Drive to Simplify Section 89 Accelerates as Congress Responds to Pressure (p. 1) Surveys Explore 401(k) Investment Options (p. 4)
The Impropriety of Benefit-Motivated Employment Actions (p. 7) Legislation & Litigation (p. 10) In the States (p. 13) For Your Benefit (p. 14)

Drive to Simplify Section 89 Accelerates as Congress Responds to Pressure

Efforts to modify section 89 welfare benefit nondiscrimination rules have heated up in Congress. Both the House and Senate are moving quickly in response to an outcry from business groups. The powerful tax-writing committees of both houses—House Ways and Means and Senate Finance—have held hearings to address ways to simplify the complex rules.

Also, in an important turnabout, Rep. Dan Rostenkowski (D-IL), chairman of Ways and Means, introduced legislation (H.R. 1864) that would significantly simplify section 89. Markup of the bill is expected this month.

The Bush administration has also shown support for revision of section 89. The Department of the Treasury ordered that the beginning date for employer testing of welfare benefit plans under section 89 be delayed from July 1 until Oct. 1.

In announcing the delay, Treasury Secretary Nicholas Brady said he supports the law's “fundamental logic” but would like to work with Congress to “revise and improve it.” Dana Trier, Treasury's tax legislative counsel, told the Ways and Means Committee on May 2 that “complete revision of section 89 is necessary.” He added that Treasury continues to believe that “repeal is not a viable option at this time.”

The Rostenkowski Bill

H.R. 1864 would replace the current section 89 nondiscrimination rules (which are based on coverage, eligibility, and benefits) with a design-based test.

A plan would pass the proposed test if: (1) the plan is available to at least 90 percent of the employer's nonhighly compensated employees; (2) the plan requires an employee premium contribution of no more than $10 per week for single coverage and $25 per week for family coverage; and (3) the maximum amount of employer-paid premium that may be excluded from the income of any highly compensated

Bentsen Introduces Section 89 Bill

As this issue went to press, Senate Finance Committee Chairman Lloyd Bentsen (D-TX) introduced a bill similar to Rostenkowski's that would replace section 89 nondiscrimination rules with a design-based test. Bentsen's bill (S. 1129) would go farther, however, by allowing plans to satisfy the affordability standard of the proposed rules if the employee is not required to pay more than 40 percent of health insurance premiums. Moreover, it would delay implementation of all section 89 rules until 1990. The bill, introduced on June 6, has some 50 cosponsors, including 18 members of the 20-member Finance Committee. With the introduction of this bill, a major overhaul of section 89 seems highly likely. Further details of S. 1129 will be provided in the July issue of Employee Benefit Notes.
employee is no greater than 133 percent of the employer-paid premium in a plan available to 90 percent of the nonhighly compensated.

The bill would exclude group term life insurance from section 89. Also, employees who work less than 25 hours per week would be excluded from testing, an increase from the 17.5-hour requirement included in the current regulations.

H.R. 1864 also includes additional relief measures that address leased employees, union plans, former employees, and penalties for failure to meet the qualification requirements (Notes, 5/89, pp. 11-12).

Suggested Modifications

The House Ways and Means Committee held hearings May 2-3 on the Rostenkowski bill. Witnesses generally praised H.R. 1864 as an important step toward simplification, while offering suggestions for changes in several provisions.

90 Percent Eligibility Test—Several witnesses criticized the 90 percent eligibility test as too steep, and asked Rostenkowski to modify its “cliff effect.” Under the test, if an employer fails to meet the 90 percent requirement by a few or even one employee, all of its highly compensated employees would be taxed on the total value of all of their health and welfare benefits. Those that fail the test by a small margin would be penalized as harshly as those that fail by a large margin.

Witnesses representing the American Society for Personnel Administration, the ERISA Industry Committee, and the Section 89 Coalition, among others, suggested modifying the cliff effect to a graduated scale based upon an employer’s degree of failure or, in the interest of keeping the law simple, lowering the threshold to 70 percent or 80 percent.

$10/$25 Affordability Standard—Several witnesses recommended that the limit on employee premium contributions be based on a percentage of their wages and/or overall premiums rather than on fixed dollar amounts. Their objections focused on the large regional differences in both pay and medical costs.

H.R. 1864 provides that the maximum employee contribution be adjusted in the future as wages increase. Witnesses suggested that employee contributions be indexed instead to health care inflation.

“Indexing health care costs to wage inflation may keep employee contributions to a minimum, but it will also have the effect of reducing overall access to health care,” said Alice Griffin, speaking on behalf of National Small Business United at the May 2 hearing. “Even if employee contributions were reasonable in the beginning, health care inflation would assure that employers would bear an ever-increasing share of the health care burden. Eventually, employers will be forced to reduce the extent of their health care provisions or cancel plans entirely.”

Cafeteria and Salary Reduction Plans—Advocates of cafeteria plans told the House panel that Rostenkowski’s proposal would pose critical problems for section 125 cafeteria plans. The bill would treat salary reduction as an employer-provided benefit for highly compensated employees, but as an employee-purchased benefit for nonhighly compensated employees. In applying the 133 percent benefits test to highly compensated employees’ benefits, the limit could easily be exceeded as a result. According to the Employers Council on Flexible Compensation (ECFC), this could result in all of the benefits under a plan being taxable to highly compensated employees even though the plan provides identical benefits to all employees. Furthermore, the bill would treat “cashable benefits”—credits provided by the employer that the employee may use to select benefits or take as taxable cash—as employee contributions.

The Cafeteria Plan Coalition and ECFC told the Ways and Means Committee that because of the way the bill treats employer credits and salary reduction, a cafeteria plan is highly likely to exceed the $10 and $25 affordability limits. Supporters of cafeteria plans maintain that these plans can pass the requirements under current law but would fail the nondiscrimination rules under Rostenkowski’s bill. According to ECFC, this might seriously endanger the future of flexible benefit plans.
According to the Society of Professional Benefit Administrators, employers have turned to the salary reduction arrangement in an effort to control increasing health costs, and thereby have been able to sustain the existence of their health plans. Furthermore, advocates maintain that cafeteria plans allow dual-earner couples to avoid the redundant costs of two medical plans and choose benefits that better suit their needs.

Part-Time Employees—Several witnesses told the committee the law should apply to employees working 30 or more hours per week rather than 25. According to Frank Swain, chief counsel for advocacy for the U.S. Small Business Administration, 30 hours per week is the traditional dividing line between full- and part-time workers that many insurance companies use to set their rates. Swain said many small employers have said that it is too expensive, if not impossible, to obtain insurance for employees working fewer than 30 hours per week.

Multiemployer Plans—Multiemployer benefit plans differ from single-employer plans in the way they are funded and administered. Under a multiemployer plan, two or more employers contribute to a pooled fund on behalf of workers covered by a collectively bargained agreement. The benefits purchased from the fund are selected and administered, not by the employers but by independent trustees.

H.R. 1864 would impose an excise tax on employers equal to 34 percent of the amount of benefits paid under health plans that did not meet the qualification standards. According to the National Constructors Association, this would unfairly penalize employers who sponsor multiemployer plans because they have little or no control over how the plans are administered.

Delay—Witnesses also urged the committee to delay the effective date of section 89 until Jan. 1, 1990. Frederick Rumick of Buck Consultants told the committee that there is confusion among plan sponsors concerning the ultimate direction of section 89, and that many employers have adopted a “wait-and-see” attitude because of this uncertainty.

Other Legislative Efforts

Pressure to change or repeal section 89 has been growing since the 101st Congress convened this year. Several other bills have been introduced to repeal, delay, or simplify the current regulations.

Repeal—Rep. John LaFalce (D-NY), chairman of the House Committee on Small Business, is leading the effort to repeal section 89. His bill (H.R. 634) has nearly 300 cosponsors. The National Federation of Independent Business (NFIB), the U.S. Chamber of Commerce, and other business groups are lobbying extensively for repeal and have generated substantial support for the bill. Many observers believe this groundswell of opposition caused Rostenkowski to draft H.R. 1864.

LaFalce told the Ways and Means Committee on May 2 that H.R. 1864 “can become an appropriate vehicle” if concerns about the definition of part-time employees, difficulties for cafeteria plans, and the “inequitable” dollar level of allowable employee contributions are addressed. While the Chamber and other business groups have shown support for Rostenkowski’s proposal, with some modifications, NFIB has held fast to its call for repeal.

Delay—S. 89, introduced by Sen. Steve Symms (R-ID), would delay the effective date of section 89 for one year to plan years beginning after Dec. 31, 1989.

Small Business Exemption—Sen. Pete Domenici’s (R-NM) bill (S. 595) would exempt employers with fewer than 20 employees from section 89. The bill would also delay the application of section 89 for two years. Treasury Secretary Brady told a Senate Appropriations subcommittee on May 2 that he would consider Domenici’s proposal to exempt small businesses.

Simplification—Sen. David Pryor (D-AR) introduced the Section 89 Simplification Act (S. 654) on March 17. This bill would create a safe harbor from the nondiscrimination requirements for plans that qualify as simplified health arrangements (Notes, 4/89, pp. 10–11).

Rep. Philip Crane (R-IL) introduced a bill (H.R. 1682) to simplify section 89 through reduction of the number of tests required and the
exclusion of leased and union employees, among other provisions.

Legislative Outlook

Although other proposals have gained widespread attention, Rostenkowski's bill is likely to be the vehicle used, on the House side, to amend section 89. As chairman of the Ways and Means Committee, Rostenkowski holds considerable control over the fate of section 89 legislation.

Most observers agree that repeal or delay is unlikely because of the effect either action might have on the federal budget; section 89 is estimated to generate some $340 million in revenues over three years. Furthermore, critics maintain that the primary motive behind the introduction of section 89 was to raise revenue; in that case, repeal would not be an option. In any case, both Rostenkowski and Senate Finance Committee Chairman Lloyd Bentsen (D-TX) have said they oppose repeal. Without the support of these two powerful players or that of the Bush administration, the repeal effort seems ill-fated.

In announcing the introduction of his bill, Rostenkowski said, "The tax revenue lost to the Treasury because of the exclusion for employer-provided health insurance will exceed $32 billion in fiscal year 1990 alone. I think it is only appropriate that this significant tax subsidy is available only to employer health insurance programs that promote broad-based health coverage, rather than coverage of only highly paid employees or executives."

Many legislators have said that section 89 has produced more mail than any other issue this year and, therefore, they would like to respond as quickly as possible. While advocates of flexible benefits will strive to preserve the tax advantages afforded cafeteria plans, other groups will seek clarification of the rules for their firms' special needs. Any attempt to accommodate such diverse interests could lead to additional complexity—defeating the stated purpose of Rostenkowski's bill. Thus, given the political climate, simplified nondiscrimination rules seem destined to emerge from the legislative process.

Surveys Explore 401(k) Investment Options

Assets in cash or deferred arrangements, commonly called 401(k) plans, now constitute a sizeable investment pool of funds. The U.S. General Accounting Office (GAO) estimates that in 1986, participant and employer contributions to 401(k)s amounted to $9 billion, with assets totaling $70.4 billion. This equals about one-quarter of assets invested in individual retirement accounts and Keogh plans in the same year. Thus, an assessment of the investment options offered by employers and those chosen by employees provides insight into the management of this significant pool of assets.

While comprehensive nationwide data on 401(k) investment vehicles and options are not available, three recent surveys shed some light on these issues. This article is based on three sources: GAO, 401(k) Plans: Incidence, Provisions, and Benefits (Gaithersburg, MD: GAO, PEMD-88-15BR, March 1988); Hewitt Associates, What's New in 401(k) Administration and Experience (Lincolnshire, IL: Hewitt Associates, 1988); and Buck Consultants, 401(k) Investment Practices (New York: Buck Consultants, 1989).

Both the Hewitt and Buck surveys are small-sample surveys representing larger employers. There were 327 respondents to Hewitt's survey, with a median company size of 8,000 employees; Buck's survey included 102 respondents, with a median size of 3,800 employees.

GAO survey data are more representative of smaller plans. Somewhat more than 3,600 firms responded to the survey, which GAO generalized to about 793,000 U.S. firms, 35,000 of which had 401(k) plans in 1986. Among these firms, 94 percent employed fewer than 100 employees, while 6 percent employed 100 or more.

What Investment Options Do Employers Offer?

Participants in 401(k) plans are usually offered a choice among
Table 1
401(k) Plan Investment Options and Participant Choices among Options

**Hewitt Associates Survey**

<table>
<thead>
<tr>
<th>Investment Option</th>
<th>Employee Before-Tax Contributions</th>
<th>Employer Contributions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Percentage of plans offering option</td>
<td>Percentage of assets allocated to option</td>
</tr>
<tr>
<td>Equity Fund</td>
<td>81%</td>
<td>23%</td>
</tr>
<tr>
<td>Guaranteed Investment Contracts</td>
<td>68</td>
<td>64</td>
</tr>
<tr>
<td>Employer Stock</td>
<td>43</td>
<td>33</td>
</tr>
<tr>
<td>Government Bonds or Other Fixed Income</td>
<td>39</td>
<td>21</td>
</tr>
<tr>
<td>Short-Term Securities or Money Market</td>
<td>36</td>
<td>19</td>
</tr>
<tr>
<td>Balanced Fund</td>
<td>20</td>
<td>28</td>
</tr>
<tr>
<td>Life Insurance</td>
<td>3</td>
<td>NA</td>
</tr>
</tbody>
</table>

**Buck Consultants Survey**

<table>
<thead>
<tr>
<th>Investment Option</th>
<th>Employee Before-Tax Contributions</th>
<th>Employer Contributions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Percentage of plans offering option</td>
<td>Percentage of assets allocated to option</td>
</tr>
<tr>
<td>Company Stock</td>
<td>40%</td>
<td>33%</td>
</tr>
<tr>
<td>Guaranteed Investment Contracts</td>
<td>68</td>
<td>62</td>
</tr>
<tr>
<td>Fixed Income</td>
<td>45</td>
<td>21</td>
</tr>
<tr>
<td>Equities</td>
<td>88</td>
<td>25</td>
</tr>
<tr>
<td>Money Market</td>
<td>35</td>
<td>31</td>
</tr>
</tbody>
</table>


Note: Tabulations for asset allocations are only for plans offering that option. Percentages do not add to 100 due to multiple responses.

Investment options for their own pretax contributions and sometimes for employer contributions. Participants typically have the option of investing the two types of funds differently, but sometimes the plan automatically directs the investment of employer contributions.

All three surveys indicate that equity funds are the most common investment option offered by employers (table 1, chart 1). Hewitt reports that 81 percent of plans offered equity funds (for participant contributions), while Buck reports 88 percent (also for participant contributions); GAO reports that 72 percent of plans offered such options. Hewitt and Buck both report a smaller percentage of
Hewitt and Buck surveys, with 43 percent and 40 percent of plans, respectively, offering the option. GAO, on the other hand, reports that only 7 percent of companies surveyed offered company stock as an investment option. Money market funds are more common among companies in the GAO survey—63 percent of plans—compared to 36 and 35 percent, respectively, of plans in the Hewitt and Buck surveys.

The surveys suggest that the most common number of investment options is about three, but the actual number ranges from one to seven. Most of these investment options are fairly conservative instruments. Few plan sponsors offer more risky options, such as commodity futures and real estate.

Which Investment Options Do Participants Choose?

GICs and company stock are popular choices among investment alternatives for participant contributions. Sixty-four percent of assets among plans offering GICs in the Hewitt survey and 62 percent in the Buck survey are invested in GICs; 33 percent of assets in both surveys are invested in company stock. In the GAO survey, a relatively smaller percentage (compared to other surveys) is invested in GICs—31 percent—with 30 percent invested in company stock.

Fixed income funds are less popular. In the Hewitt and Buck surveys, 21 percent of employee contributions are invested in government bonds or other fixed income vehicles.

---

respondents (51 percent and 66 percent, respectively) offering equities as an investment option for employer contributions. GAO does not report employer/employee contributions separately.

Guaranteed investment contracts (GICs) are the next most common investment option reported by Hewitt (68 percent) and Buck (68 percent). Company stock is also a common investment option in the
Investment of employer contributions to 401(k) plans is somewhat different and may not always reflect employee choice. An average of 69 percent of employer contributions in the Hewitt survey and 63 percent in the Buck survey are invested in company stock. In the survey report, Hewitt comments that many companies require employer contributions to be invested in employer stock, which may reflect the different allocation percentages between employer and employee contributions.

In general, the utilization patterns of investment options show that many investment vehicles are not used in proportion to their availability. For example, while about three-quarters of plans among the surveys offer equities, only one-quarter of the assets represented in each of the Hewitt and Buck surveys are allocated to these instruments, and less than 10 percent of those in the GAO survey.

On the other hand, while only 7 percent of the employers that GAO surveyed offer company stock as an investment option, fully 30 percent of assets are invested in employer stock. The higher utilization may reflect more employer contributions in the form of company stock.

Changing Investment Options

GAO and Hewitt surveyed the frequency with which employees can change investment options. What emerges from the surveys is a relationship between the number of times changes in investment allocation to 401(k) plans are permitted and employer size.

The Hewitt survey indicates some flexibility in changing investments. It reports that 23 percent of plans allow monthly changes, 38 percent allow quarterly changes, and 22 percent allow changes semiannually (chart 2). Respondents to the GAO survey appear to have more limited flexibility in changing investments. GAO reports that fully 50 percent of firms allow changes only on an annual basis, with another 17 percent allowing them semiannually. It is likely that the small employers GAO surveyed limit investment changes in an attempt to minimize paperwork and the cost of administration, communications, and education.

Massachusetts Mutual Life Insurance Company's 401(k) Survey Report 1988 also provides information on 401(k) plan design and experience.

—Bonnie Newton, EBRI

The Impropriety of Benefit-Motivated Employment Actions

In a blistering, 80-page condemnation of the company, New Jersey Federal District Court Judge Sarokin recently delivered the latest chapter

in Continental Can's difficulties with Employee Retirement Income Security Act (ERISA) section 510. That section makes it unlawful to "discharge, fine, suspend, expel, discipline, or discriminate against a participant or beneficiary . . . for the purpose of interfering with the attainment of any right to which such participant may become entitled under the plan . . . ."

According to the court, the company recognized some years ago that the declining market for its product was likely to result in substantial layoffs, which in turn could create huge unfunded pension liabilities. The organized workers of the company had negotiated special, very expensive, pension benefits that were payable to eligible employees on plant shutdown or extended involuntary layoff.

Eligibility, based on an all-or-nothing, "cliff" qualification, was determined by a plan formula based primarily on age plus years of service, and produced a full normal retirement benefit well before normal retirement age. Thus, there was a significant economic incentive both to lay off those who had not become eligible so that they would not qualify, and to protect the jobs of those who already qualified so that the special benefits would not actually become payable to them. The court found that such a benefit-motivated program of layoffs for some and job protection for others was exactly what the company had done:

Accordingly, defendants developed a sophisticated computer program which enabled them to identify those employees who had not yet qualified and who, therefore, should be and were targeted for dismissal. The same computer system kept track of the employees so laid off in order to prevent the resurrection of their rights through inadvertent recall.

Judge Sarokin's outrage at the defendants' conduct comes through clearly in his summary of the company's implementation of the program and response to the plaintiffs' charges:

The plan was shrouded in secrecy and executed company-wide at the specific direction of the highest levels of corporate management. It was intended to save hundreds of millions of dollars in unfunded pension liabilities. The evidence of the plan, its secrecy, and its execution comes from the files of the defendants themselves. The documents are more than a smoking gun; they are a fusillade.

The evidence in support of plaintiffs' claims has been known to and possessed by the defendants since the inception of this case. Nonetheless, defendants have denied the existence of the plan and its implementation. For a corporation of this magnitude to engage in a complex, secret and deliberate scheme to deny its workers bargaining-for pension benefits raises questions of corporate morality, ethics and decency which far transcend the factual and legal issues posed by this matter.

The judge's anger seems based at least in part on the careful and calculated planning of the company as shown in the extensive internal documentation produced at trial. For example, the computer program cited in the earlier quotation, which the defendants admitted was referred to within the company as the "Liability Avoidance Program," had a user manual stating the following:

There are two fundamental principles contained in the concept referred to as avoidance. First, we must be very careful that our plans make every attempt to avoid, insofar as practicable, triggering liabilities already vested in 70-75 [one of the special benefits] qualified employees. Secondly, we must, wherever appropriate, shrink and cap our work forces in order to prevent currently inexpensive D.V.B.'s [deferred vested benefits] from migrating into the very expensive 70-75 category.

The court's opinion is replete with similar statements from the company's records. There seemed little doubt from the documentation presented that the principal, if not sole, purpose of this program was to

limit the attainment of eligibility for bargained pension rights.

Continental Can's Position

The company's defense centered on the proposition that most or all of the aggrieved workers would have been laid off anyway—that whatever this program was intended to do, it did not cause the lost benefit eligibility of which the plaintiffs complained. In part, the argument seemed to be that independent business conditions, principally the decline in demand for steel cans, required some fundamental restructuring, and that structuring these changes with costs—including pension costs—in mind was only sensible and proper.

The court recognized the potential viability of this argument, but introduced its rejection of the argument here by the following characterization: "[T]he issue presented in this matter is whether avoidance of pension liability was the motivating force in the company's decisions or merely a result of the decisions so made." In other words, if potential benefit consequences drove the business decisions, rather than the other way around, that was unlawful.

If the court's ultimate view on this question is correct, this company's business decisions were, in fact, to an extraordinary extent controlled by the desire to minimize pension liabilities. The court characterized the process at each company plant as follows:

[F]irst the decision was made as to the ideal [employment] cap, one which would achieve the maximum amount of liability avoidance. Then, if necessary, the business would be sized to the predetermined cap, and if reductions were necessary, business would either be reduced or reassigned to other plants or internal changes would be made to accommodate the existing volume. Most significantly, the layoffs were monitored through the computer system to make certain that the advantages attained through the layoffs would not be lost through some inadvertent recall.

The court cited an internal company document which stated that, in the past, "most of our locations needed only to adjust their manning to fit the available business at any given point in time. We now find it necessary to begin thinking about fitting the business to the available manning." [Emphasis supplied.] This kind of evidence put the company quite squarely on the wrong side of the business decision/benefit liability line drawn earlier by the court.

Resolution of Case Unclear

Where this case will end up is not clear. It is part of a complex set of litigations in several judicial districts, and Judge Sarokin's decision may, of course, be appealed. The judge himself alluded to this possibility in noting that a litigant is clearly entitled to defend itself, particularly in a case involving potentially hundreds of millions of dollars. He took this occasion, however, to administer a final, rather extraordinary, tongue-lashing to the company:

[I]n this case, despite the overwhelming evidence against them, evidence which has been in their possession since the commencement of this suit and certainly before, defendants have chosen to extend these proceedings, resist discovery, initiate appeals, and in general lengthen the proceeding and increase plaintiffs' expenses. There are times when a litigant must admit its guilt and make amends, rather than defend to the death the indefensible.

Whatever the timetable for the ultimate resolution of this case, its message for other employers is clear: where benefit consequences are considered in connection with a business decision affecting employment, the specter of ERISA section 510 should also be contemporaneously considered.

—This column was prepared by EBRI's legal counsel, Arnold & Porter, under the supervision of K. Peter Schmidt

Legislation & Litigation

Treasury Does Not Support Tax Changes to Curb LBOs

At a hearing of the House Ways and Means Committee on tax options to...
curb corporate takeovers and leveraged buyouts (LBOs), John Wilkens, acting assistant secretary of tax policy at the Treasury Department, said that Treasury "will not counsel major tax changes to correct a trend which may be about to correct itself."

Wilkens told the committee that LBOs are a symptom of the tax code bias that favors debt over equity financing. He said that Treasury is opposed to limiting the interest deduction on debt because it would increase the cost of capital for U.S. corporations and hinder global competitiveness. However, Wilkens said a partial dividends-paid deduction or partial tax credit to shareholders for dividends paid by corporations "would be a meaningful first step" toward changing the existing incentive for corporations to raise capital through debt (Notes, 2/89, pp. 1-3).

Wilkens said the committee should consider the appropriateness of some of the new tax preferences afforded employee stock ownership plans (ESOPs)—including the interest exclusion for ESOP loans, the deduction for dividends paid with respect to ESOP securities, and the nonrecognition of gain on sales of stock to ESOPs.

The committee heard testimony May 16–17 from over 20 witnesses, including Rep. Christopher Cox (R-CA), chairman of the House Republican Task Force on Capital Markets; T. Boone Pickens, general partner of Mesa Limited and chairman of the United Shareholders of America; and representatives from the AFL-CIO, the Securities Industry Association, and the Employee Stock Ownership Association.

Senate Panel Examines Minimum Health Insurance Bill

The Senate Labor and Human Resources Committee held a hearing May 1 to examine the Basic Health Benefits for All Americans Act, introduced by Chairman Edward Kennedy (D-MA). The bill (S. 768) would require all employers to provide a minimum package of health insurance benefits to full-time employees and their dependents (Notes, 5/89, p. 12).

Deborah Steelman, former director of domestic policy for the Bush campaign, told the committee that the proposed legislation fails to deal with the principal barrier to health coverage—affordability—particularly for small employers, who are most susceptible to rising health care costs. Steelman, who is currently a health attorney with the law firm of Epstein, Becker, and Green, asserted that small employers would be forced to choose between compliance with mandated benefits and the job itself. "For the population in question, trading health care for a job is not only an impossible choice for them, but should be for policymakers as well," she said.

Elliott Richardson, former secretary of the Department of Health, Education, and Welfare, agreed with Kennedy's approach, calling the legislation "the best idea we've been able to come up with" for providing health care to poor Americans.

Other witnesses included representatives from the American Public Welfare Association, the American Diabetes Association, the Council of Smaller Enterprises, and the National Association for Public Hospitals.

Federal Standards for Long-Term Care Insurance Considered

The House Ways and Means Subcommittee on Health held a hearing on federal standards for private long-term care insurance on May 17. Chairman Pete Stark (D-CA) has introduced H.R. 1325, a bill that would establish minimum federal standards for private long-term care insurance. The legislation would build upon the amended model state statute developed by the National Association of Insurance Commissioners (NAIC).

Stark said he believes minimum standards are necessary. "With the steady increase in the number of seniors putting their trust in private insurance, there is an appropriate federal role to minimize the potential abuse of vulnerable senior citizens who are trying to act prudently," according to Stark.

While most of the witnesses expressed support for the NAIC model, several objected to the establishment of federal standards. NAIC, the Blue Cross and Blue Shield Association, and the Health Insurance Association of America...
testified that insurance should continue to be regulated by the states. Earl Pomeroy, insurance commissioner of North Dakota, told the subcommittee, on behalf of NAIC, that a federal “Baucus-like” approach is not necessary at this time. The regulatory framework for long-term care insurance will soon be in place in all states, Pomeroy advised.

Consumers Union and the American Association of Retired Persons (AARP) expressed strong support for the establishment of federal minimum standards for long-term care insurance. AARP said that H.R. 1325 represents “an important step toward protecting consumers by assuring more uniform and adequate regulation of this relatively new product.”

Joshua Wiener, senior fellow at the Brookings Institution, said that although use of private insurance is likely to spread substantially, it is unlikely to become the major source of long-term care financing because policies are too expensive for most elderly and have restrictions that limit the amount of financial protection they provide. Using the Brookings-ICF Long-Term Care Financing Model, Wiener estimated that, by the year 2018, private long-term care insurance may be afforded by 25 percent to 45 percent of the elderly, may account for 7 percent to 12 percent of total nursing home expenditures, and may reduce Medicaid expenditures and the number of Medicaid nursing home patients by 1 percent to 5 percent.

House, Senate Budget Negotiators Reach Agreement

A House-Senate conference committee approved a compromise $1.17 trillion budget resolution for fiscal year 1990 on May 11. The spending plan would reduce next year's budget deficit to $99.7 billion, just under the Gramm-Rudman deficit-reduction target of $100 billion. Congressional staff expect final resolution of the budget before the August recess.

The approved budget calls for freezing defense outlays at their current level of about $299 billion, while allowing total outlays for domestic spending to keep pace with inflation. In keeping with the budget agreement approved by both houses, the compromise measure calls for $5.3 billion in unspecified taxes to be determined through negotiations among congressional tax writers and Bush administration officials.

Conferences agreed to cuts in entitlement programs of $6.8 billion. The Senate agreed to the House proposal to cut Medicare by $2.3 billion next year, down from the $2.7 billion in cuts called for in the Senate budget. The reduction would come from decreased payments to doctors and hospitals. The House proposal for $200 million in additional spending for the Medicaid program was included in the compromise agreement.

Senate Clears Minimum Wage Bill; Veto Anticipated

The Senate voted 63-37 to raise the minimum wage to $4.55 an hour over three years, but the vote fell four votes short of the number needed to override an almost certain presidential veto. President Bush has vowed to veto any bill that raises the minimum wage above $4.25 an hour (Notes, 5/89, p. 12; 4/89, p. 10).

The House voted 247-172 for the bill—far short of the two-thirds majority needed to override a veto.

Legislation to Reinstatement Section 127 Introduced

A bill that would allow employees to exclude employer-provided educational assistance from their gross income was introduced April 18 by Rep. Frank Guarini (D-NJ). The Employee Educational Assistance Act of 1989 (H.R. 2037) would reinstate section 127 of the Internal Revenue Code and allow employees to exclude up to $5,250 of employer-provided educational assistance. It would also restore coverage of graduate level courses.

Guarini's bill has over 145 cosponsors. Similar legislation (S. 260) has been introduced in the Senate by Sen. Daniel Moynihan (D-NY). The bills have been referred to the House Ways and Means and Senate Finance committees, respectively.

House Panel Examines Medical Care Quality

The House Ways and Means Subcommittee on Health held a hearing May 24 on the Medical Care Quality Research and Im-
Sections 401(b) Proposed

IRS issued proposed regulations relating to the minimum coverage requirements of section 401(b) of the Internal Revenue Code of 1986 on May 17. The notice also contains amendments to previously proposed regulations relating to the minimum participation requirements under section 401(a)(26) of the code. These regulations would affect sponsors of and participants in pension, profit sharing, and stock bonus plans.

Under the new coverage rules, a plan is considered qualified if it satisfies one of three minimum coverage tests.

The percentage test requires that a plan must benefit at least 70 percent of the employer's non-highly compensated employees.

The ratio test requires that a plan must benefit a percentage of the nonhighly compensated employees that is at least 70 percent of the percentage of the highly compensated employees who benefit under the plan.


Section 89 Testing Date Extended

The Internal Revenue Service (IRS) has issued Notice 89-65, providing employers with additional transitional relief for testing their health and welfare plans under Internal Revenue Code section 89.

Employers now have until Oct. 1, 1989, to assure that their employee plans meet the nondiscrimination requirements of section 89(a), as was announced by Treasury Secretary Nicholas Brady on May 1 (Notes, 5/89, pp. 11-12). In addition, the notice provides that employers have until Oct. 1, 1989, to meet the requirement to make a reasonable notification of benefits to their employees under section 89(k).


Revenue Ruling Provides Guidance on Accumulated Contributions

IRS issued Revenue Ruling 89-60 on May 1 to provide guidance on the interest rates that should be used to determine an employee's "accumulated contributions" under the minimum vesting standards.

The notice indicates that under section 411(c)(2) of the Internal Revenue Code an employee's accumulated contributions are to be determined using 5 percent interest for all plan years beginning on or after the effective date of section 411(a)(2) and before Jan. 1, 1988. For plan years beginning after Dec. 31, 1987, the interest rate is 120 percent of the midterm federal rate for the month that includes the first day of the plan year.

Litigation

Supreme Court Denies Review of Statute of Limitations Case

The U.S. Supreme Court denied review of a U.S. appeals court ruling that a retiree challenging an alleged breach of fiduciary duty by pension plan administrators has a separate cause of action under ERISA each time he or she receives a reduced benefit payment.
The case \textit{(International Association of Machinists [IAM] v. Meagher)} concerns a retiree, Frank Meagher, who claimed the trustees of his pension plan had violated their fiduciary duty under ERISA. IAM argued that whatever the merits of Meagher's claim, the statute of limitations for such a claim had expired.

ERISA section 413 requires that claims be filed within six years of the fiduciaries' alleged breach or within three years of the latest date on which the claimant obtained knowledge of the trustees' action. IAM argued that since Meagher had been retired nine years he could not legally bring suit. A federal district court agreed with this argument.

However, on appeal, the U.S. Court of Appeals for the Ninth Circuit found that "each check issued to [Meagher] in an amount reduced under the inoperative amendment constitutes a fresh breach by the trustees of their duty to administer the pension plan in accordance with the documents and instruments of the plan that are not inconsistent with ERISA." The court said that "a separate cause of action arises with the issuance of each check, and the limitations period runs separately for each cause of action." Under this theory, the statute of limitations for legal claims against pension plans would expire only when a retiree died.

The Supreme Court's refusal to hear the case leaves the Ninth Circuit ruling in place. Attorneys involved in the case have predicted that the court ruling could lead to many class action suits against pension plans.

\textbf{LTV Wins Another Round against PBGC}

A federal appeals court upheld a ruling in favor of LTV Corporation finding that the Pension Benefit Guaranty Corporation (PBGC) cannot require LTV to be held responsible for a $2 billion shortfall in three of the company's pension plans.

LTV, a Dallas-based steel, energy, and aerospace corporation, filed for bankruptcy under Chapter 11 of the federal Bankruptcy Code nearly three years ago; LTV has argued that it would be unable to pay its debt if held responsible for the pension funds' shortage (Notes, 11/88, p. 13; 7/88, p. 13).

PBGC argued that LTV could afford to make up the shortfall because the company's operating profit for the first five months of 1987 had surpassed projections. The appeals court disagreed and affirmed the lower court ruling that PBGC's conclusion had been reached in an "arbitrary and capricious" manner. PBGC's notice of restoration of several pension plans maintained by LTV and LTV Steel Inc. was vacated.

\textbf{In the States}

\textbf{Health Care Rationing}—Oregon will attempt to define a "socially acceptable minimum level of care" within which all persons could be guaranteed access to health care, according to Oregon Senate President John Kitzhaber. The state is compiling a "master list" of medical procedures ranked from the most effective to the least, according to which save the most lives and improve the quality of life for the most people.

\textbf{State-Funded Health Insurance}—Maine's Department of Human Services and the University of Southern Maine's Human Services Development Institute have developed a state-subsidized managed care insurance program aimed at providing affordable insurance to small firms and their uninsured workers. The program, called MaineCare, is supported by the Robert Wood Johnson Foundation. A private health maintenance organization is under contract with the state to administer the program and provide covered services to enrollees.

\textbf{Regulation of In-Home Care}—According to a survey by the Intergovernmental Health Policy Project of George Washington University, 36 states require home health care agency licensure. By July 1990, at least two other states, Washington and Minnesota, will require that skilled home care providers be licensed. Alabama and Oklahoma state legislatures have also been considering bills to regulate home health care.
PBGC has said the decision may encourage other companies with underfunded pension plans to seek bankruptcy law protection to ease their own pension obligations. Observers have indicated that PBGC premiums will have to rise as a result.

For Your Benefit

EBRI Selects Third Fellow

EBRI has named Jean M. Barber, associate director for retirement and insurance at the Office of Personnel Management, as its third fellow. Barber will concentrate her work on a comparison of public- and private-sector benefit programs. She will participate in the EBRI Fellows Program through the Intergovernmental Personnel Act for one year.

UAW, Ford Sponsor Long-Term Care Pilot Project

The United Auto Workers (UAW) union and the Ford Motor Co. are conducting a two-year pilot program to provide long-term care insurance for union members and their family members who are functionally disabled but ineligible for skilled nursing care under Medicare. The plan covers 4,800 active workers at Ford's assembly plants in Louisville, Kentucky.

UAW officials say that if the program is successful, they plan to propose long-term care coverage for the entire auto industry in next year's negotiations.

NAM Offers Health Care Reform Proposal

In response to a survey of its members showing that health care costs have increased nearly 30 percent in one year, the National Association of Manufacturers (NAM) recently issued a 10-point program aimed at reducing health care costs.

NAM called for the "implementation of a competitive cost management strategy" and listed recommendations for reform of the medical liability system, education of employees to be better health care consumers, and improved access to information about hospitals and physicians, along with specific public policy and private actions needed to facilitate the proposal.

PBGC Senior Officials Resign

Kathleen Utgoff, executive director, and Royal Dellinger, principal deputy executive director and chief negotiator, of the Pension Benefit Guaranty Corporation (PBGC) have announced their resignations, effective July 31, 1989.

Government Publications

Social Security Handbook 1988, Social Security Administration


This report outlines current studies, future directions, and coordination of efforts of the Patient Outcome Assessment Research Program. The program was established to promote research with respect to patient outcomes of selected medical treatments and surgical procedures for the purpose of assessing their appropriateness, necessity, and effectiveness. Request pub. no. 1989-241-274/00022 from the National Center for Health Services Research and Health Care Technology Assessment, 18-12 Parklawn Bldg., Rockville, MD 20857. (301) 443-4100. Free.

Nongovernment Publications

Lessons from the First Twenty Years of Medicare: Research Implications for Public and Private Sector Policy, Leonard Davis Institute

In this book, leading experts on health policy assess the effects of Medicare policy over the last 20 years, analyze the impact of chang-
ing economic and demographic conditions, and consider how best to implement successful reform of the Medicare system. The role of private employers in supporting health care to the elderly, reimbursement changes, and the current status of Medigap insurance are among the topics considered. Contact the University of Pennsylvania Press, P.O. Box 4836, Hampden Station, Baltimore, MD 21211. (301) 338-6945. Cost $34.95.

Debt, Leveraged Buyouts, and Corporate Governance, Cato Institute

This study urges government not to restrict leveraged buyouts (LBOs). According to the authors, fears about the effects of LBOs “stem from a misunderstanding about the role of debt and the role of takeovers in the modern corporation.” They maintain that public corporations ensure that management will act in the stockholders’ interest by employing a number of tools: incentive pay for managers, outside directors and auditors, and the market for corporate control. Request paper no. 120 from the Cato Institute, 224 Second St., SE, Washington, DC 20003. (202) 546-0200. Cost $2.

The “Mommy Track” Debate and Beyond: Public Policy? Corporate Reality?, Bureau of National Affairs, Inc. (BNA)

The “mommy track” proposal is a call to arms to corporations to ensure that women reach their potential, not an attempt to impede working women, Felice Schwartz, president of Catalyst, said at a roundtable discussion on work and family issues sponsored by BNA. This report is an edited transcript of the discussion, which included nine other work and family experts. Schwartz’s “mommy track” idea—that employers should consider creating two career tracks for women based on their family responsibilities and desires—is controversial among feminists and business leaders alike. Contact BNA’s Customer Service Center, 9435 Key West Ave., Rockville, MD 20850. (800) 372-1033. Cost $35; multicopy discounts.

Surveys

Employee Benefits in the Year 2000, Northwestern National Life Insurance Company (NWNL)

This survey asked corporate leaders to describe employee benefits now and in the year 2000. Two-thirds of the respondents said they will be offering fewer choices in the year 2000; in 1986, two-thirds said they planned on adding benefits. One-half of those surveyed predicted some type of national health insurance would be in place by the year 2000; however, 81 percent said they believe national health insurance would be ineffective in controlling health care costs. The executives surveyed included a random sample responsible for benefit plan design from companies with 100 to 48,000 employees. Contact NWNL, Route 6525, Box 20, Minneapolis, MN 55440. (612) 372-5784. Free.

National Nonprofit Wage & Benefit Survey, Technical Assistance Center (TAC)

This survey analyzes the compensation practices of nonprofit, charitable organizations (also known as 501(c)(3) organizations). The national data show the average salary increase in nonprofits is 4.01 percent for 1988, down slightly from 4.21 percent in 1987. Sixty percent of reporting agencies contribute a major portion of the cost of health insurance and 75 percent offer health insurance to their exempt employees, according to the survey. Contact TAC, 1385 S. Colorado Blvd., Suite 504, Denver, CO 80222. (303) 691-9610. Cost $50.

National Survey of Mental Health, Alcohol and Drug Abuse Services in HMOs: Chartbook, InterStudy

This study analyzes how mental health and substance abuse benefits and services vary by characteristics of health maintenance organizations (HMOs), such as model types, age, size, profit status, federal qualification status, and corporate affiliation. The survey found that virtually all HMOs surveyed offered at least one benefit package covering mental health, alcohol, and drug abuse services in 1985. However, the majority of HMOs surveyed specifically excluded from standard coverage long-term rehabilitation for alcohol and drug abuse in 1985. Over one-half excluded long-term psychotherapy for mental health care. Contact InterStudy, P.O. Box 458, Excelsior, MN 55331. (612) 474-1176. Cost $30.
The Employee Benefit Research Institute (EBRI) is a nonprofit, nonpartisan public policy research organization based in Washington, DC. Established in 1978, EBRI provides educational and research materials to employers, employees, retired workers, public officials, members of the press, academics, and the general public. The Employee Benefit Research Institute Education and Research Fund (EBRI-ERF) is a nonprofit, nonpartisan education and research organization established by EBRI in 1979. EBRI-ERF produces and distributes a wide range of educational publications concerning health, welfare, and retirement policies. Through their books, policy forums, and monthly subscription service, EBRI and EBRI-ERF contribute to the formulation of effective and responsible health, welfare, and retirement policies. EBRI and EBRI-ERF have—and seek—a broad base of support among interested individuals and organizations, as well as among private-sector companies with interests in employee benefits education, research, and public policy.

Employee Benefit Notes and EBRI Issue Brief (a monthly periodical devoted to expert evaluations of a single benefit issue) are published by the Employee Benefit Research Institute Education and Research Fund with the assistance of the staff of the Employee Benefit Research Institute. Editorial inquiries may be directed to EBRI, 2121 K Street, NW, Suite 600, Washington, DC 20037-2121, (202) 659-0670. Orders, payments, inquiries, and all other correspondence relating to subscriptions should be sent to EBRI’s distribution agent, The Johns Hopkins University Press, 701 W. 40th Street, Suite 275, Baltimore, MD 21211, USA, (301) 338-6964.

Nothing herein is to be construed as necessarily reflecting the views of the Employee Benefit Research Institute or the Employee Benefit Research Institute Education and Research Fund or as an attempt to aid or hinder the passage of any bill pending before Congress.

© 1989. Employee Benefit Research Institute. All rights reserved.
ISSN: 0887-1388 0887-1388/89 $.50 + .50

is registered in the U.S. Patent and Trademark Office.