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Notes

EXECUTIVE SUMMARY

Target-Date Fund Use Over Time

IMPORTANCE OF TDFs: The use of target-date funds (TDFs) in 401(k) plans has grown rapidly in recent years: The percentage of all 401(k) plan participants using them increased from 25 percent in 2007 to 31 percent in 2008. Use of these funds has been more likely among participants who are young, have lower account balances and shorter tenure at their current job, as new workers are the most likely to be auto-enrolled in their employer's 401(k) plan. Because TDFs are still relatively new for most participants, little is known how participants use these funds over time.

PARTICIPANTS STICKING WITH TDFs: Data from the EBRI/ICI 401(k) database for 2007–2008 show that 401(k) plan participants who use TDFs have a very high likelihood (94 percent) of remaining in these funds the following year. Future growth can be expected in TDFs as the participants in target-date funds remain in them, and as new participants sign up for them voluntarily or through a default option. Therefore, the design of TDFs (especially the investment allocation "glide path"), as well as participants' understanding of these funds, will become more critical to the future success of 401(k) plans.

The Early Retiree Reinsurance Program: $5 Billion Will Last About Two Years

PPACA'S EARLY RETIREE REINSURANCE PROGRAM: The Patient Protection and Affordable Care Act (PPACA) of 2010 created a temporary reinsurance program for sponsors of employment-based health plans that provide retiree health benefits to retirees who are over age 55 and not yet eligible for the Medicare program. The program provides an 80 percent subsidy for retiree claims of between $15,000 and $90,000. Congress appropriated $5 billion for the program, which is effective June 1, 2010, and the subsidy will be available through the earlier of Jan. 1, 2014, or the date when the funds are exhausted.

EMPLOYER INCENTIVE: One goal of the program is to provide an incentive for employers to maintain retiree health benefits and assist retirees with their costs for health coverage. Under the early retiree reinsurance program, plan sponsors must be able to show that the subsidies were not used to reduce their level of support for the plan. Subsidies can be used to reduce retiree costs, and sponsors must also show that the subsidies were used to generate savings or had the potential to generate savings.

EXHAUSTION LIKELY WITHIN TWO YEARS: An important question is whether the $5 billion will be exhausted before 2014. This article finds that if the subsidy were drawn down for all early retirees and their dependents, $2.5 billion of the $5 billion available would be exhausted in the first year of the program. The $5 billion would last no more than two years and would not be available in 2012 or 2013.

Target-Date Fund Use Over Time

by Craig Copeland, Employee Benefit Research Institute

Introduction

The use of target-date funds (TDFs) in 401(k) plans has increased rapidly in recent years. The percentage of all 401(k) plan participants using TDFs increased from 25 percent in 2007 to 31 percent in 2008.[1] One of the reasons for this growth is that TDFs have been a popular choice for the default fund when 401(k) plans have an auto-enrollment feature. Consequently, use of these funds has been found to more likely occur among younger participants, participants with lower account balances, and participants with shorter tenure at their current job, as new workers are the most likely to be auto-enrolled in their employer's 401(k) plan.[2]

This study examines the persistence of use of TDFs among those who were using these funds in 2007. Therefore, the percentage of participants who remain in these plans is determined, as well as the percentage of participants who added TDFs among those not already using them in 2007. The analysis is focused on 401(k) participants who were in plans that offered TDFs in 2007 to see whether they remained in TDFs, moved out of TDFs, or moved into TDFs if they were not already using them.

Data

This study uses the unique richness of the data in the EBRI/ICI Participant-Directed Retirement Plan Data Collection Project, which in 2007 had 21.8 million participants from 56,232 plans across a spectrum of plan administrators.[3] In this database in 2007, 67.3 percent of the plans offered target-date funds as an investment option. This study focuses on only those 401(k) participants identified as being in plans that *offered* target-date funds, as the goal is to examine participants' choices when target-date funds are offered. In addition to the 2007 data, all participants in the database in 2008 who were in the plans that were identified as offering TDFs in 2007 were included to create a longitudinal database from 2007 to 2008 of participants who were in plans offering TDFs in 2007.

Use of TDFs

In 2007, of those participants who were in a plan that offered a TDF in 2007 and were still in the database in 2008, 36.0 percent had at least some of their account balance in TDFs (Figure 1). By 2008, of this same group of participants, 39.8 percent had at least some of their account balance in TDFs. Furthermore, of those participants having an allocation to TDFs in 2007, 93.9 percent still had some of their account balance allocated to TDFs in 2008. Nearly 10 percent of participants who were in a plan in 2007 that offered TDFs but did not use them in 2007 were using them in 2008.

Participants who were younger, had shorter tenure, or lower account balances were more likely to remain in a TDF and were more likely to begin using them in 2008 (Figure 1). Furthermore, participants with the lowest salaries were more likely to stay in TDFs and begin using them in 2008. However, as salaries increased, there was no significant difference in new TDF use.

For participants in larger plans, the likelihood of new TDF use in 2008 increased, but the probability of continuing use showed very little change across plan sizes. In plans with 1−10 participants, 94.8 percent of those using TDFs in 2007 still had dollars allocated to them in 2008, compared with 93.0 percent of those in plans with more than 10,000 participants.

The participants most likely to <u>stop</u> using TDFs and least likely to <u>start</u> using them if they haven't already done so are those with the highest levels of tenure and the highest account balances (Figure 1). Of those participants in 2007 with 30 or more years of tenure and having some of their account balance allocated to TDFs, 85.8 percent continued to have some assets in TDFs in 2008. For comparison, of participants in 2007 with two−five years of tenure, 95.5 percent remained allocated to TDFs in 2008 after having done so in 2007.

401(k) plan participants in TDFs in both 2007 and 2008 were younger than those who did not use them when they were an option (Figure 2). The average age of those participants using TDFs in 2007 was 43.1 and in 2008 it was 42.4, compared with 45.6 and 46.2, respectively, for those participants not using TDFs. The average age for those using TDFs in both years was 42.9.

Participants using TDFs had lower average salaries, shorter average tenure, lower average account balances, and, on average, were in smaller plans based on number of participants, than participants who did not use TDFs (Figure 2). Correspondingly, the participants who used TDFs in both years had, on average, lower salaries, shorter tenure, and lower account balances, and were in smaller plans.

Conclusion

401(k) plan participants who use TDFs have a very high likelihood (94 percent) of remaining in these funds the following year. Younger and shorter-tenure workers are the most likely to use these funds and remain in them. Consequently, future growth can be expected in these plans as the participants in them remain in them and as new participants begin using them. Therefore, the design (glide path, initial and final equity allocation, etc.) of the TDFs, as well as the participants' understanding of these funds, will be more critical to the success of 401(k) plans.

TDFs have been evolving and are likely to continue to evolve. This evolution of TDFs is due to participants' differences in longevity, risk tolerance, savings outside of the retirement plan, planning horizon, and a myriad of other factors, as well as changing market conditions. Therefore, finding the best fund for a 401(k) plan's participants should be the goal when picking the target-date fund offerings, not standardizing the funds across all providers of these funds. However, the ability of many participants to understand these issues is limited—which is why automatic enrollment and default investments were encouraged under PPA—so more guidance and explanation is likely to be needed.[4]

A critical factor is that of the "glide path" (the reallocation of equities over time as the current year becomes closer to the target date year) and where the reallocation stops. One fund using a 50 percent equity allocation when the target year is very close to the current year has very different risk/return characteristics than another fund with the same target year but using a 20 percent equity allocation. Therefore, participants must determine the goal for their money at retirement: Is it for further accumulation, or preservation and income generation?

The sharp market downturn at the end of 2008 that continued into 2009 dramatically highlighted some of these issues for TDF investors, due to the investment losses they suffered. Given that experience, a re-examination of TDF usage in another two years may show a decline in the near-complete retention of these funds found between 2007–2008. Furthermore, some target-date funds changed their investment glide paths in response to the market downturn, which could contribute to different responses by participants in 2009 than those that were found in 2008. When data are available for 2009, a study will be conducted to determine whether this very high persistence level of TDF use remains.

Endnotes

[1] See Jack VanDerhei, Sarah Holden, Luis Alonso, and Craig Copeland, "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2007," *EBRI Issue Brief,* No. 324, and *ICI Perspective,* Vol. 14, no. 3 (Employee Benefit Research Institute and Investment Company Institute, December 2008); and Jack VanDerhei, Sarah Holden, and Luis Alonso, "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2008." *EBRI Issue Brief,* No. 335, and *ICI Perspective,* Vol. 15, no. 2 (Employee Benefit Research Institute and Investment Company Institute, October 2009) for more detail on overall asset allocation in 401(k) plans.

[2] See Craig Copeland, "Use of Target Date Funds in 401(k) Plans, 2007," *EBRI Issue Brief,* No. 327 (Employee Benefit Research Institute, March 2009) for an extensive examination of TDF use in 2007, including asset allocation in the funds as well as asset allocation of participants who use TDFs along with other investment options in their 401(k) plan.

[3] The EBRI/ICI Participant-Directed Retirement Plan Data Collection Project is the largest, most representative repository of information about individual 401(k) plan participant accounts. As of December 31, 2007, the EBRI/ICI database includes statistical information about 21.8 million 401(k) plan participants, in 56,232 employer-sponsored 401(k) plans, holding $1.425 trillion in assets. The 2007 EBRI/ICI database covers 45 percent of the universe of 401(k) plan participants, 12 percent of plans, and 47 percent of 401(k) plan assets. The EBRI/ICI project is unique because of its inclusion of data provided by a wide variety of plan recordkeepers and, therefore, portrays the activity of participants in 401(k) plans of varying sizes—from very large corporations to small businesses—with a variety of investment options. See VanDerhei, Holden, Alonso, and Copeland (2008), op. cit., for overall asset allocation of the participants in the database in 2007 and VanDerhei, Holden, and Alonso (2009), op. cit., for the overall asset allocation in the database for 2008.

[4] In fact, the U.S. Securities and Exchange Commission (SEC) is proposing new rules for target-date funds that will address many of these issues. See the SEC press release for further information about the proposed rules, at www.sec.gov/news/press/2010/2010-103.htm

Figure 1

Percentage of 401(k) Plan Participants Who Were in a Plan That Offered Target-Date Funds in 2007 Who Used Them in 2007, 2008, and Both Years, by Various Factors

	Percentage With Target-Date Fund When Offered, 2007	Percentage With Target-Date Fund When Offered, 2008	Percentage With Target-Date Fund When Offered, 2007 and 2008	Percentage of Those With Target-Date Funds in 2007, Having Them in 2008	Percentage of Those Without Target-Date Funds When Offered in 2007, Having Them in 2008
Age					
All	36.0%	39.8%	33.8%	93.9%	9.4%
Under 30	43.7	57.1	42.1	96.5	26.6
30–39	40.7	44.2	38.7	95.1	9.4
40–49	35.1	37.8	33.0	94.0	7.5
50–59	32.8	34.8	30.2	92.0	7.0
60 or Older	27.3	28.3	24.6	90.1	5.2
Salary[a]					
<$20,000	49.9	56.8	48.1	96.3	17.3
$20,000–$39,999	43.5	47.6	40.7	93.5	12.2
$40,000–$59,999	38.9	44.1	36.1	92.9	13.1
$60,000–$79,999	38.2	42.4	35.5	93.0	11.2
$80,000–$99,999	38.1	42.4	35.6	93.3	11.1
$100,000 or more	37.3	40.4	34.5	92.4	9.4
Tenure[b]					
Less than 2 years	49.6	56.0	47.5	95.7	16.9
2 to less than 5 years	42.6	48.3	40.6	95.5	13.3
5 to less than 10 years	34.9	38.3	32.7	93.8	8.5
10 to less than 20 years	28.9	31.9	26.7	92.5	7.3
20 to less than 30 years	25.3	27.1	22.6	89.3	6.0
30 or more years	20.6	21.8	17.7	85.8	5.1
Account Balance					
<$5,000	45.1	52.6	43.8	97.1	16.0
$5,000–$9,999	42.5	46.0	40.4	95.1	9.7
$10,000–$19,999	36.8	39.6	34.7	94.1	7.8
$20,000–$39,999	32.9	35.2	30.5	92.8	7.0
$40,000–$59,999	30.8	33.0	28.3	91.8	6.7
$60,000–$99,999	29.4	31.5	26.7	90.8	6.8
$100,000–$199,999	28.0	29.9	25.0	89.5	6.8
$200,000 or more	24.7	26.4	21.3	86.3	6.7
Plan Size (number of participants)					
1–10	47.7	48.0	45.2	94.8	5.3
11–25	39.2	40.2	37.1	94.6	5.2
26–50	38.2	39.7	36.0	94.4	6.0
51–100	38.0	39.6	36.0	94.7	5.9
101–250	39.6	41.2	37.4	94.4	6.4
251–500	38.6	40.9	36.5	94.8	7.2
501–1,000	38.8	40.9	36.4	93.9	7.4
1,001–2,500	35.5	38.3	33.3	93.8	7.9
2,501–5,000	38.1	42.1	36.2	95.1	9.6
5,001–10,000	39.6	42.6	37.1	93.6	9.1
> 10,000	32.2	37.8	29.9	93.0	11.6

Source: EBRI tabulations from the EBRI/ICI Participant-Directed Retirement Plan Data Collection Project.

[a] This category includes only the observations with salary information.

[b] This category includes only those observations with tenure data.

Note: Categries are based on the particpant's status in 2007. “Funds” include mutual funds, bank collective trusts, life insurance separate accounts, and any pooled investment product primarily invested in the security indicated.

Figure 2

Distribution of 401(k) Plan Participants Who Were in a Plan That Offered Target-Date Funds in 2007, and Who Used Them in 2007 and 2008, by Various Factors, and the Average Amount of Each Factor

	Distribution of All Participants With Access to Target-Date Funds, 2007	Distribution of Those Not Investing In Target-Date Funds, 2007	Distribution of Those Investing in Target-Date Funds, 2007	Distribution of Those Not Investing In Target-Date Funds, 2008	Distribution of Those Investing in Target-Date Funds, 2008	Distribution of Those Investing In Target-Date Funds, 2007 and 2008
	Average/Percentage					
Age (years)	*44.7*	*45.6*	*43.1*	*46.2*	*42.4*	*42.9*
All	100%	100%	100%	100%	100%	100%
Under 30	11.3	9.9	13.6	8.0	16.1	14.0
30–39	23.5	21.8	26.5	21.8	26.1	26.9
40–49	30.1	30.5	29.3	31.1	28.6	29.3
50–59	25.4	26.7	23.1	27.5	22.2	22.7
60 or Older	9.8	11.1	7.4	11.7	7.0	7.1
Salary[a]	*$56,412*	*$60,845*	*$50,309*	*$62,205*	*$49,848*	*$49,726*
<$20,000	21.1%	18.3%	25.1%	17.2%	25.6%	25.7%
$20,000–$39,999	25.6	25.0	26.5	25.3	26.0	26.4
$40,000–$59,999	20.9	22.1	19.3	22.0	19.7	19.1
$60,000–$79,999	13.1	13.9	11.8	14.2	11.8	11.7
$80,000–$99,999	7.8	8.3	7.1	8.4	7.1	7.0
$100,000 or more	11.5	12.4	10.2	12.9	9.9	10.0
Tenure[b] (years)	*10.5*	*11.6*	*8.4*	*11.9*	*8.3*	*8.2*
Less than 2 years	10.5%	8.2%	14.9%	7.6%	15.1%	15.2%
2 to less than 5 years	24.2	21.4	29.3	20.5	30.0	29.9
5 to less than 10 years	25.7	25.8	25.6	26.0	25.3	25.6
10 to less than 20 years	23.2	25.4	19.1	25.9	19.0	18.9
20 to less than 30 years	10.8	12.5	7.8	12.9	7.5	7.5
30 or more years	5.6	6.8	3.3	7.1	3.1	3.0
Account Balance	*$66,295*	*$76,009*	*$49,041*	*$78,595*	*$47,700*	*$46,421*
<$5,000	27.8%	23.9%	34.9%	21.9%	36.8%	36.1%
$5,000–$9,999	9.8	8.8	11.6	8.8	11.4	11.7
$10,000–$19,999	12.3	12.2	12.6	12.4	12.3	12.6
$20,000–$39,999	13.6	14.2	12.4	14.6	12.0	12.2
$40,000–$59,999	8.0	8.7	6.9	8.9	6.6	6.7
$60,000–$99,999	9.6	10.5	7.8	10.9	7.6	7.5
$100,000–$199,999	10.6	11.9	8.2	12.3	7.9	7.8
$200,000 or more	8.3	9.8	5.7	10.2	5.5	5.3
Plan Size (number of participants)	*14,955*	*17,138*	*11,078*	*16,911*	*11,997*	*10,956*
1–10	0.3%	0.3%	0.4%	0.3%	0.4%	0.4%
11–25	1.2	1.1	1.3	1.2	1.2	1.3
26–50	1.9	1.8	2.0	1.9	1.9	2.0
51–100	2.8	2.7	3.0	2.8	2.8	3.0
101–250	5.5	5.2	6.0	5.4	5.7	6.1
251–500	5.9	5.7	6.3	5.8	6.1	6.4
501–1,000	7.6	7.2	8.2	7.4	7.8	8.2
1,001–2,500	13.1	13.2	12.9	13.4	12.6	12.9
2,501–5,000	13.9	13.5	14.7	13.4	14.7	14.9
5,001–10,000	12.2	11.5	13.4	11.6	13.0	13.4
> 10,000	35.6	37.8	31.8	36.8	33.8	31.5

Source: EBRI tabulations from the EBRI/ICI Participant-Directed Retirement Plan Data Collection Project.

[a] This category includes only the observations with salary information.

[b] This category includes only those observations with tenure data.

Note: Categries are based on the particpant's status in 2007. “Funds” include mutual funds, bank collective trusts, life insurance separate accounts, and any pooled investment product primarily invested in the security indicated.

The Early Retiree Reinsurance Program: $5 Billion Will Last About Two Years

by Paul Fronstin, Employee Benefit Research Institute

Introduction

The Patient Protection and Affordable Care Act (PPACA) of 2010 created a temporary reinsurance program for sponsors[1] of employment-based health plans that provide retiree health benefits to retirees who are over age 55 and not yet eligible for the Medicare program. The program can also be used to cover costs associated with a retiree's spouse, surviving spouse, and dependents, even if they are under 55 and/or eligible for Medicare. The program provides an 80 percent subsidy for retiree claims of between $15,000 and $90,000.[2] Congress appropriated $5 billion for the program, which became effective June 1, 2010. The subsidy will be available through the earlier of Jan. 1, 2014, or the date when the funds are exhausted.

One goal of the program is to provide an incentive for employers to maintain retiree health benefits and assist retirees with their costs for health coverage. Between 1993 and 2001, the percentage of employers with 500 or more employees offering health benefits to early retirees fell from 46 percent to 29 percent (Figure 1). Since 2001, the percentage offering coverage has remained stable, although cost sharing for workers has been increasing in these plans. In the absence of the PPACA program, cost sharing could be expected to continue to increase in order to reduce or keep constant sponsor costs for retiree health coverage. Under the early retiree reinsurance program, sponsors must be able to show that the subsidies were *not* used to reduce their level of support for the plan. Subsidies can be used to reduce retiree costs, and sponsors must also show that the subsidies were used to generate savings or had the potential to generate savings.

An important question is whether the $5 billion will be exhausted before 2014. This article tries to answer that question. It starts by examining the work status of the population ages 55–64. It analyzes the sources of this population's health coverage. Employer spending for health care services is then examined.

It was found that if the subsidy were drawn down for all early retirees and their dependents, $2.5 billion of the $5 billion available would be exhausted in the first year of the program. The $5 billion would last no more than two years and would not be available in 2012 or 2013.

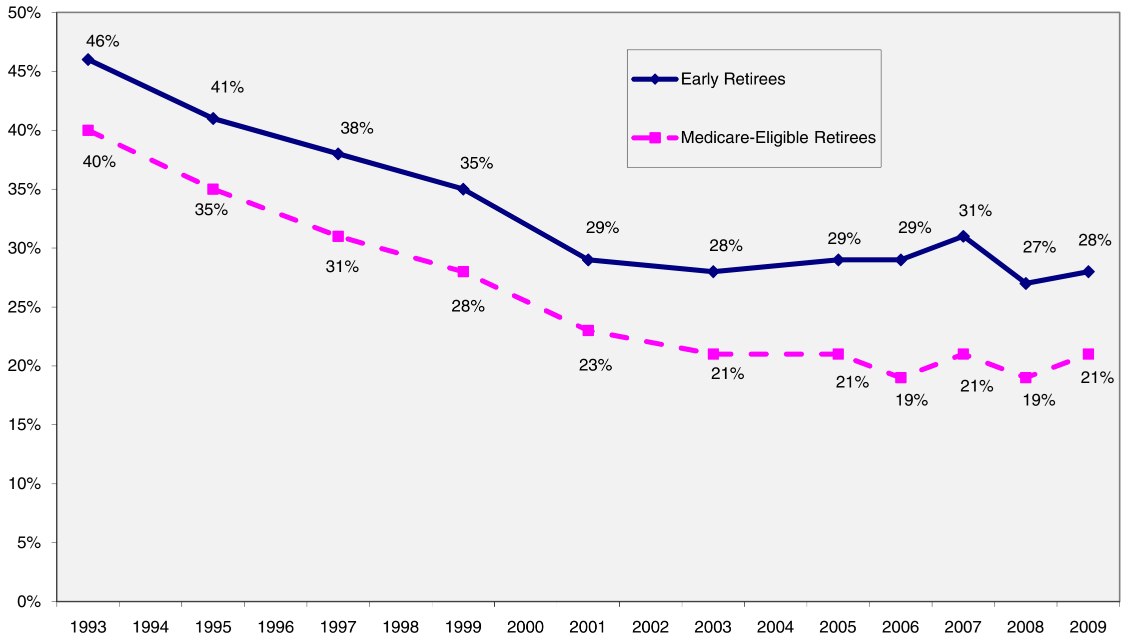
Estimating Retiree Health Care Costs

In order to determine aggregate subsidy amounts that sponsors will qualify for, a number of variables must be examined. They include:

- The number of eligible individuals with retiree health benefits. These were expected to be nonworking retirees, but there may be some retirees in the group who went back to work and continue to receive health benefits through their former employer.
- The number of eligible spouses and dependents.
- The distribution of health spending for all eligible individuals.

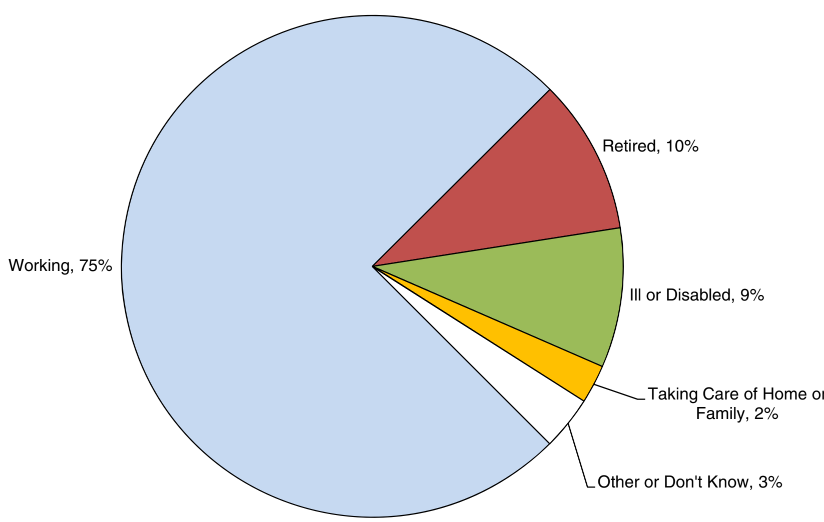
The data for this study come from two sources: the 2007 Medical Expenditure Panel Survey (MEPS) and the 2004 panel of the Survey of Income and Program Participation (SIPP). MEPS is conducted by the Agency for Health Care Research and Quality, part of the Department of Health and Human Services. It is a nationally representative survey of the U.S. civilian noninstitutionalized population that provides estimates for the number of nonworkers with health coverage through a former employer, the portion of those nonworkers who are also covered by Medicare, annual health care expenditures, and the portion of expenditures paid out of pocket and by source of insurance coverage. Annual health

Figure 1
Percentage of Employers With 500 or More Employees Offering Health Insurance to Retirees, 1993–2009



Source: Mercer National Survey of Employer-Sponsored Health Plans.

Figure 2
Work Status, Individuals Ages 55–64, 2007



Source: Employee Benefit Research Institute estimates from the 2007 Medical Expenditure Panel Survey.

care expenditures and the portion paid out of pocket and by source of insurance coverage are also provided for their dependents when covered by the same health plan.

SIPP is conducted by the U.S. Census Bureau and is used to provide data on the portion of nonworkers with coverage through a former employer who are covered by COBRA (the Consolidated Omnibus Budget Reconciliation Act of 1985). It is also used to determine the portion of workers ages 55–64 who have coverage through a former employer.

Because data on health care expenses come from MEPS and data on COBRA coverage and workers with retiree health benefits come from SIPP, a number of simplifying assumptions are made:

- The distribution of health care expenses for individuals and their dependents through a former employer is the same for those with retiree health benefits and those with COBRA.
- The distribution of health care expenses for individuals with retiree health benefits is the same for workers and nonworkers.

Furthermore, because the MEPS data are from 2007, health care expenses were inflated based on premium increases in 2008 and 2009, and expected premium increases for 2010 as reported by Mercer.[3]

According to EBRI estimates from MEPS, there were 34.5 million people ages 55–64 in the United States in 2007. Three-quarters of this population were working, 10 percent were not working because they considered themselves retired, 9 percent were not working because of their health status, and 2 percent were taking care of their home or family (Figure 2). MEPS was unable to determine the work status and reasons not working for about 3 percent of the population. The 10 percent who were retired represent 3.5 million individuals, and the 9 percent who were not working because of their health status represent 3.1 million individuals. Prior research has shown that the number of nonworkers ages 55–64 with coverage through a former employer has remained relatively stable, so it can be assumed that these numbers are valid in 2010.[4]

Among the population ages 55–64, 47 percent had health coverage through their own employer or through a former employer, 25 percent were covered through an employer as a dependent, 3 percent purchased coverage on their own, 7 percent had Medicare, 4 percent had Medicaid, and 12 percent were uninsured (Figure 3).

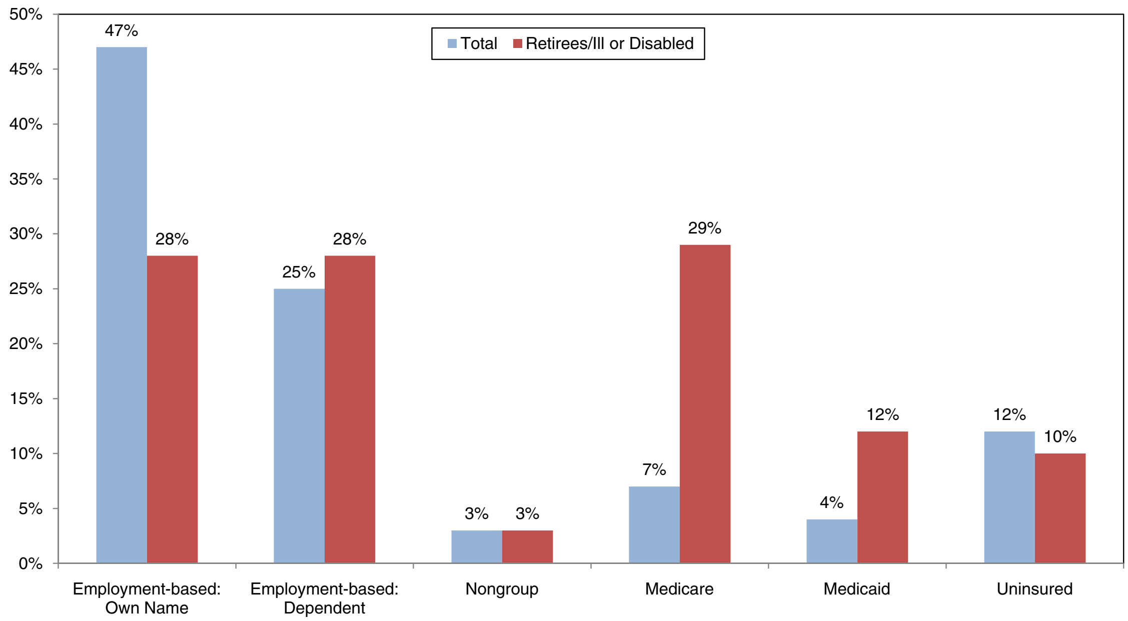
The distribution of health coverage for the 6.6 million individuals who were either retired or did not work because of their health status was different from the rest of the 55–64 population. Fewer have employment-based coverage and a greater percentage was covered either by Medicare or Medicaid.

Individuals can have more than one source of coverage in MEPS. About 6 percent of retirees and persons not working because of their health status were covered both through their former employer and by Medicare. Reinsurance is not available for these individuals, even if an employer is paying part of the cost of their health care, because they are covered by the Medicare program. Overall, of the 6.6 million individuals who are either retired or do not work because of their health status and who had coverage through a prior employer, 1.3 million had coverage through a former employer and were not also covered by Medicare.

One issue with using the 1.3 million estimate is that some retirees with coverage through a former employer may be covered by COBRA and not their former employer's retiree health benefits. EBRI estimates from SIPP indicate that 47 percent of individuals ages 55–64 with coverage through a former employer were covered by COBRA, and 53 percent had retiree health benefits. Thus, employers covered about 670,000 early retirees through retiree health programs (Figure 4). An additional 290,000 dependents were covered as well.

According to SIPP, 1 percent of workers ages 55–64 have retiree health benefits through a former employer, which accounts for about 260,000 individuals. Assuming these workers have policies that cover the same number of dependents proportionately as do nonworkers with retiree health benefits, another 110,000 dependents of workers have coverage through a retiree health benefits program.

Figure 3
Sources of Health Insurance, Individuals Ages 55–64, 2007



Source: Employee Benefit Research Institute estimates from the 2007 Medical Expenditure Panel Survey.

Figure 4
Predicted Number of Individuals With Retiree Health Benefits, Average Spending, Distribution of Spending, and Estimated Subsidies, 2010

	Population With Retiree Health Benefits Eligible for Subsidy	Average Employer Spending	Aggregate Employer Costs	Aggregate Employer Costs Below $15,000	Aggregate Employer Costs $15,000 or More	Aggregate Annual Subsidy
	(millions)		(millions)	(millions)	(millions)	(millions)
Total	1.3	$7,213	$9,653	$3,959	$5,695	$2,544
Retirees (ages 55–64) with retiree health benefits	0.7	7,600	5,107	2,011	3,097	1,388
Dependents of retirees	0.3	6,300	1,860	846	1,013	443
Workers (ages 55–64) with retiree health benefits	0.3	7,600	1,969	775	1,194	537
Dependents of Workers	0.1	6,300	718	327	391	176

Source: Employee Benefit Research Institute estimates based on data from the 2007 Medical Expenditure Panel Survey and the 2004 panel of the Survey of Income and Program Participation.

Thus, overall, early retiree health benefit programs cover 1.3 million people, either as retirees (ages 55−64) or their spouses and dependents (any age), and some of the retirees have jobs. Figure 4 provides a breakdown of the 1.3 million individuals covered by retiree health benefits, by work status and dependent status.[5]

Medical Expenses—The 2007 MEPS contains annual spending on health care for each nonworker with coverage through a former employer. Spending for dependents also covered by the retiree health plan is also available. Only employer-paid expenses are examined. Retiree out-of-pocket spending is excluded from this analysis because in order for an employer to receive credit for the cost-sharing amounts paid by the early retiree (or their spouse, surviving spouse, or dependent), the sponsor must provide evidence that the cost-sharing amount was actually paid. If evidence is not provided by the sponsor, it may not receive subsidies based on out-of-pocket spending.

Figure 4 provides a summary of predicted average employer spending, aggregate employer spending, the distribution of aggregate employer spending, and potential subsidies from the early retiree reinsurance program. The table provides separate estimates for individuals not working with retiree health benefits and their covered dependents. It also provides separate estimates for retirees who are working and have coverage through a former employer and their covered dependents.

Overall, employers paid an average of $7,600 per retiree and $6,300 per dependent. About 87 percent of nonworking retirees did not incur claims (not including cost sharing) above $15,000, and those claims accounted for 39 percent of total employer costs. The 13 percent of retirees incurring claims of $15,000 or more accounted for 61 percent of all claims. In aggregate, employer costs for these claims were $5.1 billion, of which $2 billion went to claims below $15,000 and $3.1 billion went to claims of $15,000 or more. Subsidizing 80 percent of the cost of claims between $15,000 and $90,000 would yield $1.4 billion in subsidies in the first year of the program for early retirees.

In addition to the 700,000 retirees with coverage through a former employer's retiree health benefits program, about 300,000 of their dependents were covered. Nearly all of the dependents were spouses, as only 3 percent of the dependents were under age 18. The age of spouses ranged from 41 to 77, with about one-quarter of the dependents age 65 or older. Ninety percent incurred expenses below $15,000, but these expenses accounted for 46 percent of employer spending for dependents. The 10 percent with costs of $15,000 or above accounted for 54 percent of expenses. Subsidizing 80 percent of the cost of claims between $15,000 and $90,000 would yield an additional $443 million in subsidies in the first year of the program.

Workers with retiree health benefits would yield about $537 million in subsidies, while their dependents would yield $176 million.

Overall, the early retiree reinsurance program will provide about $2.5 billion in subsidies to employers during the first year of the program. Because the reinsurance program provides a maximum of $5 billion in subsidies, the program will likely run out of money in 2011, leaving no money for subsidies in 2012 and 2013. This assumes that all employers eligible to apply do so, and is also contingent on the assumptions mentioned above. The analysis also does not take into account the timing of expenses in the first year, which may lower the subsidy received in that year.[6]

Conclusion

Given the temporary nature of the reinsurance program, it is intended to provide employers an incentive to maintain benefits until the health insurance exchange is fully operational. Once the health insurance exchange is fully operational, employers will have less incentive to provide health benefits to early retirees, and retirees would have less need for former employers to maintain a program. Under the health insurance exchange, retirees could not be denied coverage because of pre-existing conditions and they could not be charged a higher premium because of their health status. Limited age rating would be allowed. Furthermore, subsidies would be available to individuals in families with income below 400 percent of the federal poverty level who purchase health insurance through the exchange.

In the short term, the reinsurance provisions would help shore up early retiree coverage, but in the longer term, the underwriting reform combined with new subsidies for individuals enrolling for coverage through the exchange would create significant incentives for employers to drop coverage for early retirees.

Endnotes

[1] Sponsors include group plans maintained by private employers, state or local governments, employee organizations, voluntary employees' beneficiary associations, a committee or board of individuals appointed to administer such a plan, or a multiemployer plan as defined by ERISA. Both fully insured and self-funded plans are eligible.

[2] These amounts are indexed for plan years starting on or after Oct. 1, 2011.

[3] See Figure 1 in www.mercer.com/summary.htm?idContent=1364345

[4] See Paul Fronstin, "Health Insurance Coverage of Individuals Ages 55−64, 1994−2007," *EBRI Notes,* no. 8 (Employee Benefit Research Institute, August 2009): 2−10.

[5] Surviving spouses could not be identified, so to some degree this study underestimates the number of individuals covered by plans eligible for the subsidy.

[6] The portion of expenses exceeding $15,000 incurred before June 1, 2010, cannot be used to claim the subsidy during 2010. However, expenses incurred below $15,000 before June 1, 2010 can be counted toward the first $15,000 in annual claims for purposes of determining whether the $15,000 threshold has been met.

New Publications and Internet Sites

[Note: To order U.S. Government Accountability Office (GAO) publications, call (202) 512-6000.]

Employee Benefits

Employee Benefit Research Institute. *Fundamentals of Employee Benefit Programs*. Sixth Edition. $19.95 (EBRI members get a 55 percent discount) plus shipping. EBRI member organizations, or those interested in bulk purchases of *Fundamentals*, should contact Alicia Willis at (202) 659-0670 or e-mail: publications@ebri.org

Employee Stock Ownership Plans (ESOPs)

The National Center for Employee Ownership. *Issue Brief: The State of Employee Ownership* [27 photocopied pages]. NCEO members, $15; nonmembers, $25. National Center for Employee Ownership, 1736 Franklin St., 8th Fl., Oakland, CA 94612, (510) 208-1300, fax: (510) 272-9510, e-mail: customerservice@nceo.org, www.nceo.org

Financial Planning

U.S. Government Accountability Office. *Consumer Finance: Factors Affecting the Financial Literacy of Individuals with Limited English Proficiency*. Order from GAO.

Health Care

Davidson, Stephen M. *Still Broken: Understanding the U.S. Health Care System*. $27.95 (cloth). Stanford University Press, Chicago Distribution Center, 11030 South Langley Ave., Chicago, IL 60628, (800) 621-2736, fax: (800) 621-8471, e-mail: custserv@press.uchicago.edu, www.sup.org

Rice, Thomas, and Lynn Unruh. *The Economics of Health Reconsidered*. Third Edition. $94 + S&H. ACHE/HAP Order Fulfillment Center, P.O. Box 75145, Baltimore, MD 21275-5145, (301) 362-6905, fax: (301) 206-9789, e-mail: HAP1@ache.org, www.ache.org/hap.cfm

Health Insurance

Mercer. *National Survey of Employer-Sponsored Health Plans, 2009 Survey Report*. Report, $600, Report and tables, $1,200 (tables not sold separately). Mercer Health & Benefits, Attn: Tara Lewis, 1166 Avenue of the Americas, 29th Fl., New York, NY 10036-2708, (212) 345-2451, e-mail: tara.lewis@mercer.com, www.mercer.com

U.S. Government Accountability Office. *Medicare Advantage: Relationship between Benefit Package Designs and Plans' Average Beneficiary Health Status*. Order from GAO.

Pension Plans/Retirement

Schaus, Stacy L. *Designing Successful Target-Date Strategies for Defined Contribution Plans: Putting Participants on the Optimal Glide Path*. $75. John Wiley & Sons, Customer Care Center - Consumer Accounts, 10475 Crosspoint Blvd., Indianapolis, IN 46256, (877) 762-2974, fax: (800) 597-3299, www.wiley.com

Turner, John A. *Pension Policy: The Search for Better Solutions*. $20 + S&H. W.E. Upjohn Institute for Employment Research, Attn: Publications Department, 300 S. Westnedge Ave., Kalamazoo, MI 49007-4686, (888) 227-8569 or (269) 343-5541, fax: (269) 343-7310, wyrwa@upjohninstitute.org, www.upjohninst.org

U.S. Government Accountability Office. *Retirement Income: Challenges for Ensuring Income throughout Retirement*. Order from GAO.

Reference

Insurance Information Institute. *The Financial Services Fact Book 2010*. Hardcopy, $45; PDF, $58 (discounts for multiple copies are available). Insurance Information Institute, 110 William St., 24th Fl., New York, NY 10038, (800) 331-9146 or (212) 346-5500, e-mail: publications@iii.org, www.iii.org/publications

Social Security Reform

Sass, Steven, Alicia H. Munnell, and Andrew Eschtruth. *The Social Security Fix-It Book*. 2009 Edition. PDF and e-book versions are available free of charge at the following site: http://crr.bc.edu/special_projects/the_social_security_fix-it_book.html For information about bulk orders (hard copies), please contact Monica Sambataro at monica.sambataro@bc.edu or (617) 552-9143 at the Center for Retirement Research at Boston College.

Web Documents

AARP: *Automatic 401(k) Plans: Employer Views on Enrolling New and Existing Employees:* http://assets.aarp.org/rgcenter/econ/auto401k.pdf

America's Health Insurance Plans: *January 2010 Census Shows 10 Million People Covered by HSA/High-Deductible Health Plans:* www.ahipresearch.org/pdfs/HSA2010.pdf

Aon Consulting: *The "Captivation" of Employee Benefits: How Captives Can Reduce Costs and Enterprise Risk:* www.aon.com/attachments/benefits_captives2010.pdf

Bureau of Labor Statistics: "How Does Your 401(k) Match Up?": www.bls.gov/opub/cwc/cm20100520ar01p1.htm

Center for Retirement Research at Boston College: *Should You Convert a Traditional IRA into a Roth IRA?:* http://crr.bc.edu/images/stories/Briefs/ib_10-5.pdf

Center for State & Local Government Excellence and National Institute on Retirement Security: *Out of Balance? Comparing Public and Private Sector Compensation over 20 Years:* www.slge.org/vertical/Sites/%7BA260E1DF-5AEE-459D-84C4-876EFE1E4032%7D/uploads/%7B03E820E8-F0F9-472F-98E2-F0AE1166D116%7D.PDF

Deloitte Center for Health Solutions: *2010 Survey of Health Care Consumers: Key Findings, Strategic Implications:* www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/US_CHS_2010SurveyofHealthCareConsumers_050310.pdf

Hewitt Associates: *Research Highlights: Retirement Income Adequacy at Large Companies: The Real Deal 2010:* www.hewittassociates.com/_MetaBasicCMAssetCache_/Assets/Articles/2010/Hewitt_Research_Retirement_Income_Adequacy_2010.pdf

Internal Revenue Service: *Tax Treatment of Health Care Benefits Provided With Respect to Children Under Age 27* [Notice 2010-38]: www.irs.gov/pub/irs-drop/n-10-38.pdf

Investment Company Institute: *Research Fundamentals,* "The U.S. Retirement Market, 2009": www.ici.org/pdf/fm-v19n3.pdf

Mercer: *How Does Your Retirement Program Stack Up? – 2010:* www.mercer.com/retirementbenchmarking

Milliman, Inc.: *Multiemployer Review: Update on Issues Affecting Taft-Hartley Plans:* http://publications.milliman.com/periodicals/mer/pdfs/MER05-27-10-health-reform.pdf

Pension Benefit Guaranty Corporation: *PBGC Annual Report 2009:* www.pbgc.gov/docs/2009_annual_report.pdf

The Pew Charitable Trusts Philadelphia Research Initiative: *Not Out of the Woods: The Recession's Continuing Impact on Big City Taxes, Services and Pensions:* www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Reports/Philadelphia_Research_Initiative/Not%20Out%20of%20the%20Woods_May%2026.pdf?n=203

PricewaterhouseCoopers' Health Research Institute: *Behind the Numbers: Medical Cost Trends for 2011:* http://pwchealth.com/cgi-local/hregister.cgi?link=reg/Behind_the_numbers_Medical_cost_trends_for_2011.pdf

Profit Sharing/401k Council of America: *2010 403(b) Plan Survey Highlights: Reflecting 2009 Plan Experience:* http://guest.cvent.com/EVENTS/Info/Agenda.aspx?e=4c795c3f-3674-4238-b559-c0a5e4cfd215

TIAA-CREF Institute: *Trends and Issues,* "Retirement Confidence on Campus: The 2010 Higher Education Retirement Confidence Survey": www.tiaa-crefinstitute.org/pdf/research/trends_issues/ti_confidencesurvey0610.pdf

Towers Watson: Health Care Reform: Looming Fears Mask Unprecedented Employer Opportunities to Mitigate Costs, Risks and Reset Total Rewards www.towerswatson.com/assets/pdf/1935/Post-HCR_Flash_survey_bulletin_5_25_10(1).pdf

Transamerica Center on Retirement Studies: *The Employers' Perspective on Retirement Benefits and Planning: 11th Annual Transamerica Retirement Survey:* www.transamericacenter.org/resources/TCRS%2011th%20Annual%20Employer%20Report_FINAL.pdf

Unum: *Beyond the Usual Benefits: 2010—The Power of Employee Education to Influence Workforce Satisfaction:* http://forms.unum.com/StreamPDF.aspx?strURL=/FMS_099229-3.pdf&strAudience=StreamByNumber

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