

July 13, 2005

The Honorable Robert Bunda, President  
and Members of the Senate  
Twenty-Third State Legislature  
State Capitol, Room 003  
Honolulu, Hawaii 96813

Dear Mr. President and Members of the Senate:

Re: House Bill No. 1608 HD1 SD2 CD1

On July 12, 2005, House Bill No. 1608, entitled "Relating to Voluntary Employees' Beneficiary Association Trusts" became law without my signature, pursuant to Section 16 of Article III of the State Constitution.

The purpose of this bill is to allow for the temporary establishment of a voluntary employees' beneficiary association (VEBA) trust. The VEBA trust would provide health benefits for State and county employees of a particular bargaining unit, as well as future retirees of that bargaining unit and existing retirees who wish to participate in the trust. The stated purpose of this VEBA trust pilot program is to allow a thorough analysis and evaluation of the costs and benefits of a VEBA trust compared with the Hawaii employer-union health benefit trust fund (EUTF) to determine what actual cost savings could be realized by the State through VEBA trusts.

I have a number of concerns about this bill. First, I am concerned about the effectiveness of the bill's safeguards against fraud or mismanagement by VEBA trustees. These VEBA trusts will likely not be covered by the federal Employee Retirement Income and Security Act of 1974 (ERISA), which provides strict standards and enforcement for private employee benefit plans. Although this bill attempts to create similar provisions in State law, there are some critical gaps. Unlike ERISA, the bill does not provide for a single State agency to be responsible for administering and regulating the VEBA trusts, provides no State agency with authority to make rules that may be necessary for such administration and regulation, and provides no funding for such administration and regulation.

Second, although creating what is described as a three-year pilot program, the bill does not provide for any study of the costs and benefits of a VEBA trust compared with the EUTF. No entity is designated to conduct the study. No funds are budgeted for the study.

Third, VEBA trusts could result in increased overall costs, and will certainly result in increased costs for employee groups consisting of older, less healthy members. The EUTF was formed, in part, to: (1) eliminate the negative effect on health benefit plan rates due to adverse selection caused by employee organization sponsored health plans, (2) eliminate the duplication of administrative costs caused by having multiple health plans for State and county employees, and (3) establish one large health plan that would have the leverage to negotiate better rates and benefits with insurance carriers and others offering health benefits plans.

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Under the provisions of this bill, the VEBA trusts can increase adverse selection in two ways. Bargaining units that have employees with better than average claims or loss experience can form VEBA trusts and exit the EUTF. This would increase the overall claims and loss experience of the remaining EUTF membership and tend to result in increased rates for those remaining in the EUTF. In addition, the bill provides for the VEBA trusts to cover all future retirees. This will result in the VEBA trusts having younger retirees while the EUTF would be left with older retirees. This would also tend to result in the EUTF having higher rates for retiree plans.

Fourth, the bill does not address certain adverse effects to the EUTF caused by the establishment of VEBA trusts. The EUTF's administrative budget is paid out of the public employers' monthly contributions for each employee's and retiree's health plans. The bill requires such contributions with respect to VEBA trust members to be transferred to the applicable VEBA trust. With respect to the Hawaii State Teachers Association VEBA trust, it is estimated that this will result in a shortfall of over \$500,000 in the EUTF's administrative budget. No appropriation was made to address this shortfall or any other shortfalls caused by the formation of VEBA trusts by other employee organizations.

Finally, there are questions as to whether membership in a VEBA trust can be mandatory for retirees and whether employee organizations can be empowered to negotiate on behalf of such retirees. There are also certain unresolved legal issues regarding VEBA and EUTF eligibility and public employer contributions. For example, where both spouses are public employees or retirees and only one belongs to a bargaining unit that sponsors a VEBA trust, it is not clear whether both spouses can have separate memberships in the EUTF and VEBA trust, and whether public employer contributions to them can exceed the cost of one EUTF family health plan. Another issue regarding retirees who opt to transfer to a VEBA trust is whether the public employers must pay the VEBA trust the same contribution as it pays the EUTF even if the VEBA trust's retiree health plans cost less than the EUTF's retiree health plans.

Despite these concerns, I allowed the bill to become law without my signature. There are many public employees who feel that the VEBA trust has significant benefits, and who wish to have the VEBA option available to them. Further, because this bill will sunset in three years, there will be an opportunity to assess its results. However, I urge the Legislature to address the concerns I have outlined above during the 2006 session, so as to provide greater protections for employees, a meaningful assessment of the results of this pilot program, and to resolve the other legal concerns about this bill.

Therefore, I allowed House Bill No. 1608 HD1 SD2 CD1 to become law as Act 245 effective July 12, 2005 without my signature.

Sincerely,

LINDA LINGLE