

September 2007

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.

IRS Posts Pension Protection Act Guidance Charts

On September 19, 2007, the IRS posted two charts showing provisions of the Pension Protection Act of 2006 (PPA) organized by 1) topic and 2) Internal Revenue Code section. The charts list the changes made by the PPA along with related IRC section numbers, relevant published guidance, and other information available from the IRS. Topics of potential interest to public pension plans include: 415 limits, distributions, Indian tribal governments, permissive service credit, phased retirement, and rollovers.

PPA published guidance by topic and IRC section are available, respectively, at: http://www.irs.gov/pub/irs-tege/ppa_chart_topic.pdf and http://www.irs.gov/pub/irs-tege/ppa_chart_code.pdf

IRS Releases Proposed Rules on Medical and Accident Insurance Payments

On August 17, 2007, the IRS released proposed regulations (REG-148393-06) regarding the tax treatment of payments made by qualified retirement plans for medical or accident insurance under IRC § 402(a). The proposed rules would clarify that a payment from a qualified plan for a participant's accident or health insurance premium generally is a taxable distribution under IRC § 72 in the taxable year in which the premium is paid. Furthermore, under IRC § 213 the participant may take a tax deduction for this amount, to the extent that it and the participant's other qualified, uncompensated medical expenses exceed 7.5% of adjusted gross income. Moreover, to the extent the premium payment is treated as a distribution from a qualified plan, the amount received by the participant through related accident or health insurance for personal injury or illness would not be includible in gross income.

The proposed regulations would also clarify that employer contributions to provide medical benefits in an IRC § 401(h) account under a qualified plan or annuity would not be includible in the participant's gross income, provided the 401(h) account satisfies all related requirements. Similarly excluded are distributions by the plan under IRC § 402(l) of up to \$3,000 annually to directly purchase accident or health insurance (or qualified long-term care insurance) for eligible retired public safety officers and their spouses or dependents. The IRS found that these narrow exceptions are consistent with the general rules related to premium payments by qualified plans for accident and health insurance.

Written or electronic comments on the proposed rules are due by November 19, 2007.

The proposed regulations are available at:

<http://a257.g.akamaitech.net/7/257/2422/01jan20071800/edocket.access.gpo.gov/2007/E7-16084.htm>

Congress Considers Allowing Retired Federal Workers to Pay Health Insurance Premiums with Pretax Dollars

On September 18, 2007, the U.S. House Oversight and Government Reform Committee approved H.R. 1110, which would amend the Internal Revenue Code to permit (i) retired federal workers (civilian and military) to pay federal health insurance premiums on a pretax basis, and (ii) provide a tax deduction for TRICARE supplemental premiums and enrollment fees. (TRICARE is the U.S. military's health care plan.) The bill was introduced by Representative Tom Davis (R-VA) at the beginning of 2007 and has 263 cosponsors. Senator John Warner (R-VA) introduced an identical bill in the Senate (S. 773), which has 52 cosponsors.

In some ways, the bills are similar to the 2006 Pension Protection Act provision allowing qualified retired public safety officers to pay up to \$3,000 of their health insurance premiums with retirement plan distributions on a pre-tax basis. However, while the provision for retired public safety officers requires the pretax health care payments to be capped at \$3,000 and paid directly by the pension plan to the insurer, it appears no similar requirements would apply to federal retirees.

The text and current status of the bills are available on the Library of Congresses' Thomas web site: www.thomas.gov

U.S. Treasury Department Releases Issue Brief on Social Security Reform

In September 2007, the U.S. Treasury Department issued the first in a series of issue briefs on Social Security reform titled *Social Security Reform: The Nature of the Problem*. The brief presents a historical overview of the Social Security program, explains the extent of Social Security's financial imbalance, and discusses the importance of implementing Social Security reform soon in fairness to future generations of workers. Key findings include:

- Social Security faces a shortfall over the indefinite future of \$13.6 trillion in present value terms, or the equivalent of 3.5% of future taxable payrolls.
- Social Security can be made permanently solvent only by reducing the present value of scheduled benefits and/or increasing the present value of scheduled tax revenues.
- Delaying changes to Social Security reduces the number of cohorts over which the burden of reform can be spread.
- Faster economic growth will not automatically solve Social Security's financial imbalance.

The second issue brief will focus on whether trust fund accumulations, such as Social Security surpluses, increase the government's capacity to pay future Social Security benefits and the resulting implications for Social Security reform.

The issue brief is available at: <http://www.treas.gov/press/releases/reports/post.pdf>

Center for Retirement Research Analyzes Raising Social Security's Early Retirement Age

In August 2007, the Center for Retirement Research (CRR) at Boston College released an issue brief titled, "Promoting Work: Implications of Raising Social Security's Early Retirement Age." The brief focuses on the effects of raising Social Security's Early Eligibility Age (EEA) from age 62 to age 63.5 to promote working longer. Currently, many analysts believe that the availability of EEA at age 62 causes many workers to leave

the workforce to claim early Social Security benefits. According to the report, over 50% of male and female workers claim Social Security at age 62. Currently, the average retirement age is 63 for males and 62 for females.

The brief examines the possibility of raising the EEA to encourage workers to work longer without undue hardship. Some of the key findings included:

- Raising the EEA would encourage longer working lives and help improve retirement security.
- Trends in the health of older workers and less physical demands of jobs make raising the EEA feasible.
- Only 10% or less of older workers would be considered at risk due to raising the EEA.

The issue brief is available at: http://crr.bc.edu/images/stories/Briefs/wob_12.pdf

American Academy of Actuaries Publishes Issue Brief Finding Defined Benefit Structure Preferable for Basic Social Security Benefits

In September 2007, the American Academy of Actuaries published its Issue Brief, “Social Security: Evaluating the Structure for Basic Benefits.” The brief was prepared by the Academy’s Social Insurance Committee which concluded, after extensive study, that the defined benefit structure is preferable to the defined contribution structure for providing basic retirement and disability benefits under Social Security. The brief stressed that the predictable retirement income and inherent risk-sharing features of the current defined benefit structure of Social Security are especially important due to the trend toward defined contribution structures among employer-sponsored retirement plans. The Academy’s Senior Pension Fellow Ron Gebhardtshauer stated, “In many cases, conversions of defined benefit pension plans to defined contribution plans, such as 401(k) plans, have left Social Security as the only remaining source of a guaranteed lifetime income for many workers.”

Additionally, the brief provides a side-by-side comparison and analysis of the advantages and disadvantages of using defined benefit and defined contribution approaches to providing basic Social Security benefits. Currently, Congress is considering Social Security reforms which could include changes within the defined benefit structure, such as decreasing the benefits payable or increasing the tax rate. Other reforms under consideration include adopting a defined contribution structure with individual accounts to supplement or replace the current defined benefit structure. However, the committee cautioned that the use of a defined contribution approach, such as individual accounts, should only be considered as a supplement to Social Security benefits, rather than as a primary source.

The issue brief can be found on the American Academy of Actuaries’ website at: http://www.actuary.org/pdf/socialsecurity/structure_sept07.pdf

BLS Publishes Survey Findings for Private-Sector Employee Benefits in 2007

On August 22, 2007, the U.S. Labor Department’s Bureau of Labor Statistics (BLS) published its report, the “National Compensation Survey: Employee Benefits in the United States, March 2007.” The survey represents about 108 million full- and part-time workers in over 8,200 private-sector establishments in the U.S. In preparing the report, the BLS focused on retirement and medical care plan access and participation, paid leave, life insurance, and disability benefits. In addition, for the first time, the report shows plan “take-up rates” in the same tables that show access and participation rates. The take-up rate is the percentage of workers with access to a plan who participate in the plan.

As reported by the BLS, 71% of private-sector workers had access to medical care plans in March 2007, with 52% of private-sector workers participating (a take-up rate of 73%). Sixty-one percent had access to retirement plans, with 51% participating (a take-up rate of 84%). The proportions of workers participating in employer-sponsored medical and retirement plans were unchanged from the previous year; however, the proportion of

employers offering health insurance declined from 62% in 2006 to 60% in 2007, and those offering retirement plans declined from 48% to 46%. Larger employers (those with 100 workers or more) are much more likely to offer these benefits than smaller employers.

Of the workers with access to retirement plans, 84% participated in defined benefit (DB) or defined contribution (DC) plans, or both. Twenty-one percent had access to DB plans, with 20% participating (a take-up rate of 95%). Fifty-five percent had access to DC plans, with 43% participating (a take-up rate of 77%). Other major findings related to private sector employee benefits include:

- 77% of private-sector workers had paid holidays and vacations with an average of eight paid holidays per year and nine paid vacation days after one year of service.
- Most workers were covered by medical plans requiring employee contributions for premiums. On average employees paid \$81.37 per month for single coverage and \$312.78 per month for family coverage.
- Employers requiring employee contributions for medical plan premiums paid an average of \$293.25 per month for single coverage and \$664.04 per month for family coverage. Employers who paid the full premium for medical plans paid an average of \$382.19 per month for single coverage and \$814.44 per month for family coverage.
- 58% of workers had access to life insurance with 56% participating.
- 39% of workers had access to short-term disability and 31% had access to long-term disability, with nearly all participating who had access to the plans.

In Spring 2008, a similar release is scheduled to be issued covering state and local government workers.

The news release is available at: <http://www.bls.gov/news.release/pdf/ebs2.pdf> and the summary report is available at: <http://www.bls.gov/ncs/ebs/sp/ebsm0006.pdf>

EBRI President Discusses Employers' Incentives for Improving Employees' Financial Literacy

On September 19, 2007, Employee Benefit Research Institute (EBRI) President and CEO Dallas Salisbury spoke to the ERISA Advisory Council's Working Group on Financial Literacy and the Role of the Employer. In responding to a question about whether retirement plan sponsors should receive financial incentives for helping participants plan for retirement, he indicated that he did not believe direct incentives would be useful. However, he argued that plan sponsors do have strong long-term incentives for supporting employees' financial literacy, regardless of whether they currently realize it. As stated in his written remarks, there is an "incentive to have retirees have lifetime supplementation of Social Security so that they have the capacity to consume, and therefore assist the economy, as long as they live, which is in the interest of all plan sponsors."

He also indicated that over one-third of new retirees depend *entirely* on Social Security, and two thirds get a *majority* of their income from Social Security. Moreover, data show that "as retirees age, the proportion of their income that comes from Social Security continues on a steady climb until death because the individual has not chosen to put savings into an inflation-indexed life income annuity."

His remarks are available at: <http://www.ebri.org/pdf/T-149.DOL.ERISA.19Sept07.pdf>

Health Insurance Study Finds 33% of Non-Elderly Americans Are Uninsured

On September 20, 2007, Families USA released its study titled *Wrong Direction: One Out of Three Americans Are Uninsured*. On a national basis, the study reported that 89.6 million Americans under age 65 were without health insurance at some time in the two-year period between 2006 and 2007, up from 72.5 million in the period from 1999-2000. Among those uninsured, 63.9% were without health coverage for at least six months and 50.2% were uninsured for more than nine months.

Furthermore, 79.3% of those without health coverage were in working families. Families USA Executive Director, Ron Pollack, indicated 70% of the uninsured were full-time employees who did not have health insurance offered in their workplace. The study also found that premium rates for employer-based health insurance increased 73.8% between 2000 and 2006, while wages only rose 11.6%.

The number of states with more than 33% of their non-elderly population without health insurance at some point between 2006 and 2007 increased to 20 states and the District of Columbia, up from nine states in 1999-2000. States with the highest uninsured rates were: Texas (45.5%), New Mexico (44.3%), Arizona (41.8%), California (40.5%), and Florida (40.1%).

The study is available at: <http://www.familiesusa.org/assets/pdfs/wrong-direction.pdf>

New York County Reports on Retiree Health Care Cost Containment Options

In July 2007, the Comptroller's Audit Advisory Committee of suburban New York's Nassau County issued a report titled, "*Providing Affordable Health Benefits for County Employees and Retirees: Some Suggested Solutions.*" In the report, the advisory committee identifies various options to restrain the growth in health costs without sacrificing access to high quality care. The report was prepared to help the county implement the Governmental Accounting Standards Board's Statement No. 45, related to the measurement and reporting of other postemployment benefit (OPEB) costs and liabilities. Beginning in its 2007 financial statements, Nassau County will report its OPEB liability, currently estimated to be between \$3 and \$4 billion.

According to the report, health care costs for the county's employees and retirees have increased 60% over the last five years, rising from \$151 million to \$242 million. In 2007, the total health care costs are expected to reach \$298 million, or about 10% of the county's budget and 32% of residential property taxes. Assuming an 8% annual increase in health care costs over the next three years, almost 39% of current property taxes will be required to fund employee and retiree health care. However, if the growth rate of health care costs could be halved to 4% rather than 8%, the county's cumulative savings would be roughly \$62.7 million over the next three years. Key options considered in the report (many of which would require collective bargaining) include:

- **Participant Contributions.** Currently, most county employees and retirees make no contribution for health care benefits. If employees and retirees were required to contribute toward the costs of health care premiums in the same manner as New York State employees (10% of cost for individuals and 25% of cost for dependents), the county's estimated savings would be \$129 million over the 3-year period from 2008 through 2010.
- **Benefit Plans.** Currently, the county offers a "core plus" plan, with enhancements offering greater maximum benefits and expanded coverage. If, through collective bargaining, the county could offer the core plan as the basic health care benefit package and have active employees and retirees to pay the cost difference to enroll in the enhanced plan, the county's estimated savings would be \$90 million over the 3-year period.
- **Elimination of Benefit Duplication.** A previous study recommended eliminating duplicate health coverage in cases when both spouses are county employees, and the county legislature has been doing this as collective bargaining agreements are negotiated. When completed, the county's savings over the 3-year period ending 2010 are estimated to be \$15.7 million.
- **Wellness Program.** If the county established an expanded wellness program (to include voluntary health assessments as well as educational, nutritional and disease management programs), the estimated savings over the 3-year period would be \$4 million.

The report is available at:

http://www.nassaucountyny.gov/agencies/Comptroller/NewsRelease/2007/documents/07Jul19-health_benefit_rpt.pdf