CITY OF MADISON, WISCONSIN

REPORT OF:	**City Attorney, Michael P. May Comptroller, Dean Brasser Interim Human Resources Director, Roger Goodwin**
TITLE:	**Establishing New Plans and Trusts for Post-retirement Medical Payments and a 401(a) Plan.**
AUTHOR:	**Michael P. May**
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REF: Ordinance ID #04163
Resolution ID #04164

TO THE MAYOR AND COMMON COUNCIL:

Background.

The City of Madison has an existing plan allowing employees, upon retirement, to convert the value of unused sick leave to purchase health insurance from the City's current providers. The plan is set up through some collective bargaining agreements and is also in secs. 3.36(6)(e)2., and 3.52(1)(b)3., MGO. If not converted to purchase insurance, the employee receives a cash payment.

At the time the plan was established in the late 1990s, the City was advised by its independent accounting firm that the plan met Internal Revenue Service (IRS) requirements. In light of guidance and rulings from the IRS issued over the last several years, the City Attorney examined the current plan. In the opinion of the City Attorney, it is necessary to change our existing plan to bring it into compliance with these new IRS rulings.

As a result of this determination, representatives of the Office of the City Attorney, the Human Resources Department and the Comptroller's Office interviewed four different firms offering plans for conversion of unused sick leave to post-retirement health benefits. The group unanimously recommended that the City participate in a new plan called "Prime Choice." This plan is offered by Precision Retirement Group, Inc., of Chippewa Falls, and utilizes J.D. Benefits, Inc., as trustee. The plan is in use by other governmental bodies in Wisconsin, including the Oregon School District. Oregon has obtained a Private Letter Ruling (PLR) from the IRS finding that the plan complies with IRS rules.

The City Attorney has reviewed the PLR and other aspects of the plan and believes it meets current legal standards.

The New Plan.

There are two major differences between the City's current plan and Prime Choice. First, at the front end where the plan is funded, the employee's ability to opt for health benefits or cash is changed. Under Prime Choice, the City as the employer will make that decision based on a series of objective questions posed to the employee at the time of retirement. The questions relate to the availability of funds for health care costs, amount of other retirement funds available, etc. Based on the interview, the City will determine whether to place the value of an employee's unused sick leave into the Medical Reimbursement Trust or into a 401(a) retirement plan. This decision is irrevocable. In order to comply with IRS rulings, the Prime Choice plan provides for employer, rather then employee, choice on the front end.

Second, the plan greatly expands the uses of the funds placed into the plan. Unlike the City's current plan, funds placed in the Medical Reimbursement Trust may be used for any medical costs allowed under sec. 213 of the Internal Revenue Code. Thus, any health insurance (not just the City's carriers) may be chosen, making the plan portable. Dental expenses, insurance co-payments and even long term care insurance are allowed expenses. This essentially allows retirees to pay for many medical costs, similar to those that are allowed under the City's existing Health Flex plan for employees. The plan similarly works on a reimbursement basis.

Another benefit of the plan is that it will be administered by Precision Retirement Group, Inc., and J.D. Benefits Inc., thus taking City staff out of the role of administering the plan.

The plan will also be offered to the City's unions. Some labor groups, such as Local 60 and the MCAA, who participate in the City's existing plan, will be required to change from the current plan to a new plan, and Prime Choice is being offered by the City. A memorandum of understanding or change to the existing collective bargaining units will be needed. If no plan is chosen by a union, union employees retiring on or after October 1, 2006, will only be allowed to receive a cash payment for accrued sick leave. Employees who are in a union that has a different plan than the City's plan for non-represented employees will have the choice (which must apply to the entire union) of keeping their existing plan or moving to the new Prime Choice plan.

Under the new plan, employees are not taxed when the sick leave value is placed in the Trust. Since the funds are used only as allowed under sec. 213 of the IRC, the employees are not taxed when used for medical expenses. The Trust will accrue earnings on a tax-free basis to be credited to the employees' accounts.

The final aspect of the plan is the 401(a) retirement trust. This is similar to a 401(k) plan, but is for governmental entities. If payout is made to this trust, it becomes available to the employee just as funds from any retirement fund would be. Payment into the trust is tax-free and earnings are tax-free. The employee is taxed when funds are taken from the plan, but it is net of FICA taxes, saving both the employer and the employee the 7.65% FICA tax. This is different from the City's current plan, where cash payments are taxed as wages. Under the Prime Choice plan, funds placed into the 401(a) plan are available upon request of the employee.

The new plans will be effective October 1, 2006.

Conclusion.

The City's current plan needs to be changed. For retiring employees who previously would have obtained future medical payments under the City's current plan, the Prime Choice plan improves the options for them. For employees who previously would have obtained a cash payment under the City's current plan, the new retirement trust plan improves their situation. The new plans are good for the City of Madison and its employees.

Implementation.

In order to implement the Prime Choice Plan, the Common Council must take several actions:

1. Approve a resolution establishing the various Trusts and Plans and authorizing the Mayor and Clerk to sign the necessary documents. For tax reasons, separate Medical Reimbursement Trusts and Plans will be established for existing retirees and new retirees. The new Plans are set to be effective October 1, 2006.

2. Amend sec. 3.36(6)(e)2., and 3.52(1)(b)3., MGO, to track the new plan.

3. Upon reaching agreement on the language to place into collective bargaining agreements, the Council will have to approve the new agreements. A MOU will be used in the interim.

The proposed resolution and ordinance amendments are before the Council as separate items, to which this Report is attached. The Plan documents are quite lengthy and complex. It is our intent to place them in Legistar as they are completed, but we will not distribute them to all Council members.

Michael P. May, City Attorney
Dean Brasser, Comptroller
Roger Goodwin, Interim Director of Human Resources