



Democrats Set Sights on Financial Reform

Having successfully passed Health Care Reform this spring, Congress has taken up another high profile issue, a sweeping overhaul of the US financial system. And like health care, this is a hot button for both Democrats and Republicans.

Currently, the action is centered in the Senate with a bill authored by Banking Committee Chairman Christopher Dodd (D-CT) on its way to the Senate floor. Initial strong opposition from Republicans has significantly eased as both sides have participated in productive compromise talks in the final weeks of April. Facilitating Republicans' willingness to negotiate was a lawsuit filed by the Securities and Exchange Commission (SEC) against Goldman Sachs for allegedly defrauding investors. Widespread media coverage once again stoked public anger at Wall Street and may have been a potent reminder to those on Capitol Hill of the political price for inaction.

Senate Minority Leader Mitch McConnell (D-KY), who had been loudly complaining that the bill "institutionalized" taxpayer bailouts of Wall Street banks, suddenly announced on the Senate floor that he was "heartened" to hear that bipartisan talks had resumed in earnest. Following a meeting with fellow

Republicans, he told reporters that while the legislation still has flaws, he is convinced "there is a new element of seriousness attached to this."

In an important side development, the Senate Agriculture Committee, which has jurisdiction over futures markets, on April 21 approved legislation addressing the \$450 trillion over-the-counter derivatives market. The bill, crafted by Committee Chair Senator Blanche Lincoln (D-AR), takes a much more aggressive stance against big banks than either the Senate Banking Committee or House bills and would force derivatives to be traded on commodity exchanges. It would also block major banks from trading directly in derivatives, depriving them of a key source of income. Ultimately intended to be incorporated into the larger Senate Banking Committee financial overhaul package, the bill passed the Agriculture Committee with the help of Republican Senator Charles Grassley of Iowa. Grassley has played a major role in securing bipartisan support for a number of key bills in the past.

Other GOP legislators are also reaching across the aisle to achieve a compromise on the banking bill, including Banking Committee Ranking Republican Sen. Richard C. Shelby (AL). Among the issues being raised in these discussions are how the new

regulations will impact community banks and small businesses, and how to wind down large, troubled financial firms.

The core of the legislation as passed out of the Banking Committee rests on four major reforms. The first would end "too big to fail" bailouts. This would be accomplished by creating a safe way to liquidate failed financial firms; imposing tough new capital and leverage requirements that make it undesirable to get too big; updating the Federal Reserve's authority to allow system-wide support but no longer propping up individual firms; and establishing rigorous standards and supervision to protect the economy as well as consumers, investors and businesses.

Second, the bill creates a new independent watchdog, housed at the Federal Reserve, with the authority to ensure consumers get clear, accurate information when they shop for mortgages, credit cards, and other financial products, and protects them from hidden fees, abusive terms, and deceptive practices.

Critics have singled out this bureau for particular attention, noting that the legislation imposes significant limits on the autonomy of the "new watchdog." For instance, the bureau

would be overseen by a Financial Stability Oversight Council comprised of nine members, all but one of whom would be existing financial regulators such as the Treasury Secretary. Furthermore, before writing a new rule, the bureau would be required to consult with other financial regulators to ensure consistency with those agencies' objectives, some of which have been accused of playing a role in bringing about the recent financial crisis.

Third, the Dodd bill creates an early warning system in the form of a systemic risk council. This council would be tasked with identifying and addressing systemic risks posed by large, complex companies, products, and activities before they threaten the stability of the economy.

Finally, the bill aims to bring transparency and accountability to exotic instruments like hedge funds and derivatives through elimination of loopholes that allow risky and abusive practices to go on unregulated, including loopholes for over-the-counter derivatives, asset-backed securities, hedge funds, mortgage brokers and payday lenders. Sen. Dodd acknowledged that this section remains a work in progress and as consensus is reached, changes will be incorporated into the final bill.

President Obama, as he did on healthcare, is taking the fight for financial reform outside Washington and directly to voters. His message: "If we don't change what led to the crisis, we'll doom ourselves to repeat it."

NCPERS will continue to closely monitor progress in Congress on the financial reform package. For the latest updates, visit www.NCPERS.org.

FBAR Round 2

Statements by representatives of the IRS last summer regarding which types of foreign financial accounts must be reported under the Report of Foreign Bank and Financial Accounts (FBAR) led to confusion among our nation's governmental pension plans. While past precedent was that governmental pension plans were not required to report under FBAR, the IRS seemed to be saying, without formal written guidance, that these plans would now have to file. Governmental plans across the country met the FBAR filing deadlines last year. The reports required a great deal of time for plan employees and also legal costs.

In October 2009, NCPERS, along with the National Association of State Retirement Administrators (NASRA) and the National Council on Teacher Retirement (NCTR), submitted formal comments to the Treasury Department.

We said that the Bank Secrecy Act requires reports where they have a high degree of usefulness in criminal, tax or regulatory proceedings and in the conduct of intelligence or counterintelligence activities, including analysis to protect against international terrorism. Public pension trust funds, however, are generally

qualified tax-exempt entities. As a consequence, there is no incentive for plan trustees to hide assets or investments from the U.S. government. Furthermore, the plans are creations of state law, municipal ordinance and often state constitutions. Given this design, public plans receive a high degree of oversight and public scrutiny.

We concluded by saying that FBAR reporting by public pension plans will not further the aims of the statute and will instead create an unproductive and unnecessary administrative burden for governmental pension plans. Finally, we noted that it will often be the case that the information public plans would report is already being reported by U.S.-domiciled investment entities in their own FBAR forms.

On February 26, 2010, the Treasury Department issued a proposed rulemaking on FBAR, which included a draft set of new instructions for taxpayers. NCPERS believes that the proposed rule is a significant step in the direction of excepting governmental pension plans from the FBAR reporting requirements. We are gratified that the comments we submitted in October were given weight by the Treasury Department.

As of this writing, NCPERS is working with NASRA and NCTR once again on formal comments to the Treasury Department on FBAR. Specifically, we are requesting further clarification on the exception for governmental plans in the proposed rule and a potential unintended gap in the temporary administrative relief.

NCPERS believes that the language in the draft instructions for the FBAR form, which include a specific exception for governmental entities and in part defines such an entity as an employee retirement or welfare benefit plan of a governmental entity, is a great deal clearer than the language of the proposed rule. In addition, it does not appear that the delayed FBAR filing deadline of June 30, 2011, contained in the temporary administrative relief (Treasury Notice 2010-23) would apply to a governmental plan that has an interest in certain foreign financial accounts, such as bank accounts in overseas branches of U.S. banks. The second issue becomes moot if the proposed rule takes effect prior to June 30, 2010, because it will include an exception for governmental plans – hopefully, a clarified exception.

We will keep you apprised of future developments.

Health Reform – Highlights of the New Legislation

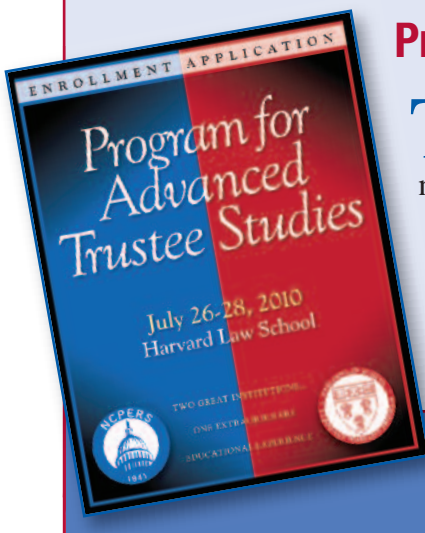
In late March 2010, the President signed ground-breaking health care reform legislation into law, a task worked on by seven presidents before him. The long road to health care reform was contentious, bitter and highly partisan, with Republicans and Democrats on Capitol Hill accusing the other of foul play and disseminating misinformation. And while the bill is now law, the debate is far from over. Republicans vow to overturn some, if not all, of the bill's provisions and have promised to make health care the centerpiece of the November 2010 elections. Undeterred, the Administration is moving forward with the heavy lifting of implementing the law's provisions and the massive job of educating the American public about what is in the bill and how it will affect them.

Speaking on health care reform recently at the National Press Club in

Washington, DC, Health and Human Services Secretary Kathleen Sebelius stated that “the Affordable Care Act is not a magic pill that will cure all the problems in our health care system. It will take time for all the benefits to kick in. And if you look at the history of major social legislation, you see that there are always revisions and adjustments along the way.

“But this law is the biggest expansion in health care coverage since Medicare; the biggest middleclass tax cut for health care in American history; the most aggressive health care cost-cutting law we’ve ever had; and the most ambitious health care innovation legislation I’ve ever seen, all rolled into one.”

Sebelius highlighted three key changes the legislation makes in building on the current health care system: it makes sure that every American with an insurance policy gets “real security” by requiring insurance companies to treat people fairly; it makes insurance



Program for Advanced Trustee Studies (PATS)

The Program for Advanced Trustee Studies (PATS) is intended to provide a unique educational experience for trustees to gain the knowledge and skills necessary to effectively grapple with important issues facing public pension plans. It is designed to educate through dialogue and interaction among program faculty and trustee participants.

The 2010 program will focus on two areas of importance to public funds: **Fiduciary Duty and Pension Fund Risk Management.**

For more details on the PATS program or to complete the application, visit www.ncpers.org. **The application deadline is May 17, 2010.**

affordable for millions of Americans by creating a new insurance marketplace and providing tax credits for those who need additional help; and it starts to bring down costs for families, businesses, and governments with the “broadest health care cost-cutting package ever.”

Other highlights of the health reform package include:

- By 2014, most Americans will be required to carry health insurance or pay a penalty, beginning at \$95 or up to 1 percent of income,

whichever is greater. The penalty is capped at \$695 or 2.5 percent of income, by 2016, for an individual.

- Medicaid will be expanded in 2014, allowing incomes up to 133 percent of the federal poverty level, or \$14,404 for individuals and \$29,326 for a family of four, based on current guidelines.
- State-based insurance exchanges begin in 2014, for individuals and small businesses with up to 100 employees. Minimum coverage for a policy would include 60

percent of the benefit cost of the plan, with an out-of-pocket limit equivalent to the Health Savings Account law limit (\$5,950 for individuals and \$11,900 for families in 2010). According to Congressional Budget Office (CBO) estimates, premiums for those in the individual market would jump 10-13 percent on average in 2016 since coverage would be more inclusive. New policies will be required to include such benefits as hospitalizations,

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Executive Director's Corner

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Pension Assets Jump by a Half-Trillion Dollars— And We’re Telling the Media about It

Numerous new articles published in the last several months have focused on inadequate pension funding, suggesting that public employee pensions may be underfunded by as much as \$1 trillion. These studies focus much of their attention on the worst two-year investing period since the depression, a time when pension funds—and many 401Ks—experienced dramatic declines in their assets.

New data from the Federal Reserve, however, shows that this situation has changed—dramatically—in the past year. From the first quarter of 2009 to the fourth, the total assets of public employee pensions grew by an impressive \$501 billion. This half-trillion-dollar increase occurred after these studies, such as the one published by the Pew Charitable Trust, were written. We expect that total asset amount to increase again when figures for the first quarter of 2010 are released.

In response to these new stories we’ve created a new public relations program to spread the word about this impressive increase in pension assets and to counter misrepresentations about public employee pensions. We have sent material to reporters for *Baron’s*, *Business Week*, and *The New York Post*, with more to follow. We have also posted new fact sheets on a revamped media website and sent word of this information to a list of several hundred reporters for print, broadcast, and Internet media, as well pension trade publication editors.

If you read an article that you believe misrepresents the fiscal situation for public employee pensions, or hear about a story being prepared, call NCPERS in Washington and let us know so we can send our side of the story to the reporter involved.

doctor visits, prescription drugs, maternity care and certain preventive care tests.

- Premium tax credits are available to certain Americans making up to 400 percent of the poverty level, up to \$88,200 for a family of four in 2010. For example, a family of four making \$50,000 would receive a tax credit of \$5,800.
- Those getting insurance through their employers are expected to see an average decrease in premium costs of up the 3 percent by 2016.
- An estimated \$196 billion in savings are expected from permanent reductions in the annual payment adjustments for some Medicare services.
- Beginning in 2014, insurers will not be able to reject adult applications based on pre-existing conditions and, upon the bill becoming law, children with pre-existing conditions must be covered. In the period between now and 2014, the federal government will create and operate a high-risk pool for adults.
- Young people have the option of staying on their parents' health insurance plan until they turn 26, or alternatively, can purchase a "catastrophic" plan with low premiums.
- There are no lifetime limits on the dollar value of health insurance coverage.

- Large businesses with more than 50 employees that do not offer coverage and have at least one full-time employee receiving a premium tax credit will be assessed a \$2000 fee per employee, excluding the first 30 employees. Those companies offering insurance and having employees receiving the tax credit will pay the lesser of \$3,000 for each employee receiving a premium credit or \$750 for each full-time employee.
- Small businesses with more than 25 employees and average annual wages of less than \$50,000 will receive a tax credit of up to 35 percent of the employer's contribution if the employer pays at least 50 percent of health insurance premiums. Full credit is given to those companies with fewer than 20 employees who make on average less than \$25,000.
- Pharmaceutical and health insurance industries would be required to pay a new annual fee in coming years.
- The bill did not address tort reform.

The Health of the Social Security Trust Funds – Get the Facts

Rumors of the impending insolvency of the Social Security Trust Funds appear to be, much like the famous quote about the death of Mark Twain, "greatly exaggerated." While recent

news reports warn that the system will soon need to start cashing its Treasury bonds due to shortfalls from the economic downturn, the Congressional Budget Office (CBO) paints a different picture. In fact, CBO's January 2010 baseline shows the combined old age and disability trust funds **increasing** from \$2.5 trillion in 2009 to \$3.8 trillion in 2020.

So what are the facts?

It is true that payroll tax receipts have declined as the economic downturn has had a shrinking effect on the US job market. As such, CBO forecasts that Social Security will run a *primary* deficit, a measure that does not include interest earned on trust fund assets, until 2014 when the economy is projected to return to full employment.

With payroll tax receipts down, and Social Security outlays exceeding payroll tax revenues, some have argued that, as a result, Social Security will be forced to become a net seller of Treasury bonds. The experts say "no" and point out that Social Security is actually continuing to purchase \$100 billion worth of Treasury bonds annually. These bonds are "special-issue securities," redeemable at face value before they mature – a key fact that increases their value. Realistic expectations are that Social Security will need to begin tapping into the trust funds sometime after 2020 when increasing numbers of the Baby Boomer generation begin hitting retirement age.

Looking beyond the Social Security Trust Funds to the overall health of the system itself, it has been 27 years since the system was last in balance. During this period, Social Security's overall finances continue to be eroded by flat wages while changes in life expectancy and other long-term trends have also required system adjustments. The bottom line is that once the assets of

the trust funds are exhausted, payroll tax receipts for future generations of retirees will only cover approximately 80 percent of promised benefits.

To address this future shortfall, experts see two possible solutions: 1) a modest increase in payroll taxes (estimated to be the equivalent of 0.5% of GDP), or 2) taking an approach similar to

Medicare and taxing earnings above \$106,800.

The Social Security Board of Trustees will soon be making its annual report to Congress which will provide additional information on the financial health of the Social Security Trust Funds. Look for coverage of this report in the next issue of *The Monitor*.

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