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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 the message "SUBSCRIBE NEWS SCAN" in the subject line. To stop receiving this publication electronically, send the message "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.

New York City Contributes \$2 Billion to Newly Established Retiree Health Benefit Trust Fund

On June 27, 2006, New York Mayor Michael Bloomberg and the City Council reached an agreement allocating \$2 billion of the city's \$52.9 billion fiscal 2007 budget to establish a trust fund for financing future retiree health and welfare benefits. The irrevocable trust fund was formally established after Mayor Bloomberg's approval of a council bill (Intro. No. 367) that passed with a 51-0 vote. Under the bill, the amount of funds to be deposited in the trust and the direct payment of retiree health and welfare benefits from the trust will be determined in the normal budget process. The bill also assigns the City Comptroller responsibility for auditing the trust and managing the fund's investments to ensure accountability and transparency for payments into and from the trust.

The committee report and bill text are available at: <http://www.nyccouncil.info/index.cfm> by searching for introduction bill number "367" and year "2006."

Medicare Part D Study Reports Most Enrollees Unaffected by "Donut Hole"

On June 15, 2006, the Healthcare Leadership Council released a study conducted by PriceWaterhouseCoopers, titled *Significance of the Coverage Gap Under Medicare Part D*. The study indicates that of the 43.1 million Medicare enrollees in 2006, 22.7 million (53%) are estimated to be enrolled in Medicare's prescription drug program (Part D). Another 16.2 million (38%) are estimated to have equivalent prescription drug coverage, either through their former employer or another source. The remaining 4.2 million (10%) are estimated to have no prescription drug coverage, although many are believed to qualify for the low-income Part D subsidy.

The study also found that of the 22.7 million Medicare beneficiaries with Part D coverage, 3.4 million will have prescription drug costs that exceed the threshold for the Part D coverage gap, also known as the "donut hole." Under Medicare Part D, the coverage gap occurs because a provision of Part D requires participants to pay 100% of their prescription drug costs between \$2,250 and \$5,100. According to the study, for those participants whose prescription drug costs fall within this coverage gap, total prescription drug costs average \$4,815 per

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year, of which \$2,529 is paid by the participant. The 3.4 million estimate does not include the 4.2 million people who have no prescription drug coverage.

A summary is available at: <http://www.medicaretoday.org/pdfs/HLCBrief.pdf>

CRS Finds Personal Savings Unresponsive to Tax Incentives

On June 21, 2006, the Congressional Research Service (CRS) released its report *Saving Incentives: What May Work, What May Not*. CRS indicates that the annual U.S. net national savings rate has declined from a peak of 12.4% in 1965 to a low of 0.8% in 2005. The declining personal savings rate has been linked to behavioral and economic barriers. One of the major behavioral reasons for the low savings rate is that individuals often do not make optimal decisions concerning consumption and savings. The government has offered tax incentives to encourage personal savings, but research has shown that tax incentives tend to favor those with higher incomes rather than with lower incomes. Higher-income individuals are more likely to save, since they have higher marginal tax rates and benefit more from sheltering income from taxation.

However, while tax incentives may marginally affect personal savings, they typically lower overall public savings by reducing the federal budget surplus or increasing the budget deficit. In fiscal year 2006, the tax revenue loss due to current tax incentives cost the U.S. Treasury an estimated \$125.6 billion (almost 40% of the 2006 federal budget deficit). CRS cautioned that any changes to federal tax policy should include an analysis of the aggregate effects of savings incentives on both public and personal savings, since increasing personal savings could decrease public savings. The report also warned that “the long-term net effect of tax incentives on national savings and economic growth is likely negative.”

Source: BNA *Pension and Benefits Reporter*, June 27, 2006.

CRS Reports on Social Security Insolvency

On July 3, 2006, the Congressional Research Service (CRS) released its report, *Social Security: What Would Happen If the Trust Funds Ran Out*. Based on the 2006 Social Security Trustees Report, CRS found that the Social Security trust funds are projected to be exhausted in 2040, and the Social Security program would have a \$4.6 billion shortfall in present value terms by 2080.

In its report, CRS urged Congress to act promptly to restore Social Security solvency since the sooner Congress acts, the smaller the necessary tax increases or benefit reductions would need to be. If Congress delays action until insolvency, the annual trust fund deficits could be eliminated by reducing benefits by about 26% in 2041, with the reduction gradually increasing to 30% in 2080. Alternatively, to pay full Social Security benefits after insolvency, the Social Security payroll tax rate could be increased from 12.40% to 16.65% in 2040 gradually rising to 17.78% in 2080.

CRS clarified that insolvency would not mean that Social Security would be completely bankrupt and unable to pay any benefits. Instead, because the Antideficiency Act prohibits government spending in excess of available funds, full Social Security benefits would likely be reduced or delayed. If this were to happen, Congress or the courts would need to resolve the legal conflict between benefit entitlement and the Antideficiency Act.

The CRS report is available for a fee from BNA PLUS at:
<http://www.library.vcu.edu/tml/docsupp/bnaplus.html>

Kaiser Family Foundation Releases Latest Report on Prescription Drug Trends

In June 2006, the Kaiser Family Foundation released the latest in its series of reports on prescription drug trends. The analysis describes various factors that underlie increases in prescription drug costs, as well as recent public- and private-sector responses intended to curb the increases. Overall, however, the analysis projects prescription drug spending in the U.S. will grow from \$188.5 billion in 2004 to \$446.2 billion in 2015, an increase of 138%. Drug spending as a percent of overall health care spending is also expected to increase from 10% in 2004 to 11% in 2015. The key factors affecting prescription drug spending include:

- **Increased Utilization:** From 1994 to 2005, the number of total prescriptions purchased increased 71%, rising from 2.1 billion to 3.6 billion, compared to U.S. population growth of 9%;
- **Increased Prices:** During the same period, retail prescription prices grew from an average of \$28.67 to \$64.86, an increase of 8.3% or more than triple the average inflation rate of 2.5%; and
- **Changes in Types of Drugs:** Prescription drug spending is also affected when new drugs are approved by the FDA and when brand-name drugs lose patent protection and compete with lower cost generic drugs. This has fluctuated over the past decade.

Public- and private-sector responses to increasing drug costs have evolved a number of strategies, including:

- **Discounts and Rebates:** Many prescription drug programs use pharmacy benefit managers (PBMs) to negotiate with drug manufacturers for discounts and rebates based on volume and market share. In addition many federal governmental programs (including Veterans Affairs, the Defense Department, and Medicaid) purchase drugs from manufacturers at prices that are equal to or lower than those charged to non-federal purchasers.
- **Purchasing Pools:** Under this approach, some public and private entities have grouped their prescription drug purchases to pool their risks and obtain a competitive advantage when purchasing prescription drugs.
- **Utilization Management:** According to the report, health plans have also worked to control drug costs by excluding certain drugs from coverage, establishing dispensing limits, and increasing enrollee cost-sharing. In 2005, 74% of employer-sponsored prescription drug plans had cost-sharing arrangements including three or four tiers, up from 27% of plans in 2000.

Although the Medicare Part D program is legislatively prohibited from negotiating drug prices directly with manufacturers, the Department of Health and Human Services (HHS) estimates that the private Part D drug plans will be able to negotiate prices/rebates that are greater than originally expected (i.e., 27% instead of 15%).

The report is available on the Kaiser web site at: <http://www.kff.org/rxdrugs/upload/3057-05.pdf>

FDA Approval of Generic Drugs May Provide Substantial Savings

In June 2006, the Food and Drug Administration (FDA) approved generic versions of four of the ten best-selling prescription drugs treating such common ailments as high cholesterol and asthma. The FDA projected that the four generic alternatives will generate savings of about \$1 billion per year for consumers, employers, and the Medicare drug plan. The four brand-name drugs are due to lose patent protection starting in 2006 through 2010.

As reported in the Los Angeles Times on July 15th, over 50% of prescription drugs have generic versions today, up from about 25% in 1986. Express Scripts Inc., a leading pharmacy benefits manager, estimates the potential savings from generics will be \$24.7 billion in 2006, since generic drugs can cost as much as 80% less than branded versions.

Drug companies generally have 12 to 14 years of exclusive rights to sell the drugs after obtaining FDA approval. The current increase in generic drugs is due to the many blockbuster medicines developed by drug manufacturers in the early 1990s. As the patent protection period comes to a close, a record number of brand drugs, with annual sales of about \$75 billion, will lose their patents in the next few years.

Some pharmaceutical companies are responding to the loss of patent protection by selling “authorized generics” which are either licensed or manufactured by the companies and marketed under private labels. In order to ensure this approach does not undermine competition, the Federal Trade Commission (FTC) is studying the impact of authorized generics. Also, in the near future, the FDA is planning to establish a “hierarchical approach” for reviewing generic products more efficiently in an effort to increase access to safe and effective generic drugs.

Source: Los Angeles Times, July 15, 2006.

AARP Publishes Survey of Retirement Planning Among U.S. Adults Age 40 and Older

On June 28, 2006, the AARP published its report: *Retirement Planning Survey Among U.S. Adults Age 40 and Older*, based on telephone conversations with a national sample of 1,782 adults age 40 and older, including 686 retirees. It found that only 35% of those surveyed felt “very confident” that they would have enough money to live comfortably throughout retirement. According to the report:

- 28% of workers and 12% of retirees are not confident about having enough money in retirement to pay their medical expenses;
- 40% of workers and 33% of retirees are not confident about having enough money to pay long-term care expenses; and
- 15% of workers and 9% of retirees are not confident about having enough money to take care of basic expenses.

The survey also requested information about the steps people have taken to secure their retirement. Of the working respondents, 68% indicated that they have saved money for retirement, with median savings of less than \$25,000 (excluding the value of their residence).

Most of the responding workers expect to obtain their retirement income to come primarily from employer-provided retirement benefits, including 401(k) plans (44%) and pension plans (35%). However, 40% are also worried that their employers will cut back on retirement income or health care benefits before or during their retirement. In some of the cases, the workers reported that employers had already eliminated (10%) or frozen (9%) their pension benefits. In 44% of the cases, the employer had reduced retiree health care benefits.

The report is available at: http://assets.aarp.org/rgcenter/econ/ret_planning.pdf

GM Chairman Testifies Before Congress on Changes to U.S. Health Care System

On July 13, 2006, General Motors Chairman and CEO, G. Richard Wagoner, testified before the U.S. Senate Special Committee on Aging regarding the cost of health care for employees and retirees. As reported in BNA’s July 18th *Pension & Benefits Reporter*, Wagoner indicated that the rising cost of health care is prompting U.S. corporations to turn to Congress for assistance in changing the nation’s health care system. While arguing against mandating health care for employers, he called upon the federal government to do more to reduce health care costs, including support for a “vigorous and robust competitive prescription drug market.” He also called for more federal support related to better health care education for employees and retirees in order to identify effective health care providers and better prevent and manage chronic illnesses.

Source: BNA *Pension and Benefits Reporter*, July 18, 2006.

U.S. Senate Finance Committee Requests GAO Study of Public Pension Funding

On July 10, 2006, Senator Charles Grassley (R-IA), chairman of the U.S. Senate Finance Committee, and ranking committee member Max Baucus (D-MT) requested that the U.S. Government Accountability Office (GAO) study the current funded status of public pension plans. Indicating their concern that public plans may be poorly funded, the senators requested that the GAO research the following questions:

- What is the general financial health of state and local government defined benefit plans, and how has it changed over the last decade?
- How widespread is the provision of retiree health care benefits by state and local government employers, and what is the funded status of these plans?
- To what extent will recent changes in the applicable accounting standards affect the funding of state and local pension and retiree health care plans?
- What are the implications of these trends for state and local employee retirement security and retirement security generally?

The request echoes statements made this February by Chicago Federal Reserve Bank President, Michael Moskow, who criticized state and local retirement plans as being poorly funded and suggested that public plans be governed by federal legislation similar to the Employee Retirement Income Security Act (ERISA), which currently governs private-sector plans. Representatives of Gabriel, Roeder, Smith & Company (GRS) and the National Association of State Retirement Administrators (NASRA) responded to Mr. Moskow's comments in a letter posted on the NASRA web site at: www.nasra.org.

A copy of the Senate Finance Committee's letter to the GAO is available at: <http://finance.senate.gov/>