News Scan

GRS
Gabriel Roeder Smith & Company
Consultants & Actuaries

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The following news summaries were developed by Gabriel, Roeder, Smith & Company to inform clients and other benefit professionals of news in the benefits industry. Our thanks to Mary Ann Vitale for her diligent work on this issue. To receive this publication electronically, send an email to web.admin@gabrielroeder.com with "SUBSCRIBE NEWS SCAN" in the subject line. To stop receiving this publication electronically, send "UNSUBSCRIBE NEWS SCAN" in the same manner. Copies of this and other benefit-related publications are available on the GRS web site at www.gabrielroeder.com.

Note: The authors of these summaries are not attorneys and the statements made are not legal advice or opinion. Qualified legal advice should be obtained before acting with regard to related laws and regulations.

NASRA and NCTR Release Public Fund Survey Findings for 2007

In November 2008, the National Association of State Retirement Administrators (NASRA) and the National Council on Teacher Retirement (NCTR) released the Public Fund Survey Summary of Findings for FY 2007. The survey presents key data from 101 public retirement systems with 125 plans, covering 13.2 million active members, 6.5 million retirees and other annuitants, and holding $2.79 trillion in assets as of fiscal year (FY) 2007. The data pertain to defined benefit plans, including several hybrid plans. Overall, the systems surveyed represent approximately 85% of public retirement plan membership and assets.

The Summary of Findings presents statistical analysis regarding plan funding, membership, benefits, contribution rates, cash flows, and actuarial assumptions. Key findings include:

- The average actuarial funded ratio for the surveyed plans was 86.1% in FY 07, up slightly from 85.7% in FY 06, with 62% of the plans having funded ratios above 80.0%. Notably, the plans funded above 80.0% comprise three-fourths of the assets of all surveyed plans.
- The aggregate funding level increased slightly for the first time since FY 01. However, projections indicate that over the next three to five years funding levels will likely be significantly lower due to the sharp decline in assets values in 2008.
- Since FY 01, the number of annuitants has increased by a cumulative 26.1% compared with an increase in active members of only 5.4%. The ratio of active members to annuitants fell from 2.10 in FY 06 to 2.05 in FY 07.
- The median annual investment return was -4.7% in FY 07, down from 17.6% in FY 06. Median returns were negative in FY 01 and FY 02, but FY 04 to FY 07 produced strong, double digit returns – illustrating the significant investment volatility since the start of the decade.
- The median actuarial assumption for investment return was 8.0% in both FY 06 and FY 07. The median assumption for the real rate of return was 4.5% in both FY 06 and FY 07.

The survey data are available on-line for each individual system and plan, including: plan membership, actuarial assumptions and methods, plan assets and liabilities, contribution rates, and system asset allocations, among other information. Selected data can also be viewed on the survey website through comparative tables that allow sorting on selected items and provide graphs of selected data (e.g., inflation and investment return assumptions).

The survey is accessible at: http://www.publicfundsurvey.org. Registration is required to access the data; however, after registration the data are available at no charge.

IRS Announces Two-Year Extension for Governmental Plans to Adopt Normal Retirement Age Rules

On October 10, 2008, the Internal Revenue Service issued Notice 2008-98, announcing its intention to provide a two-year extension for governmental plans to comply with the final regulations related to normal retirement age. Issued in 2007, the regulations were originally effective for governmental plan years beginning on or after January 1, 2009. Notice 2008-98 extends the effective date for governmental plans to plan years beginning on or after January 1, 2011.

The 2007 regulations were issued to implement the new in-service distribution rules under the 2006 Pension Protection Act. The new rules allow retirement benefits to be paid to a plan member while the member is still employed by the plan sponsor, provided the member is at least age 62 or has reached normal retirement age under the plan. The regulations define "normal retirement age" as being "not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry…." In addition to age 62, the regulations provide several safe harbors that the IRS will presume to be the "typical" earliest normal retirement ages, depending on facts and circumstances: (1) age 55 for non-public safety employees, and (2) age 50 for public safety employees. Earlier ages are not deemed to be typical; however, the IRS Commissioner has the authority to review this based on facts and circumstances.

If not currently in compliance, governmental plan sponsors have two additional years to comply with the new regulations. This extension will also give governmental plan representatives time for further discussions with the IRS and Treasury regarding typical retirement eligibility provisions established by governmental plans. Governmental plan sponsors may rely upon Notice 2008-98 until the IRS and Treasury amend the final regulations.

Notice 2008-98 is available at: http://www.irs.gov/irb/ by searching for IRB 2008-44.

IRS Modifies the Determination Letter Cycle for Governmental Plans

On November 5, 2008, the Internal Revenue Service announced it would modify its determination letter cycle for governmental plans in order to better allow plan sponsors to seek IRS determinations that the plans are qualified under the Internal Revenue Code. The announcement was made in the November issue of *Employee Plan News*, a newsletter published by the IRS.

In 2007, Revenue Procedure 2007-44 provided that governmental plan sponsors file their requests for determination letter during Cycle C, which began on February 1, 2008, and will end on January 31, 2009. However, to date, the IRS has received only 120 applications from governmental plan sponsors. To encourage more plans to seek determination letters, the IRS will now allow governmental plan sponsors a one-time option of filing under Cycle E, which will begin on February 1, 2010 and end on January 31, 2011.

Plan sponsors can take advantage of this extension by simply filing under Cycle E. No advance notice is required by the IRS. In addition, plan sponsors who have already filed under Cycle C may withdraw their application and receive a refund of the user fee, so long as the request for determination letter was filed before November 7, 2008. For plan sponsors filing in Cycle E, plan documents will need to be amended to include all relevant changes to the qualification rules and regulations applicable for Cycle E. After 2011, all governmental plan sponsors will again be subject to Cycle C, with the next Cycle C ending January 31, 2014.

Additionally, for plan sponsors who choose to stay in Cycle C, the IRS will move the governmental filers to the "head of the queue." Moreover, for plan sponsors that filed in Cycle C and used the Voluntary Corrections Program (VCP), the IRS will reduce VCP collection fees by one-half.

Employee Plan News is available at: http://www.irs.gov/pub/irs-tege/se1108.pdf

Issue Brief Finds Local Government Pension Plans to be as Well Funded as State Plans

On October 8, 2008, the Center for State and Local Government Excellence (SLGE) published its issue brief, *The Funding Status of Locally Administered Pension Plans*, comparing the funding of locally administered pension plans with state-administered plans. Working in conjunction with Boston College researchers, the report found that local plans were generally as well funded as state plans with a funding ratio of 85% for local plans compared to 84% for state plans.

The results are based on the *Local Pension Plan Survey* (LPPS) using data on the funding status of 84 locally administered public pension plans in 38 states collected primarily for 2006 from actuarial reports and Comprehensive Annual Financial Reports (CAFRs). The comparison with state plans was made using data for state-administered plans reported in the *2006 Public Fund Survey* prepared by the National Association of State Retirement Administrators (NASRA) and the National Council on Teacher Retirement (NCTR).

According to the Center's Executive Director, Elizabeth Kellar, "State and local governments have achieved about the same funding status as private sector employers, even though Congress did not impose the same requirements on governments as it did on the private sector."

The issue brief is accessible at: http://tinyurl.com/thefundingstatus

NCSL Reports on 2008 State Pension and Retirement Legislation

In September 2008, the National Conference of State Legislatures (NCSL) published its report on the major state pension and retirement plan legislation enacted in 2008. Compiled for the National Conference on Public Employee Retirement Systems (NCPERS), the report provides a comprehensive and detailed summary of selected state pension and retirement legislation enacted through July 7, 2008.

Consistent with recent financial events, the long-term sustainability of defined benefit plans is a concern for state legislatures. The report found that benefit increases in 2008 were rare and, if enacted, were very moderate. Several states enacted new plans with reduced benefits for newly hired employees, often involving lower benefit multipliers, longer vesting periods, and limitations on the use of leave for calculating benefits. One state passed legislation allowing employees to voluntarily transfer from a defined contribution (DC) plan to a defined benefit (DB) plan, and another state enacted a hybrid retirement plan for new hires, including a DB component plus a 401(k) with matching employer contributions.

Other frequent policy issues addressed by legislation included: benefit eligibility, contribution rates, funding issues, cost-of-living adjustments, governance and investment policy, health coverage, re-employment after retirement, and purchase of service credit. The report is organized by topics and summarizes the legislation enacted by state.

The report is on the NCPERS website at: http://ncpers.org/News/PageText/documents/Leg2008July.pdf

National Assessment Compares State Retiree Health Plans

In September 2008, the Center for State and Local Government Excellence joined with researchers from North Carolina State University's School of Public and International Affairs and College of Management to examine state retiree health plans. The resulting report, *Retiree Health Plans: A National Assessment*, compares similarities and differences in retiree health plan characteristics, including: eligibility requirements and the state's share of plan costs per retiree. Additionally, the report contains a quick reference guide summarizing current retiree premiums, dependent coverage, and Medicare enrollment requirements for each state. Also included is a brief summary of each state's retiree health care plans as of March 2008 with links to the plans' websites.

The report is accessible at: http://tinyurl.com/rhpnatlassessment

CRS Analyzes Employment and Retirement Trends for Older Workers

On September 15, 2008, the Congressional Research Service updated its report, *Older Workers: Employment and Retirement Trends*, which predicts that the retirement of baby-boomers could have a significant effect on economic growth. According to the U.S. Census Bureau, the number of older workers age 55 to 64 will increase by about 11 million between 2005 and 2025, while the number of workers age 25 to 54 will grow by only 5 million. This trend could affect economic growth, since labor force participation begins to decline after age 55. As a result, millions of experienced employees will leave the labor force.

According to the report, many factors influence the rate of employment for individuals age 55 and over including: general economic conditions, eligibility for Social Security benefits, health insurance availability, and the design and prevalence of employer-sponsored pensions. Participation in the labor force among workers age 55 and over may also be affected by the trend toward defined contribution plans in the private sector, since such plans generally do not encourage early retirement.

However, the report also found that employment for workers age 62 and older has been increasing, with a trend towards more full-time employment. To further encourage retention of older workers, employers may do more to offer part-time employment or "phased retirement". Under current law, many different approaches for phased retirement are possible, including: job sharing, reduced work schedules, and rehiring retired workers on a part-time or temporary basis. In addition, the 2006 Pension Protection Act allows a pension plan to begin paying "in-service" benefits to participants who have reached age 62 or the plan's normal retirement age, even though they are still working for the plan sponsor. Some employers would like to pay partial distributions when workers attain early retirement age in the pension plan. However, this would require a change in federal law.

The report is available at: http://assets.opencrs.com/rpts/RL30629_20080915.pdf

GAO Report Recommends DOL Issue Guidance on Hedge Fund and Private Equity Investments

On September 10, 2008, leaders of the U.S. Senate Finance Committee requested the Department of Labor to develop guidance for pension investments in hedge funds and private equity. The request was based on the recommendations made in the recent Government Accountability Office (GAO) report, *Defined Benefit Pension Plans: Guidance Needed to Better Inform Plans of the Challenges and Risks of Investing in Hedge Funds and Private Equity*. The GAO report was prepared to assess the extent to which pension plans invest in hedge funds and private equity, examine the potential benefits and challenges associated with these investments, and recommend means for better regulating and monitoring the investments.

The GAO found that while a limited share of total pension assets are invested in hedge funds and private equity, a growing number of plans are making such investments. According to several recent surveys of mid- to largesized pension plans, investments in hedge funds and private equity generally averaged about 4% and 5% of plan assets, respectively. However, about 21-27% of the plans invest in hedge funds and over 40% invest in private equity. Moreover, the percentage of large plans investing in hedge funds has grown rapidly from about 11% in 2001 to 47% in 2007.

According to the report, reasons why pension plans invest in hedge funds include: 1) less volatile expected returns, 2) greater returns than expected from stocks, and 3) diversification of investments. However, the report also notes that hedge funds pose challenges which demand greater expertise than traditional investments, including: 1) limited transparency of the hedge fund's underlying assets and liabilities, 2) limited liquidity due to contract provisions, and 3) operational risks which could result in losses due to trading errors or fraud.

Reasons why plans invest in private equity include: 1) greater returns than expected from stocks and 2) diversification of investments. However, challenges include: 1) greater performance variation among private equity funds compared to other asset classes, 2) limited liquidity due to long-term commitments of 10 or more years, and 3) problems with investment valuation due to difficulties in assessing the value of underlying holdings prior to their sale.

With regard to regulating hedge funds and private equity, the GAO noted that the federal government does not specifically limit or monitor such investments. However, in order to mitigate the associated challenges, greater effort and expertise is required on the part of plan fiduciaries. To ensure plan fiduciaries are prepared for these challenges, the GAO recommended that the Secretary of Labor issue guidance on hedge fund and private equity investments, especially with regard to assessing whether and to what degree such investments would be prudent.

The GAO report is accessible at: http://www.gao.gov/new.items/d08692.pdf

American Academy of Actuaries Advocates Raising Social Security Retirement Age

On September 5, 2008, representatives of the American Academy of Actuaries briefed congressional staff on the Academy's August 2008 Position Statement advocating raising Social Security's retirement age to address the program's funding imbalance. During the briefing, Thomas S. Terry, Vice President and Chairperson of the Academy's Pension Practice Council stated "as life expectancy increases, the percentage of workers' lives spent in retirement continues to grow, while the number of working years stays relatively constant. Inevitably, Social Security's costs will exceed what its scheduled financing will support."

In 1983, Congress amended Social Security by raising the normal retirement age (NRA) for full retirement benefits from 65 to 67 phased-in over 30 years, and frozen at age 67 for all workers born after 1959. According to its Position Statement, the Academy board believes that the Social Security system should address future increases in longevity by extending the currently scheduled increases in Social Security's retirement age. However, the representatives also noted that the Academy does not advocate a specific proposal for raising Social Security's retirement age. Instead, Bruce D. Schobel, Chairperson of the Academy's Retirement Security Principles Task Force, presented the following hypothetical sample proposals for raising Social Security's retirement age:

1) Speed up increasing the NRA to age 67 for everyone not currently eligible for Social Security. This change is expected to eliminate about 10% of the program's long-term deficit.
2) Same as Proposal 1, but then increase the NRA by one month every two years until it reaches age 70. This change is expected to eliminate about 35% of the long-term deficit.
3) Retain the current schedule of NRA increases to age 67, but continue increasing it by two months every year until it reaches age 70. This change is expected to eliminate about 50% of the long-term deficit.

The Academy also urged public policymakers to promptly address Social Security's funding problems. This would allow any necessary future tax increases to be phased in gradually and allow any reductions in benefits to be applied in a way that reduces the impact on individuals. Prompt action would also allow individuals more time to modify their financial planning in response to the changes.

Further information is available on the Academy's website at:
http://www.actuary.org/pdf/socialsecurity/briefing_sept08.pdf

SSA Releases Fast Facts and Figures about Social Security for 2008

In August 2008, the U.S. Social Security Administration's (SSA) Office of Policy released *Fast Facts & Figures about Social Security, 2008*. The publication answers frequently asked questions about the programs administered by the SSA and focuses on data related to Social Security retirement, survivors, and disability benefits and Supplemental Security Income (SSI). Most of the data are from the SSA's *Annual Statistical Supplement to the Social Security Bulletin* and the 2008 Social Security Trustees Report. Highlights include:

- Overall, about 55 million people received SSA benefits or assistance in 2007, with benefits averaging about $1,079 per month for retired workers, $1,004 per month for disabled workers, and $1,040 per month for non-disabled widows and widowers.
- In 2007, the SSA paid benefits to 16% of the U.S. population and 90% of the population over age 65.
- About 64% of the population over age 65 received at least 50% of their income through SSA payments and 32% received almost all of their income through SSA payments.
- About 56% of the adult SSA benefits were paid to women.

The publication also provides a table of the gradual extended ages for full Social Security retirement benefits based on year of birth. For those born before 1938, eligibility for full retirement benefits is age 65. Beginning with those born in 1938, the age for full benefits increases by two months each year until reaching age 66 for those born in 1943. It remains at age 66 for those born from 1943 through 1954, and then continues increasing by two months each year until reaching age 67 for those born in 1960 and later.

The report is available at:
http://www.socialsecurity.gov/policy/docs/chartbooks/fast_facts/2008/fast_facts08.pdf

U.S. Census Bureau Reports 1.3 Million Fewer Americans Lacked Health Coverage in 2007

On August 26, 2008, the U.S. Census Bureau released its annual report, *Income, Poverty, and Health Insurance Coverage in the United States: 2007*. The report found that the number of uninsured Americans decreased by 1.3 million, from 47.0 million in 2006 to 45.7 million in 2007, or from 15.8% to 15.3% of the U.S. civilian population. This change was largely attributable to an increase in government-sponsored health insurance which covered 80.3 million individuals in 2006 and rose to 83.0 million in 2007. Government insurance includes Medicare, Medicaid, the State Children's Health Insurance Program, military health care and individual state plans.

Additionally, the uninsured rate for children under age 18 declined from 11.7% (8.7 million) to 11.0% (8.1 million), and the uninsured rate for children in poverty dropped from 19.3% to 17.6%. According to the Commonwealth Fund, the improvement in health insurance coverage for children also reflects an increase in the percentage of children enrolled in government programs, which rose from 29.8% in 2006 to 31.0% in 2007.

However, Americans with private insurance declined from 67.9% of the civilian population in 2006 to 65.7% in 2007, and those with employer-provided coverage dropped slightly from 59.7% to 59.3%. Overall, those with government health insurance grew from 27.0% in 2006 to 27.8% in 2007, while those with Medicaid coverage grew from 12.9% in 2006 to 13.2% 2007. Responding to the report, Henry E. Simmons, president of the National Coalition on Health Care, warned that the transition from private to public coverage may be problematic since the shift "may be difficult to sustain and expand as economic growth falters and pressures on federal and state budgets intensify." (BNA *Pension & Benefits Reporter*, September 2, 2008).

The Census Bureau also examined insurance rates by region and state. The analysis found that the Northeast and Midwest each had uninsured rates of 11.4% which were lower that those in the West and South, of 16.9% and 18.4% respectively. Texas had the highest state uninsured rate of 24.4%; whereas Massachusetts and Hawaii had the lowest uninsured rates at 8.3%.

The data were compiled from information collected in the 2008 Current Population Survey (CPS) Annual Social and Economic Supplement (ASEC). The Census Bureau's report is accessible at: http://www.census.gov/hhes/www/hlthins/hlthin07.html

Benefits Trend Study Finds Wellness Programs Can Effectively Reduce Medical Costs

On October 20, 2008, MetLife released its report, *Sixth Annual Employee Benefits Trend Study*, which found that 94% of surveyed employers who offer wellness programs believe they are effective in reducing medical costs. Wellness programs and strategies can help workers lead healthier lives. Consequently, they have the potential to control long-term healthcare costs and improve productivity by reducing absenteeism, incidence of disability, and costly future medical treatments and procedures. Wellness programs include programs for exercise, weight management, smoking cessation, and cancer screenings. Most employers offer incentives to encourage participation in wellness programs, such as:

- Fitness center discounts (40% of surveyed employers),
- Gifts and prizes (38%),
- Reduced employee contributions to medical plans (27%),
- Waiving medical plan deductibles (17%),
- Additional time off (17%),
- Credits for benefit purchases (14%), and
- Cash or bonuses (2%).

According to the study, wellness programs are:

- Used by employers to strengthen employee loyalty and achieve greater employee retention;
- Typically designed for an aging workforce; and
- Help keep health insurance viable and offset future spending on chronic medical conditions.

The study was conducted during the third quarter of 2007 and consisted of two separate surveys: 1) an employer survey of over 1,600 decision-makers in various industries and geographic locations and 2) an employee survey of almost 1,400 full-time employees, age 21 and over, who represented a broad cross-section of respondents that was weighted to reflect the total U.S. working population.

The study can be accessed at: http://www.whymetlife.com/trends/downloads/MetLife_EBTS08.pdf

California Enacts Legislation to Improve Transparency and Governance of Public Retirement Benefits

On September 27, 2008, Governor Arnold Schwarzenegger signed three bills implementing the recommendations of the California Public Employee Post-Employment Benefits Commission. In January, the commission issued its report outlining specific recommendations for improving the funding and administration of public employee pension and health benefits. The commission focused on prefunding retiree health benefits, improving governance, and increasing transparency. In its report, the commission estimated that California's state and local governments had unfunded retiree health care liabilities of $118 billion, including $48 million for state retirees and $70 million for retirees of local governments. The enacted bills are summarized below:

A.B. 1844 - This bill makes it a crime to aid and abet a person who presents false information to a retirement system in order to receive benefits or payments that are fraudulently obtained. Additionally, the bill gives pension systems greater access to information held by insurers, such as workers' compensation insurers.

A.B. 2023 - This bill applies to the California Public Employees Retirement System (CalPERS), the California State Teachers Retirement System (CalSTRS), and 20 counties participating in the County Employees Retirement Act of 1937. It requires them to consider only proper medical documentation when determining eligibility for disability benefits and prohibits consideration of other issues (e.g., personnel, disciplinary, or other non-medical issues).

S.B. 1123 – This bill is intended to increase transparency and oversight of public employee benefit plans by requiring state and local retirement systems to include post-employment benefits in their triennial actuarial valuations. It also requires that the future annual costs of these benefits be made public at least two weeks prior to any post-employment benefit increases and prohibits the system's governing body from adopting such changes by means of a consent calendar (typically used for noncontroversial bills passed with little discussion). Additionally, the bill creates the California Actuarial Advisory Panel to provide independent information on pensions, post-employment benefits, and best practices to the governor, legislature, public retirement systems, public agencies, and other interested parties.

The bills become effective January 1, 2009, and are available by searching for the bill number at: http://www.leginfo.ca.gov/bilinfo.html

Source: BNA *Pension & Benefits Reporter*, October 7, 2008.