislative change. It is an open question whether municipalities must bargain changes in premium contributions or plan design for retirees. Recognizing that such a change could be disruptive for some retirees, municipalities could phase down their contribution over time.

Require Medicare Enrollment

As discussed earlier, municipal retirees are not required to enroll in Medicare. Communities do have the option to adopt this policy on their own, and the Foundation

¹⁶ Governor Patrick has proposed increasing the pension eligibility age, but that does not automatically affect the retiree health care eligibility age.

recommends that municipalities exercise that option if they have not yet done so.

Other Recommendations

Detail Costs in Annual Budgets

One of the key reasons GASB 45 was implemented was to force municipalities to measure and recognize the liabilities they incur every year, rather than simply pushing the obligation onto future taxpayers outside of the public limelight.

In the annual budget, municipalities should publish that year's total normal cost, which is the amount the municipality should set aside to pre-fund the retiree health benefits that active employees earned that year. This will help municipalities determine their total spending on employee compensation and benefits. Municipalities should also track spending on retiree health care by making it a separate line item in the annual operating budget.

Centralize Reporting

GASB requires that all OPEB plans with at least 200 members conduct biennial valuations, but many municipalities in Massachusetts have not met this standard. In addition, as the Foundation discovered, most municipalities do not make this data readily available. With such limited transparency and lack of enforcement, municipalities have little incentive to update their valuation if it would increase their liabilities.

The Foundation recommends the state implement and enforce reporting standards for municipalities. As Governor Patrick recently proposed, municipalities should be required to report on key data points—the liability, annual required payment, pay-as-you-go costs, and assumed rate of return—annually to the state. This would allow taxpayers and other interested parties to view their community's liability, compare it to other communities, and encourage municipalities to address their large liabilities.

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Abbreviations Used in Tables

AAL: Actuarial Accrued Liability
ARC: Annual Required Contribution
AVA: Actuarial Value of Assets
FY: Fiscal Year
Paygo: Pay-as-you-go
UAAL: Unfunded Actuarial Accrued Liability

**Appendix A
OPEB Liability by Municipality**

Pop. Rank	Municipality	Retired Members	Active Members	AVA (1,000s)	UAAL (1,000s)	AAL (1,000s)	Assumed Rate of Return	ARC (1,000s)	Paygo Cost (1,000s)	Paygo as a % of ARC	Paygo FY	Date of Valuation
1	Boston	14,000	15,000	0	4,553,816	4,553,816	5.3%	252,685	153,433	61	2010	6/30/09
2	Worcester	5,285	4,348	0	765,312	765,312	4.0%	70,142	19,507	28	2009	6/30/08
3	Springfield	4,917	4,179	0	761,576	761,576	3.5%	43,555	25,004	57	2009	6/30/08
4	Cambridge	2,168	2,786	0	598,995	598,995	4.5%	39,272	18,558	47	2009	1/1/09
5	Lowell	1,959	3,029	0	432,752	432,752	3.5%	31,917	8,738	27	2009	1/1/08
6	Brockton	2,577	3,064	0	635,224	635,224	4.0%	46,244	15,808	34	2009	6/30/09
7	New Bedford	N/A	N/A	0	478,609	478,609	3.5%	31,933	12,537	39	2009	7/1/07
8	Quincy	1,928	2,307	0	435,548	435,548	3.5%	31,433	10,967	35	2009	7/1/07
9	Fall River	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
10	Lynn	2,020	2,225	0	450,682	450,682	8.0%	28,993	11,005	38	2009	6/30/08
11	Newton	2,500	2,453	0	531,675	531,675	2.0%	47,573	14,141	30	2009	6/30/10
12	Somerville	1,880	1,497	0	570,929	570,929	3.5%	34,353	15,038	44	2009	6/30/08
13	Lawrence	401	665	0	323,977	323,977	4.0%	33,661	7,843	23	2009	1/1/09
14	Framingham	1,538	1,895	0	389,843	389,843	4.0%	26,539	12,181	46	2009	7/1/08
15	Haverhill	1,838	1,160	0	299,042	299,042	5.0%	16,613	11,227	68	2009	1/1/09
16	Waltham	1,193	1,254	0	517,000	517,000	4.0%	30,129	17,869	59	2009	7/1/06
17	Plymouth	1,177	1,184	0	264,991	264,991	4.5%	21,182	11,975	57	2009	7/1/06
18	Brookline	1,523	1,444	0	323,000	323,000	5.3%	20,503	9,532	46	2009	6/30/08
19	Malden	1,132	1,135	0	164,766	164,766	5.0%	16,137	5,309	33	2008	6/30/08
20	Chicopee	1,289	1,182	0	165,267	165,267	5.0%	11,481	6,613	58	2009	12/31/06
21	Taunton	1,421	1,717	0	335,113	335,113	3.5%	22,258	6,150	28	2009	6/30/08
22	Medford	900	933	0	247,639	247,639	3.5%	14,018	6,215	44	2009	6/30/08
23	Weymouth	1,385	1,267	0	131,756	131,756	8.0%	11,020	0	0	2009	1/1/07
24	Peabody	1,649	1,296	0	419,806	419,806	3.5%	26,183	9,926	38	2008	7/1/06
25	Revere	951	1,048	0	160,287	160,287	N/A	15,636	6,912	44	2009	7/1/07

	Municipality	Retired Members	Active Members	AVA (1,000s)	UAAL (1,000s)	AAL (1,000s)	Assumed Rate of Return	ARC (1,000s)	Paygo Cost (1,000s)	Paygo as a % of ARC	Paygo FY	Date of Valuation
26	Barnstable	723	915	0	159,322	159,322	5.0%	11,202	5,060	45	2009	6/30/08
27	Methuen	763	794	0	209,816	209,816	4.5%	14,340	4,494	31	2009	6/30/08
28	Attleboro	N/A	N/A	0	274,301	274,301	4.3%	24,309	0	0	2009	6/30/09
29	Pittsfield	1,250	1,500	0	224,749	224,749	N/A	17,719	7,549	43	2009	1/1/07
30	Leominster	859	1,107	0	154,772	154,772	4.5%	13,454	4,968	37	2009	1/1/08
31	Fitchburg	939	1,090	0	177,764	177,764	4.3%	13,159	5,444	41	2009	1/1/09
32	Westfield	482	1,201	0	178,430	178,430	3.8%	20,440	5,197	25	2009	6/30/08
33	Arlington	941	1,049	2,909	139,440	142,349	5.3%	12,729	8,762	69	2009	1/1/08
34	Salem	928	919	0	159,946	159,946	5.0%	11,129	6,799	61	2009	12/31/07
35	Holyoke	1,450	1,433	0	300,166	300,166	4.0%	19,471	6,564	34	2008	6/30/07
36	BillERICA	917	825	0	233,836	233,836	4.3%	17,020	6,970	41	2009	1/1/09
37	Beverly	725	715	0	209,173	209,173	4.0%	12,936	6,028	47	2009	6/30/09
38	Woburn	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
39	Marlborough	709	1,161	0	111,574	111,574	3.5%	8,796	2,344	27	2009	7/1/08
40	Everett	669	1,337	0	137,107	137,107	4.0%	12,574	5,183	41	2009	1/1/07
41	Chelsea	399	968	0	184,806	184,806	4.0%	20,010	1,861	9	2008	6/30/08
42	Amherst	217	457	0	68,990	68,990	4.3%	6,025	2,140	36	2009	7/1/07
43	Braintree	858	1,066	0	158,006	158,006	4.9%	14,500	5,498	38	2009	1/1/07
44	Dartmouth	N/A	N/A	0	59,273	59,273	4.0%	6,240	1,647	26	2009	7/1/08
45	Chelmsford	952	800	0	162,400	162,400	4.3%	14,043	5,040	36	2010	1/1/09
46	Shrewsbury	N/A	N/A	0	85,122	85,122	3.5%	6,700	1,504	22	2009	7/1/09
47	Andover	485	747	0	245,108	245,108	3.5%	18,051	5,363	30	2009	6/30/09
48	Watertown	N/A	N/A	0	118,381	118,381	3.5%	N/A	N/A	N/A	N/A	N/A
49	Falmouth	590	744	0	108,886	108,886	5.0%	7,776	3,232	42	2009	7/1/08
50	Natick	788	1,179	0	111,744	111,744	4.0%	10,908	2,997	27	2009	7/1/08
	Total	71,275	77,075	2,909	17,930,716	17,933,625	--	1,236,993	521,131	--	--	--

Appendix B
Health Care Cost Growth Assumptions by Municipality¹

Pop. Rank	Municipality	Date of Valuation	Health Care Growth Rate Assumptions				Actual Growth Annual Average 2001-2009 (%)
			Initial Growth (%)	Long-Term Growth (%)	Phase Down Period (years)	First Year Long-Term Growth Applies	
1	Boston	6/30/09	10 to 11	5 to 6	5	2014	9.4
2	Worcester*	6/30/08	10	5	7	2015	11.0*
3	Springfield	6/30/08	9	5	8	2016	8.8
4	Cambridge	1/1/09	11	5	13	2022	8.5
5	Lowell	1/1/08	10	5	5	2013	12.9
6	Brockton	6/30/09	7.5	5	5	2014	10.2
7	New Bedford	7/1/07	N/A	N/A	N/A	N/A	31.7
8	Quincy	7/1/07	8.5	5	6	2013	9.6
9	Fall River	N/A	N/A	N/A	N/A	N/A	9.4
10	Lynn	6/30/08	8	5	10	2018	14.2
11	Newton	6/30/10	6.9 to 7.2	5.2	3	2013	12.4
12	Somerville	6/30/08	9	5	8	2016	11.8
13	Lawrence	1/1/09	10	5	5	2014	11.2
14	Framingham	7/1/08	7	5	5	2013	11.1
15	Haverhill	1/1/09	9	5	5	2014	8.6
16	Waltham	7/1/06	9	5	8	2014	9.9
17	Plymouth	7/1/06	11	6	by 2040	2040	10.9
18	Brookline	6/30/08	10	5	5	2013	11.6
19	Malden	6/30/08	12	5	5	2013	12.8
20	Chicopee	12/31/06	N/A	N/A	N/A	N/A	8.4
21	Taunton	6/30/08	9	5	8	2016	7.5
22	Medford	6/30/08	7.5	5	10	2018	10.1
23	Weymouth	1/1/07	N/A	N/A	N/A	N/A	6.3
24	Peabody	7/1/06	10	5	10	2016	8.7
25	Revere	7/1/07	N/A	N/A	N/A	N/A	18.0
26	Barnstable**	6/30/08	10	5	7	2015	61.5
27	Methuen	6/30/08	10	5	10	2018	12.7
28	Attleboro	6/30/09	N/A	N/A	N/A	N/A	10.8
29	Pittsfield	1/1/07	N/A	N/A	N/A	N/A	10.6
30	Leominster	1/1/08	11	6	10	2018	19.8
31	Fitchburg	1/1/09	9 to 11	5 to 6	10	2019	14.6
32	Westfield	6/30/08	7.2	6.2	by 2040	2040	10.3

¹ Actual annual growth as reported to the state's Department of Revenue.

* The actual growth for Worcester is from 2002, instead of 2001, to 2009.

** Barnstable and Amherst numbers likely reflect a change in reporting between 2002 and 2009.

Pop. Rank	Municipality	Date of Valuation	Health Care Growth Rate Assumptions				Actual Growth Annual Average 2001-2009 (%)
			Initial Growth (%)	Long-Term Growth (%)	Phase Down Period (years)	First Year Long-Term Growth Applies	
33	Arlington	1/1/08	8	5	N/A	N/A	15.3
34	Salem	12/31/07	10	5	5	2012	8.6
35	Holyoke	6/30/07	4.5	4.5	N/A	N/A	6.8
36	Billerica	1/1/09	11	5	10	2019	11.5
37	Beverly	6/30/09	10	5	10	2019	20.2
38	Woburn	N/A	N/A	N/A	N/A	N/A	10.8
39	Marlborough	7/1/08	9	5	8	2016	9.8
40	Everett	1/1/07	6.98	5	10	2017	8.5
41	Chelsea	6/30/08	9	5	5	2013	3.2
42	Amherst**	7/1/07	10	5	5	2012	44.5
43	Braintree	1/1/07	11.83	5	10	2017	11.2
44	Dartmouth	7/1/08	10	5	N/A	N/A	4.0
45	Chelmsford	1/1/09	Blended, <10	5	10	2019	7.1
46	Shrewsbury	7/1/09	8.5	5	7	2016	8.7
47	Andover	6/30/09	8.5	5	8	2017	13.7
48	Watertown	N/A	N/A	N/A	N/A	N/A	12.0
49	Falmouth	7/1/08	9	5	7	2015	14.1
50	Natick	7/1/08	10	5	5	2013	10.8

** Barnstable and Amherst numbers likely reflect a change in reporting between 2002 and 2009.

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Appendix C
Impact of Underfunding the Annual Required Contribution
Based on 4.0 percent annual rate of return

FY	Amount Underfunded (1,000s)	Foregone Interest (1,000s)	Cumulative Foregone Interest (1,000s)	Total Underfunding (1,000s)
2010	700,000	28,000	28,000	728,000
2011	700,000	57,120	85,120	1,485,120
2012	700,000	87,405	172,525	2,272,525
2013	700,000	118,901	291,426	3,091,426
2014	700,000	151,657	443,083	3,943,083
2015	700,000	185,723	628,806	4,828,806
2016	700,000	221,152	849,958	5,749,958
2017	700,000	257,998	1,107,957	6,707,957
2018	700,000	296,318	1,404,275	7,704,275
2019	700,000	336,171	1,740,446	8,740,446
2020	700,000	377,618	2,118,064	9,818,064
2021	700,000	420,723	2,538,786	10,938,786
2022	700,000	465,551	3,004,338	12,104,338
2023	700,000	512,174	3,516,511	13,316,511
2024	700,000	560,660	4,077,172	14,577,172
2025	700,000	611,087	4,688,259	15,888,259
2026	700,000	663,530	5,351,789	17,251,789
2027	700,000	718,072	6,069,861	18,669,861
2028	700,000	774,794	6,844,655	20,144,655
2029	700,000	833,786	7,678,441	21,678,441
2030	700,000	895,138	8,573,579	23,273,579
2031	700,000	958,943	9,532,522	24,932,522
2032	700,000	1,025,301	10,557,823	26,657,823
2033	700,000	1,094,313	11,652,136	28,452,136
2034	700,000	1,166,085	12,818,221	30,318,221
2035	700,000	1,240,729	14,058,950	32,258,950
2036	700,000	1,318,358	15,377,308	34,277,308
2037	700,000	1,399,092	16,776,400	36,376,400
2038	700,000	1,483,056	18,259,456	38,559,456
2039	700,000	1,570,378	19,829,835	40,829,835
Total	21,000,000	19,829,835	19,829,835	40,829,835

Appendix D
Impact on Average Property Tax Bill by Municipality

Pop Rank	Municipality	ARC (1,000s)	Paygo (1,000s)	Difference (1,000s)	Tax Bill Increase, Per Parcel	Total 30-yr Average Payment, Single Family Homeowner	Average Single Family Tax Bill (FY10)	Tax Bill Increase (%)
1	Boston*	252,685	153,433	(99,252)	3,261	97,827	2,762	118
2	Worcester	70,142	19,507	(50,635)	2,049	61,478	3,129	65
3	Springfield	43,555	25,004	(18,551)	714	21,416	2,685	27
4	Cambridge	39,272	18,558	(20,714)	1,027	30,810	3,564	29
5	Lowell	31,917	8,738	(23,178)	1,971	59,118	3,072	64
6	Brockton	46,244	15,808	(30,436)	1,858	55,740	2,713	68
7	New Bedford	31,933	12,537	(19,396)	1,577	47,308	2,838	56
8	Quincy	31,433	10,967	(20,466)	1,501	45,030	4,373	34
10	Lynn	28,993	11,005	(17,988)	1,573	47,200	3,466	45
11	Newton	47,573	14,141	(33,432)	1,975	59,245	8,320	24
13	Lawrence	33,661	7,843	(25,818)	6,053	181,604	2,374	255
14	Framingham	26,539	12,181	(14,358)	1,076	32,282	4,979	22
15	Haverhill	16,613	11,227	(5,386)	529	15,871	3,474	15
16	Waltham	30,129	17,869	(12,260)	762	22,858	3,803	20
17	Plymouth	21,182	11,975	(9,208)	520	15,606	3,902	13
20	Chicopee	11,481	6,613	(4,868)	444	13,329	2,490	18
21	Taunton	22,258	6,150	(16,108)	1,571	47,135	2,612	60
22	Medford	14,018	6,215	(7,803)	995	29,848	3,931	25
23	Weymouth	11,020	0	(11,020)	843	25,288	3,322	25

* Boston's average family tax bill is for FY 2009 and includes the residential exemption.

Pop Rank	Municipality	ARC (1,000s)	Paygo (1,000s)	Difference (1,000s)	Tax Bill Increase, Per Parcel	Total 30-yr Payment, Average Single Family Homeowner	Average Single Family Tax Bill (FY10)	Tax Bill Increase (%)
24	Peabody	26,183	9,926	(16,257)	1,499	44,979	3,273	46
25	Revere	15,636	6,912	(8,724)	1,964	58,933	3,347	59
27	Methuen	14,340	4,494	(9,846)	926	27,793	3,337	28
28	Attleboro	24,309	0	(24,309)	2,614	78,434	3,153	83
29	Pittsfield	17,719	7,549	(10,170)	903	27,084	2,663	34
30	Leominster	13,454	4,968	(8,487)	1,063	31,901	3,296	32
31	Fitchburg	13,159	5,444	(7,715)	1,204	36,108	2,687	45
32	Westfield	20,440	5,197	(15,243)	1,639	49,172	3,478	47
33	Arlington	12,729	8,762	(3,967)	497	14,917	5,779	9
34	Salem	11,129	6,799	(4,330)	901	27,035	4,370	21
35	Holyoke	19,471	6,564	(12,907)	2,433	72,989	2,764	88
36	Billerica	17,020	6,970	(10,050)	937	28,119	4,077	23
37	Beverly	12,936	6,028	(6,908)	826	24,772	5,006	16
42	Amherst	6,025	2,140	(3,885)	954	28,615	5,667	17
43	Braintree	14,500	5,498	(9,003)	1,001	30,026	3,532	28
44	Dartmouth	6,240	1,647	(4,592)	474	14,234	2,966	16
45	Chelmsford	14,043	5,040	(9,003)	1,001	30,018	5,267	19
46	Shrewsbury	6,700	1,504	(5,196)	577	17,298	3,893	15
47	Andover	18,051	5,363	(12,688)	1,496	44,866	7,239	21
49	Falmouth	7,776	3,232	(4,544)	251	7,540	3,326	8
50	Natick	10,908	2,997	(7,912)	935	28,059	5,282	18

Note: Eight communities are excluded because average property tax bill data was not available: Barnstable, Brookline, Chelsea, Everett, Malden, Marlborough, Somerville, and Watertown. Fall River and Woburn are excluded because OPEB data was not available.

Appendix E

Methodology and Tax Calculations

Methodology

The Foundation collected the data on retiree health care liabilities from each community's most recent annual financial statements. As noted in the report, GASB requires that this data—which is found in Appendices A, B, and D—be included in annual financial statements.

Only a handful of the 50 communities had annual financial statements available directly on their websites. For the large majority, we collected the information from Official Statements published when they issue bonds. Many municipalities issue short-term debt on a regular basis to manage cash flow, so they publish an Official Statement—with the most recent financial statements as an appendix—nearly every year. The Municipal Securities Rulemaking Board (MSRB) maintains a comprehensive online database of Official Statements, through which we collected most financial statements.

We were not able to obtain recent financial statements through either their own websites or Official Statements for four communities—Fall River, Woburn, Watertown, and Dartmouth. We called each community and Watertown and Dartmouth provided us with the information we requested.

Clarification of Tax Calculations

The calculations of the percentage increases in property tax bills and the total amount a single family homeowner would pay over 30 years (found in Table 3 and Appendix D) assume that the retiree health care costs would be paid entirely by single family residential homeowners. While some of the burden would of course be borne by commercial and industrial property owners, those additional costs would be passed along to consumers in some fashion. Our calculation of the increase in residential property taxes captures the full effect of these additional obligations on taxpayers and consumers. In either case, the estimates are only illustrative because retiree health care obligations far exceed the capacity of homeowners or businesses to pay for these liabilities.

Acknowledgement

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The Crushing Burden of Municipal Retiree Health Care Liabilities

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The Crushing Burden of Municipal Retiree Health Care Liabilities

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JANUARY 2012

The Crushing Burden of Municipal Retiree Health Care Liabilities

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The Crushing Burden of Municipal Retiree Health Care Liabilities

Overview

The skyrocketing costs of employee benefits—employee health care, pensions, and retiree health care—are forcing cuts in basic services in scores of communities across the state. These costs rose from 13.5 percent of municipal budgets statewide in 2001 to 20 percent in 2010 and, left unchecked, will consume nearly a third of local budgets by 2020.

While the state took two important steps to curb this trend by enacting municipal health care and pension reform legislation in 2011, cities and towns still face billions of dollars in retiree health care liabilities. Since these liabilities are almost totally unfunded, the costs of employee benefits are in fact much larger than the annual budget numbers suggest.

Exceedingly generous retiree health care benefits have saddled municipalities statewide with staggering liabilities—approximately \$20 billion for just the 50 largest municipalities in the state, as described in the Foundation's February 2011 report, *Retiree Health Care: The Brick That Broke Municipalities' Backs*.

This analysis follows up on that report by focusing on the costs of funding retiree health care in 10 geographically dispersed, midsized, industrial Massachusetts cities: Brockton, Fitchburg, Haverhill, Holyoke, Lawrence, Lowell, New Bedford, Pittsfield, Springfield, and Worcester. For years, these cities have struggled to build a strong economic base, but the costs of retiree health care threaten to overwhelm both businesses and homeowners. While this report focuses on these cities, the issues affect virtually every municipality in the Commonwealth.

As shown in Table 1 on page 2, these 10 cities have a combined retiree health care liability of \$4.5 billion, all of it unfunded. Worcester, Springfield, and Brockton have the largest unfunded liabilities, all over \$690 million. Even at the low end, Fitchburg has a huge liability of \$187 million. The liability defines how much these cities would need to set aside today in order to provide these benefits for current retirees and active employees already eligible for benefits, based on a variety of assumptions.¹

The total unfunded retiree health care liability is more than twice the total unfunded pension liability in these 10 cities; in Brockton, the unfunded retiree health care liability is six times the unfunded pension liability. Yet the pension funds in these communities are also grossly underfunded, with half funded at less than 50 percent, and none above 80 percent. Already struggling to pay for their pension obligations, these cities have no hope of meeting their retiree health care obligations.

¹ Each community calculates its own liability and chooses its own assumptions for investment performance and health care cost growth, among others. A higher assumed rate of return and a lower cost growth assumption would reduce the liability. The health plan design, number of people covered, and employees' share of contributions all also affect the liability.

Table 1
Unfunded Retiree Health Care and Pension Liabilities
(thousands of dollars)

Municipality	Retiree Health Care Liability	Unfunded Retiree Health Care Liability	Unfunded Pension Liability
Brockton	\$693,570	\$693,570	\$113,609
Fitchburg	186,634	186,634	93,300
Haverhill	299,042	299,042	138,200
Holyoke	300,166	300,166	130,099
Lawrence	323,977	323,977	187,334
Lowell	432,752	432,752	174,924
New Bedford	478,609	478,609	318,636
Pittsfield	236,149	236,149	110,879
Springfield	761,576	761,576	550,900
Worcester	765,312	765,312	308,183*
Total	\$4,477,786	\$4,477,786	\$2,126,064

**In addition to its unfunded pension liability, Worcester has approximately \$161 million in outstanding pension obligation bonds.*

Retiree health care liabilities are so large because these benefits are almost universally available to municipal employees in Massachusetts, despite having eroded sharply in the private sector. Virtually every community in the state contributes at least 50 percent towards the cost of retiree health care premiums once an employee—including most part-time employees who work at least 20 hours per week—completes just 10 years of service. By comparison, according to a 2010 survey by the state, only 14 percent of all Massachusetts employers offered health care benefits to retirees over age 65, including those employers that do not contribute anything to premiums.

Municipalities have two ways to fund retiree health care costs: pay-as-you-go or making an annual required contribution (ARC).² All 10 cities currently use pay-as-you-go to fund retiree health care, which means they pay only the annual costs of benefits for current retirees and do not fund the benefits that active employees have earned. Relying on pay-as-you-go means that the city falls short of meeting its ARC. Every year that a community does not meet its ARC, it defers that obligation to the future and increases its unfunded liability.

² The annual required contribution, or ARC, includes two parts: an amortization payment and the “normal cost” payment. The amortization payment, which increases each year, is the annual cost to reduce the existing unfunded liability over a period of time, in this case 30 years. Since the future costs for current retirees are incorporated into the unfunded liability, the amortization payment includes those expenses. The normal cost is the amount a municipality must set aside to fund all of the retiree health care obligations payable in the future that were incurred for active employees during that year.

The annual costs to tackle these liabilities are enormous. As shown in Table 2, paying for retiree health care benefits over the next 30 years would require a total annual contribution of at least \$323 million for these 10 cities, compared to the \$131 million they currently spend on a pay-as-you-go basis.

As a result, these communities are underfunding retiree health care benefits by almost \$200 million each year. By deferring more than half of the ARC each year, municipalities lose the interest and investment income they would have earned on that money, which adds to their obligations. That lost interest compounds every year they continue to defer payment and builds dramatically over time; without

change, these cities will increase their obligations by at least \$2 billion in just 10 years.

However, if municipalities continue pay-as-you-go funding, the liabilities do not disappear, and the annual costs will continue to rise. Retiree health care spending increased by 11.6 percent between fiscal 2009 and fiscal 2010 in the eight cities for which that data was available, while revenues were flat. Although municipalities may operate under the illusion that pay-as-you-go adequately meets their obligations, they are digging deeper and deeper holes that taxpayers must fill in the future, either through increased taxes or cuts in basic services.

Table 2
Annual Required Contributions and Pay-As-You-Go Costs of Retiree Health Care
(thousands of dollars)

Municipality	Annual Required Contribution	Pay-As-You-Go Costs	Difference
Brockton	\$57,791	\$20,809	\$36,983
Fitchburg	13,980	5,737	8,243
Haverhill	17,245	12,298	4,947
Holyoke	20,455	7,440	13,015
Lawrence	33,661	8,650	25,011
Lowell	32,946	9,685	23,261
New Bedford	33,457	12,105	21,352
Pittsfield	16,987	9,012	7,975
Springfield	43,555	25,004	18,551
Worcester	52,960	20,598	32,362
Total	\$323,036	\$131,337	\$191,699

Note: Holyoke and Springfield pay-as-you-go costs are for fiscal 2009; all other cities are for fiscal 2010.

The scenario in Brockton over the last two years illustrates the problem faced by these 10 cities, along with scores of other communities across the state. Between fiscal 2008 and fiscal 2010, Brockton's liability rose from \$635.2 million to \$693.6 million—an increase of \$58.4 million or almost 10 percent—and drove its ARC up by \$11.5 million to more than \$57 million. While the city continues to rely on pay-as-you-go funding, those costs rose by almost a third, from \$15.8 million to \$20.8 million, between fiscal 2008 and fiscal 2010. During those two years, the city eliminated 71 total positions, including 10 police officers and recruits. For the fiscal 2011 budget, the city eliminated 57 teachers and dozens of other positions.³

On the other hand, Worcester illustrates how even modest reforms can produce dramatic savings, in this case reducing the city's unfunded retiree health care liability by almost \$400 million, or nearly one-third (see sidebar on page 5). But even with those changes, the city still has an unaffordable retiree health care liability that is twice the size of its unfunded pension liability, underscoring the need for more significant reforms in retiree health care benefits.

Whether municipalities choose to fund their retiree health care costs by making an annual payment or continue their current practice of pay-as-you-go, their liabilities represent the real cost, in today's dollars, of these benefits. To meet such an enormous expense, municipalities face two devastating options: implement draconian property tax increases or eviscerate local services.

As detailed in this report, the property tax increases needed to fund these liabilities are

³ Many teaching positions were restored later in the school year after the school district received non-recurring federal grants.

exorbitant. The sections that follow separate the impact on residential and business property taxpayers.⁴

Not only is it unreasonable to expect property owners to bear enormous property tax increases, the Foundation recognizes that it is exceedingly unrealistic that such increases will actually happen. In all 10 municipalities, voters would have to approve dramatic overrides to pay for benefits that almost none of them receives from their employers. The last operating overrides in any of these 10 cities were approved 20 years ago, in Holyoke and Worcester. In fact, four cities—Haverhill, Lowell, New Bedford, and Pittsfield—have never even taken an operating override vote.

Nevertheless, these are obligations that must be paid, and without property tax increases—or reforming current benefits—the only way to fund these benefits is by dramatically cutting local services. Without reforms, over the next 30 years municipalities would be forced to siphon tens of millions from education, public safety, and other critical services simply to fund the annual costs of retiree health care, leading to the layoffs of hundreds if not thousands of municipal employees.

⁴ The residential calculations also include property classified as open space (only Pittsfield has open space property and it makes up less than 0.5% of the residential levy). Business calculations include commercial, industrial, and personal property classifications. Personal property is largely a tax on businesses and includes property such as machinery, poles, wires, and pipes.

Worcester: Major Savings But Still Unaffordable

The good news in Worcester is that with modest reforms to its health plans, the city was able to shave nearly \$400 million off its unfunded retiree health care liability in fiscal 2010. The bad news is the remaining unfunded balance of \$765 million is still unaffordable.

In recent years, Worcester has adopted a series of changes in health care benefits for retirees under 65. The city also recently began transferring all Medicare-eligible retirees to Medicare, a step that is now required by state law for all municipalities.

Among the most notable changes was the adoption of higher contribution rates for non-Medicare eligible retirees, who now must cover 25 percent of their premiums for standard plans, compared to previous contribution rates between 10 percent and 13 percent for most enrollees. The city also introduced new and higher copayments for medical procedures and office visits for its under-65 retirees, including copays for inpatient and outpatient hospital procedures of \$250 and \$150, respectively.

The changes collectively helped reduce Worcester's long-term retiree health care liability by a third from \$1.15 billion in fiscal 2009 to \$765 million in fiscal 2010. Nonetheless, the city is still failing to keep pace with the liability's rate of growth.

For example, to fund the liability over a 30-year term, Worcester should have set aside \$53 million in fiscal 2010 to fund its retiree liability. The city fell short of that amount by \$32.4 million.

The passage of municipal health reform in 2011 has made it easier for the state's cities and towns to make changes in their health plans. But as the Worcester experience shows, despite the opportunity for significant reductions in liabilities created by municipal health reform, that step alone will not solve the retiree health care challenge. The Legislature must address the problem directly by tightening eligibility standards and giving municipalities the flexibility to curtail costs.

Impact on Residential Taxpayers

Paying for retiree health care liabilities would place a staggering burden on the residential taxpayers of these 10 cities. This section describes two ways to address this enormous burden, one in terms of a single payment today and the other in terms of annual payments over a long period of time, specifically:

- The lump sum cost to the average homeowner today to fund these liabilities.
- The average residential tax increases, or annual payments, needed to fund retiree health care benefits over the next 30 years.

Table 3
Residential Share of Unfunded Retiree Health Care Liability, By Property Type
(thousands of dollars)

Municipality	Unfunded Retiree Health Care Liability (A)	Residential Share of Total Property Tax Levy (B)	Residential Share of Unfunded Liability (C)	Share of Unfunded Liability, Single Family Homes (D)	Share of Unfunded Liability, All Other Residential (E)
Brockton	\$693,570	65%	\$453,448	\$325,044	\$128,404
Fitchburg	186,634	75%	140,052	86,312	53,740
Haverhill	299,042	75%	223,107	137,777	85,330
Holyoke	300,166	50%	151,238	97,048	54,190
Lawrence	323,977	59%	192,682	66,773	125,909
Lowell	432,752	69%	299,648	156,411	143,237
New Bedford	478,609	68%	324,298	174,963	149,336
Pittsfield	236,149	65%	152,846	117,287	35,559
Springfield	761,576	60%	459,663	314,243	145,421
Worcester	765,312	63%	478,381	287,725	190,655
Total	\$4,477,786		\$2,875,364	\$1,763,583	\$1,111,781

Table 3 depicts the share of the total liability that all residential property owners are responsible for in each city, based on their share of the total tax levy. As shown in column C, residential property owners in these 10 cities are responsible for \$2.9 billion of the total unfunded retiree health care liability.

The table further divides the residential liability between property types, namely single family homes (column D) and all other residential properties such as condominiums, apartments, and multifamily dwellings (column E).⁵ Although multifamily homes and condominiums compose a significant share of residential properties—ranging from 23 percent in Pittsfield to 65 percent in Lawrence—this

⁵ The single family and “all other” shares of the residential liability are based on the assessed value of each city’s single family properties as a percentage of total residential property.

section focuses on the impact on single family homeowners because, as column D shows, they bear more than 50 percent of the residential liability in nine of the 10 communities analyzed.

Liability Per Homeowner

As detailed in column C of Table 4 on page 7, the single family homeowner in these 10 cities owes on average an astonishing \$13,685 today to pay for the unfunded retiree health care liability.⁶

In all 10 cities, each single family homeowner is responsible for at least \$10,000 of the retiree health care liability, although the amounts vary considerably by municipality. Brockton’s liability of \$19,826

⁶ The liability per single family homeowner was determined by dividing the single family share of a city’s unfunded retiree liability (column A) by the number of single family properties in a given community (column B).

is the highest in the group, while Fitchburg, Haverhill, Holyoke, Lawrence, Lowell, and New Bedford all top the \$13,000 mark.

The enormity of these liabilities is underscored by the fact that the obligations for single family homeowners range from 23 percent to just under 60 percent of the median household income in these 10 communities, as shown in column E of Table 4.

In Holyoke, where single family homeowners are responsible for almost one-

third of the city's total \$300 million unfunded retiree health care obligation, the \$18,297 liability for each single family home is 59 percent of the city's median household income of \$30,770. The \$15,660 that homeowners in Lawrence are responsible for is more than 50 percent of the median household income. In Brockton and New Bedford, the liability is 41 percent of median household incomes, and in all but one community the liability is equal to at least 25 percent of median household income.

Table 4
Single Family Homeowner Share of Retiree Health Care Liability

Municipality	Share of Unfunded Liability, Single Family Homes (\$1,000s) (A)	Number of Single Family Homes (B)	Liability Per Single Family Home (C)	Median Household Income (D)	Liability As a % of Median Household Income (E)
Brockton	\$325,044	16,395	\$19,826	\$48,823	41%
Fitchburg	86,312	6,446	13,390	45,481	29%
Haverhill	137,777	10,220	13,481	59,051	23%
Holyoke	97,048	5,304	18,297	30,770	59%
Lawrence	66,773	4,264	15,660	30,888	51%
Lowell	156,411	11,780	13,278	49,698	27%
New Bedford	174,963	12,332	14,188	34,893	41%
Pittsfield	117,287	11,273	10,404	41,297	25%
Springfield	314,243	26,045	12,065	36,114	33%
Worcester	287,725	24,811	11,597	44,580	26%
Total	\$1,763,583	128,870	\$13,685	N/A	N/A

Note: Median household income data from the 2008 to 2010 American Community Survey, U.S. Census.

Increases in Property Taxes

A second way of understanding these enormous costs is to calculate the tax increases that would be borne by single family homeowners if each city were to begin funding its liability by meeting its annual required contribution, or ARC, the amount required to fund benefits for current retirees and active employees. Table 5 shows that funding these benefits would add hundreds or, in some cases, more than a thousand dollars to homeowners' property tax bills every year for the next 30 years.

As discussed in the overview and shown in column A, these 10 cities currently underfund their ARCs by approximately \$192 million. In total, residential property owners would shoulder \$123 million of that shortfall in the form of additional taxes, as reflected in column B.

Of the \$123 million residential shortfall, single family homeowners would be responsible for \$72.7 million (column C). Multifamily homeowners, condominium owners, and other residential property owners would fund the nearly \$50 million balance.

Column D shows that funding the shortfall results in an average property tax increase of \$565 per single family homeowner for the 10 cities, with five cities raising tax bills by more than \$600. These increases—which would remain in place for 30 years—translate to additional taxes that range from 6 percent to 50 percent of the current average single family tax bill, as detailed in column F.

**Table 5
Increase in Average Single Family Tax Bills to Fund Retiree Health Care**

Municipality	ARC Shortfall (\$1,000s) (A)	Total Residential Share of ARC Shortfall (\$1,000s) (B)	Single Family Property Share of Shortfall (\$1,000s) (C)	Tax Bill Increase Per Single Family Property (D)	Average Tax Bill (E)	Tax Bill Increase (F)
Brockton	\$36,983	\$24,179	\$17,332	\$1,057	\$2,954	36%
Fitchburg	8,243	6,186	3,812	591	2,820	21%
Haverhill	4,947	3,691	2,279	223	3,648	6%
Holyoke	13,015	6,558	4,208	793	2,915	27%
Lawrence	25,011	14,875	5,155	1,209	2,397	50%
Lowell	23,261	16,106	8,407	714	3,205	22%
New Bedford	21,352	14,468	7,805	633	2,762	23%
Pittsfield	7,975	5,162	3,961	351	2,795	13%
Springfield	18,551	11,197	7,655	294	2,638	11%
Worcester	32,362	20,229	12,167	490	3,307	15%
Total	\$191,699	\$122,649	\$72,781	\$565	N/A	N/A

Note: The average tax bill data is for a single family home in fiscal 2011, as reported by the state's Division of Local Services.

Every homeowner in Lawrence would pay an additional \$1,209 in property taxes to fund retiree health care costs, an increase of 50 percent over the current average tax bill for a single family home in the city. In the four additional cities with increases greater than \$600—Brockton, Holyoke, Lowell, and New Bedford—property tax bills would rise between 22 percent and 36 percent.

In Worcester, the average single family tax bill would grow by \$490, or 15 percent. In Pittsfield and Springfield, which have adopted less costly benefit plans offered through the state’s Group Insurance Commission, tax bills would increase by \$351 and \$294, respectively, or greater than 10 percent. Haverhill would see the smallest increase of \$223—still a 6 percent increase on the average single family tax bill.

Table 6 compares the increase needed to fund retiree health care by meeting the ARC to the total increase in each city’s average property tax bill since fiscal 2006. In seven cities, the increase in one year simply to fund retiree health care is greater than or equal to the total increase in tax bills over the last five years.

In Brockton, to fund retiree health care the average single family tax bill would need to increase by 36 percent, or \$1,057, in one year; in comparison, the average tax bill rose by only 12 percent between fiscal 2006 and fiscal 2011. Fitchburg’s single family homeowners would see their property taxes rise by \$591 to meet the ARC—a single year increase of 21 percent that is one-and-a-half times the total five-year increase in the average property tax bill between fiscal 2006 and fiscal 2011.

Table 6
Increases in Property Taxes to Fund Retiree Health Care vs.
Total Increases in Average Single Family Property Tax Bill Since 2006

Municipality	Increase in Average Single Family Tax Bill to Meet ARC	Total Increase in Average Single Family Tax Bill, FY 2006 to FY 2011
Brockton	36%	12%
Fitchburg	21%	15%
Haverhill	6%	16%
Holyoke	27%	22%
Lawrence	50%	23%
Lowell	22%	22%
New Bedford	23%	18%
Pittsfield	13%	19%
Springfield	11%	18%
Worcester	15%	15%

Impact on Business Taxpayers

Because businesses pay a disproportionate share of taxes relative to their property values in these 10 cities, they would also bear a disproportionate share of the retiree health care liability. Businesses across the 10 communities would on average see a huge 20 percent property tax increase, large enough to force many employers with already tight margins to lay off employees and in some instances to go out of business.

As Table 7 shows, under the state's system of tax classification for commercial,

industrial, and personal properties, the average business tax rate (\$30.34 per \$1,000 of assessed value) is almost double the average residential tax rate (\$15.25) for the 10 cities as a whole. In Holyoke, Lawrence, Lowell, New Bedford, Pittsfield, and Worcester, local employers pay a tax rate that is more than twice the rate paid by residential property owners. Across the 10 cities, businesses are shouldering an average of approximately 35 percent of the total tax burden despite owning an average of only 21.5 percent of the total assessed value of all properties.

**Table 7
Business and Residential Shares of the Tax Levy and Tax Rates (FY 2011)**

Municipality	Business Property Taxes as % of Total Property Tax Levy	Business Properties as % of Total Assessed Value	Business Shift*	Tax Rate per \$1,000 of Assessed Value	
				Residential	Business
Brockton	34.6%	21.5%	1.61	15.29	29.55
Fitchburg	25.0%	20.0%	1.25	16.20	21.60
Haverhill	25.4%	16.9%	1.50	13.93	23.27
Holyoke	49.6%	29.5%	1.68	15.78	37.08
Lawrence	40.5%	23.2%	1.75	13.45	30.41
Lowell	30.8%	17.6%	1.75	14.27	29.73
New Bedford	32.2%	18.4%	1.75	12.88	27.14
Pittsfield	35.3%	21.1%	1.67	15.19	30.95
Springfield	39.6%	24.7%	1.60	19.49	38.97
Worcester	37.5%	21.8%	1.72	16.06	34.65
10 City Average	35.1%	21.5%	1.63	15.25	30.34

**Under the tax classification system for these 10 cities, the business tax rate (commercial, industrial, and personal property) can be up to 75 percent greater than what the rate would be if a municipality had a single, uniform tax rate applied to all properties. The residential and open space tax rate must be at least 50 percent of such a uniform rate.*

Because businesses pay 35 percent of the total property tax levy in these 10 cities, they are responsible for a commensurate 35 percent share of the retiree health care liability. As detailed in Table 8, the business portion of the unfunded liability in these cities is approximately \$1.6 billion of the total unfunded liability of \$4.5 billion.

At the high end, Holyoke businesses are responsible for 50 percent of the city's liability; Lawrence and Springfield businesses support about 40 percent; and Fitchburg and Haverhill businesses are at the low end at 25 percent.

Table 9 (page 12) depicts the enormous impact that funding this liability would have on business taxpayers—a nearly \$70

million, or 20 percent, increase over the fiscal 2011 levy that would be in place each year for 30 years. Six communities would need to boost business taxes by more than 20 percent, and only Haverhill would see a single-digit percentage increase.

Lawrence businesses would experience the most severe property tax jump of 50 percent, raising the city's business levy by \$10.1 million to a total of \$30.2 million. Brockton would require an additional \$12.8 million from its business community, a 36 percent property tax hike that would bring business' total tax bill to \$48.6 million. Worcester would need to increase its business taxes by 15 percent, adding \$12.1 million to the fiscal 2011 levy of \$82 million.

Table 8
Business Share of Unfunded Retiree Health Care Liability
(thousands of dollars)

Municipality	Unfunded Retiree Health Care Liability	Business Share of Total Property Tax Levy	Business Share of Unfunded Liability
Brockton	\$693,570	35%	\$240,122
Fitchburg	186,634	25%	46,581
Haverhill	299,042	25%	75,935
Holyoke	300,166	50%	148,928
Lawrence	323,977	41%	131,295
Lowell	432,752	31%	133,103
New Bedford	478,609	32%	154,311
Pittsfield	236,149	35%	83,303
Springfield	761,576	40%	301,913
Worcester	765,312	37%	286,931
Total	\$4,477,786	N/A	\$1,602,422

Table 9
Increase in Business Property Taxes to Fund Retiree Health Care
(thousands of dollars)

Municipality	ARC Shortfall (A)	Business Share of Shortfall (B)	Total Business Property Tax Levy, FY 2011 (C)	Percent Increase in Business Tax Levy (D)
Brockton	\$36,983	\$12,804	\$35,776	36%
Fitchburg	8,243	2,057	9,811	21%
Haverhill	4,947	1,256	20,546	6%
Holyoke	13,015	6,458	23,728	27%
Lawrence	25,011	10,136	20,101	50%
Lowell	23,261	7,154	32,132	22%
New Bedford	21,352	6,884	30,036	23%
Pittsfield	7,975	2,813	22,479	13%
Springfield	18,551	7,354	66,000	11%
Worcester	32,362	12,133	81,832	15%
Total	\$191,699	\$69,050	\$342,440	20%

These 10 cities typically have trailed the state as a whole during periods of economic growth and suffered more acutely in economic downturns. As Table 10 summarizes, these cities all have unemployment rates higher than the non-seasonally adjusted statewide rate of 6.4 percent. Lawrence, New Bedford, and Springfield have rates in the double digits, while Brockton, Fitchburg, Holyoke, and Lowell have rates that are a third to 50 percent above the statewide average.

The unemployment trends also contribute to higher-than-average poverty levels in these cities. Holyoke, Lawrence, New Bedford, and Springfield have poverty rates for individuals that are approximately double the state's rate of 11.4 percent, while Brockton, Fitchburg, Lowell, Pittsfield, and Worcester are approximately 50 percent greater than the statewide rate. Among families, Holyoke and Lawrence have poverty rates that are approximately triple the state's rate of 8.2 percent, while six other

communities have family poverty rates that are at least 50 percent greater than the state's level.

Table 10
Unemployment and Poverty Levels

Municipality	Unemployment Rate Nov. 2011	Individuals Below Poverty Line	Families Below Poverty Line
Brockton	8.8%	16.1%	12.8%
Fitchburg	9.8%	20.4%	15.0%
Haverhill	7.3%	11.9%	8.4%
Holyoke	9.6%	29.3%	26.2%
Lawrence	14.4%	27.3%	24.6%
Lowell	8.7%	17.2%	14.5%
New Bedford	11.7%	22.5%	19.8%
Pittsfield	7.0%	16.2%	11.7%
Springfield	10.4%	26.9%	22.0%
Worcester	7.7%	18.1%	14.3%
Statewide	6.4%	11.4%	8.2%

**The unemployment data is from the state Executive Office of Labor and Workforce Development (EOLWD) and not seasonally adjusted. The statewide seasonally adjusted unemployment rate is 7.0 percent. Poverty data is from the U.S. Census Bureau's 2008-2010 American Community Survey.*

The magnitude of the property tax increases needed to fund retiree health care liabilities would be a huge blow to the businesses and economies of these cities. The vast majority of these businesses are undoubtedly operating with tight margins so the property tax increases would inevitably lead to layoffs or the cancelation of expansion plans. Some fraction of these businesses would have no option but to close.

Conclusion

The enormous property tax increases needed to fund retiree health care liabilities demonstrate the magnitude of the problem facing cities and towns over the next decade and beyond. It is unrealistic to expect that taxpayers should or would bear this burden, and it is equally unrealistic to expect that these cities would decimate basic services like schools and public safety to pay for these benefits.

Simply put, cities and towns can no longer afford to provide retiree health care benefits in their current form. Implementing the recently enacted municipal health care reform is an important step to reduce these liabilities, but the obligations are so enormous that the Legislature needs to address the issue directly by adopting the kinds of recommendations put forward in this report.

Even with these changes, municipal retirees would still enjoy a level of health care benefits that has almost totally disappeared for virtually all other retirees in the Commonwealth. Delaying the inevitable will simply require more drastic cuts in benefits at a later date.

Recommendations

It is urgent that municipalities and the Legislature take steps to rein in these huge and growing liabilities. Delay will only require more difficult and sweeping action later.

There is a serious question whether many communities can afford to continue to provide any sort of retiree health care, particularly in combination with their pension obligations and the costs of employee health care. At a minimum, the extraordinarily generous retiree benefits must be scaled back, and the sooner communities act the more likely they will be able to preserve some form of those benefits.

This report makes a series of recommendations to address this problem. While municipalities have some flexibility to implement changes, several of the key reforms require legislative action. Because of the severity of the problem, the changes in benefits need to apply to current employees, and in some cases to current retirees, rather than only for new hires as in the case of pension changes. It is important to emphasize that even if all the recommendations were adopted, municipalities would still be providing their retirees with far more generous health benefits than all but a tiny fraction of Massachusetts employers.

Implement Municipal Health Reform

Municipal health reform is a huge and immediate opportunity for municipalities to reduce both current health care costs and long-term retiree health care liabilities. By implementing the health plan changes now permitted under state law, municipalities can lower the cost of retiree premiums and slow the rate of growth of these premiums, which will reduce municipalities' long-term retiree

health care liabilities and annual required contributions.

Tie Benefits to Years of Service and Raise the Minimum Service for Eligibility

Instead of allowing all retirees to be eligible for full retiree health care benefits after just 10 years of service, the Foundation recommends that these benefits be tied to length of service, as is the case with pensions. For example, employees could receive the municipality's maximum premium contribution of 75 percent at 35 years of service, with the contribution reduced proportionately for shorter tenures.

At the same time, the Legislature should consider raising the minimum length of service required to be eligible for these benefits from 10 years to 15 or even 20 years.

Raise the Eligibility Age for Retiree Health Care

The Foundation recommends that the eligibility age for retiree health care benefits be raised from 55 to 60, consistent with the recent reforms to the pension system. However, because the enormous retiree health care liabilities reflect what municipalities already owe—and do not account for new hires—this change must apply to current employees as well as new hires.

Currently, municipalities begin providing retiree health care benefits as early as age 55—ten years before they are eligible for Medicare. As a result, these retirees are enrolled in the same health plans as active employees with premiums that are significantly higher than Medicare premiums. Raising the eligibility age reduces the length of time for which a municipality would have to pay pre-Medicare premiums and be responsible for

the overlapping health care costs of both the retiree and the retiree's replacement.

Increase Eligibility Hours and Prorate Benefits for Part-Time Employees

Under state law employees must work only 20 hours per week to be eligible for retiree health care. Thus, an employee who works 20 hours per week for 10 years is entitled to the same retiree health benefit as an employee who works 40 hours per week for 35 years.

The Foundation recommends that the eligibility for retiree health benefits be raised to 1,400 hours or approximately 27 hours per week for part-time employees. In addition, the benefit should be tied to the number of hours an employee works. For example, an employee working three-fourths of a full-time schedule would be entitled to 75 percent of the benefits of a full-time employee with the same years of service.

End Spousal/Dependent Coverage

Providing spousal/dependent coverage to retirees is an expensive obligation and is unusually generous even among the dwindling ranks of employers still offering retiree health care. The Foundation recommends eliminating spousal/dependent coverage for all future retirees who are eligible for health benefits.

Costs for spousal/dependent coverage are at least twice as much as individual coverage. For example, in Haverhill's least expensive plan, the city pays approximately \$15,800, or over \$9,900 more, for an early retiree who elects family coverage instead of individual coverage. For supplemental Medicare plans, the city pays twice as much for retiree-plus-spouse coverage as it does for retiree-only coverage.

Reduce Municipal Share of Premium Contributions

Municipalities currently contributing more than 50 percent towards retiree health care premiums can reduce their contributions without requiring legislative action. However, for communities that adopt the new municipal health care law, there is a three-year moratorium on reducing the community's contribution for retiree premiums.

Municipalities, particularly those that contribute at the higher end, should revisit their contribution rates at the end of the moratorium required by the municipal health care law. For those municipalities that do not adopt the law, they should consider reducing their premium contributions sooner.

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