

**CalPERS Public Employees' Retirement System
Board of Administration**

**Federal Issues Update
Status as of August 25, 2004**

Long-Term Care Deductibility

Board Position: The Board supports efforts by Congress to make long-term care more affordable.

Proposals:

S. 1335, Long-Term Care and Retirement Security Act of 2003

Summary: Senate Finance Committee Chairman Charles Grassley (R-IA) has introduced his proposal to provide both a tax deduction for long-term care insurance premium costs and a tax credit for long-term care caregivers. These plans would also allow long-term care insurance to be included in cafeteria plans and flexible spending arrangements. Consumer protection measures are included as well.

Status: S. 1335 was introduced on June 25, 2003, and referred to the Senate Finance Committee

Recent Developments: None.

H.R. 2096, Long-Term Care and Retirement Security Act of 2003

Summary: This is the companion bill to S. 1335 and was introduced by Rep. Nancy Johnson (R-CT) chair of the Ways and Means Health Subcommittee.

Status: H.R. 2096 was introduced on May 14, 2003, and referred to the Ways and Means Committee.

Recent Developments: None.

Prescription Drug Benefits (Seniors)

Board Position: The Board supports the need for a prescription drug benefit for seniors but adopted a position in opposition to the Prescription Drug and Medicare Improvement Act of 2003 that was signed into law by President Bush in December. The drug benefit contained in this measure will be inadequate for most CalPERS retirees, will provide a reduced employer subsidy for public entities and includes provisions that will be harmful to the Medicare program and CalPERS Medicare enrollees in the years ahead.

Proposals:

S. 2300, Defense of Medicare Act

Summary: This measure is similar to S. 1992 in that it would amend the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 to eliminate privatization of the Medicare program and to reduce excessive payments to health maintenance organizations and other private sector insurance plans.

Status: The bill was introduced on April 7, 2004, by Senator Ted Kennedy (D-MA) and referred to the Senate Finance Committee.

Recent Developments: None.

S. 1992, Defense of Medicare and Real Medicare Prescription Drug Benefit Act

Summary: The bill would make major changes to the new Medicare prescription drug benefit by eliminating its privatization components, phasing out the “doughnut” hole in coverage, repealing the Health Savings Accounts provisions and allowing for prescription drug reimportation from Canada.

Status: The bill was introduced on Dec. 9, 2003, by Sen. Ted Kennedy (D-MA) and referred to the Senate Finance Committee. The CalPERS Board decided at its March meeting to endorse this legislation.

Recent Developments: None.

S. 1999, Medicare Prescription Drug Price Reduction Act

Summary: The bill would amend the new Medicare prescription drug law by giving the Secretary of the Health and Human Services Department the authority to negotiate prices with drug manufacturers when making bulk purchases of pharmaceuticals that are covered by the new benefit.

Status: Introduced on Dec. 9, 2003, by Senate Minority Leader Tom Daschle (D-SD) and referred to the Senate Finance Committee.

Recent Developments: None.

H.R. 3672, Medicare Prescription Drug Price Reduction Act

Summary: The bill would amend the new Medicare prescription drug law by giving the Secretary of the Health and Human Services Department the authority to negotiate prices with drug manufacturers when making bulk purchases of pharmaceuticals that are covered by the new benefit.

Status: Introduced on Dec. 17, 2003, by Rep. Chet Edwards (D-TX) and referred to the House Energy and Commerce Committee and the House Ways and Means Committee.

Recent Developments: None.

H.R. 4357, Medicare Early Access Act

Summary: The bill would allow 55 to 64-year-olds to buy into Medicare and receive a refundable tax credit equal to 75 percent of their premiums.

Status: Introduced on May 12 by Rep. Pete Stark (D-CA) and referred to the House Energy and Commerce Committee, the House Education and the Workforce Committee and the House Ways and Means Committee.

Recent Developments: None.

Prescription Drug Pricing

Board Position: There are different approaches proposed in Congress to reduce prescription drug prices. The Board will assess the proposals for their impact and potential effectiveness before determining a course of action. The Board supports legislation that would limit business tax deductions for direct-to-consumer advertised prescription drugs that are not presented in a fair and balanced manner.

Proposals:

Direct-to-Consumer Advertising:

H.R. 3155, Fair Balance Prescription Drug Advertisement Act of 2003

Summary: The bill would limit business tax deductions for direct-to-consumer advertised prescription drugs that are not presented in a fair and balanced manner. It would require print ads to display pros and cons in equal typeface and space, and on the same or facing pages. If the advertisements ran onto additional pages, those pages would have to be consecutive with the first pages. In television and radio ads, risk and benefit descriptions would be allotted equal airtime and volume level. Pharmaceutical companies who do not follow these guidelines would not be eligible for an advertising tax deduction.

Status: The bill was introduced on September 23, 2003, by Rep. Pete Stark (D-CA) and referred to the House Ways and Means Committee and the Energy and Commerce Committee. CalPERS voted to support the measure and a letter of endorsement was included in Rep. Stark's introductory materials on the measure.

Recent Developments: None.

S. 2445, Direct-to-Consumer Prescription Drug Advertising Act of 2004

Summary: The bill would require prescription drug manufacturers to “present a fair balance” between a product’s risks and benefits in advertisements targeted to consumers or face civil penalties.

Status: Introduced on May 19 by Sen. John Edwards (D-NC) and referred to the Senate Health, Education, Labor and Pensions Committee.

Recent Developments: None.

Drug Reimportation:

S. 2493, Safe Importation of Medical Products and Other Rx Therapies (Safe IMPORT) Act of 2004

Summary: The measure would allow prescription drug purchases from Canada and certain other countries. It would give the Food and Drug Administration (FDA) authority over imported drugs similar to what it now has over imported food and would require foreign companies that sell medical products to Americans to register with the FDA and submit to FDA inspections. In addition, it would establish federal licensing requirements for Internet pharmacies that conduct business in the United States. Unlike some other reimportation bills, this one would not penalize drug manufacturers that seek to block legal sales from foreign pharmacies or wholesalers to Americans.

Status: Introduced by Sen. Judd Gregg (R-NH) on June 2.

Recent Developments: None.

H.R. 2328, Pharmaceutical Market Access and Drug Safety Act of 2003

Summary: The measure would allow prescription drug purchases from pharmacies in Canada, Australia, New Zealand, Japan and several European countries, provided those pharmacies register with the U.S. Food and Drug Administration (FDA) and agree to oversight by the FDA and the U.S. judicial system.

Status: Introduced by Sen. Byron Dorgan (D-SD) on April 21.

Recent Developments: None.

S. 2307, Reliable Entry for Medicines at Everyday Discounts through Importation with Effective Safeguards Act of 2004, or the REMEDIES Act

Summary: The bill immediately halts unsafe importation but permits individuals to obtain prescriptions from Canadian pharmacies on an interim basis while FDA gets the new drug importation system up and running. Under the bill, the FDA is required to issue final regulations for the new system within 90 days of enactment. Under the new importation system, individuals, pharmacies, and drug wholesalers could purchase qualified drugs for import into the U.S. from foreign exporters that register with the FDA. To obtain a registration, a foreign exporter must demonstrate compliance with safety measures, must submit to jurisdiction of U.S. courts, and take other steps to assure safety of imported drugs. A user fee charged to registered exporters would provide the financing needed for FDA to register and oversee foreign drug exporters and ensure the safety of imported drugs. Drug makers that take direct or indirect action to prevent imports would not be allowed to claim their advertising expenses as tax-deductible business expenses.

Status: This bill was introduced by Finance Committee Chairman Charles Grassley (R-IA) on April 8, 2004. Finance Committee has partial jurisdiction on this measure.

Recent Developments: The Senate Judiciary Committee held a hearing on the bill on July 15. Sen. Judd Gregg (R-NH), Chairman of the Senate Health, Education, Labor and Pensions (HELP) Committee has announced, however, that he does not intend to act on the Grassley bill because he disagrees with the penalty provisions to deny tax deductions if drug companies limit imports.

H.R. 2427, Pharmaceutical Market Access Act of 2003

Summary: The measure would authorize the Secretary of Health and Human Services to devise regulations regarding the reimportation of prescription drugs. It would require the Food and Drug Administration to put a system in place to allow individuals, pharmacies and wholesalers to buy FDA-approved drugs made in FDA-approved facilities from 25 developed countries. The nations include Canada and members of the European Union but not Mexico, which is still viewed as a developing country. It would also require manufacturers to use counterfeit-proof packaging to protect consumers from bad medicines.

Status: Introduced by Rep. Gil Gutknecht (R-MN) on June 11 and passed in the House on July 25, 2003, by a vote of 243-186.

Recent Developments: None.

Drug Discounts:

H.R. 1694, America Rx

Summary: Rep. Michael Michaud (D-ME) introduced a bill to require drug companies to negotiate prescription drug discounts for the uninsured with the Department of Health and Human Services. If they fail to do so, they would lose federal tax credits for marketing and advertising expenses. The bill is based on a similar measure that Michaud sponsored while in the Maine State Legislature and is estimated to lower prescription drug costs by as much as 25 percent for the uninsured.

Status: Introduced on April 9, 2003, and referred to the House Energy and Commerce Committee.

Recent Developments: None.

Drug Pricing and Effectiveness:

H.R. 2356, Prescription Drug Comparative Effectiveness Act of 2003

Summary: Directs the National Institutes on Health to conduct a study of the cost-effectiveness of prescription drugs.

Status: Introduced by Rep. Tom Allen (D-ME) on June 5 and referred to the House Energy and Commerce Committee's Subcommittee on Health.

Recent Developments: None.

Universal Health Care Coverage

Board Position: The Board supports measures to maintain and expand employment-based health care coverage to ensure access and coverage to the greatest number of citizens.

Proposals:

Senator John Breaux's (D-LA) Universal Coverage Plan

Summary: The centerpiece of the Breaux plan would include a federal mandate that individuals purchase health insurance for themselves. His plan would also include a subsidy to help low income people purchase health insurance. This new mandate has been compared to the insurance requirement for licensed drivers who must purchase insurance in order to drive legally.

Status: The proposal is a work in progress that has not been released in legislative language and is still in conceptual form.

Recent Developments: None.

Senator Ted Kennedy's (D-MA) Universal Coverage Plan

Summary: The centerpiece of the Kennedy plan is an employer mandate that would require all employers with more than five workers to offer a basic health plan to its employees, but includes premium assistance for the smallest firms and low-income beneficiaries. Employers would not be required to purchase an FEHBP plan but the health insurance provided would have to be actuarially equivalent to the Blue Cross Blue Shield Standard Option plan available through the federal workers' program. Under the Kennedy plan, premium costs would be shared by employers and employees, with firms responsible for 75% of premiums.

Status: This proposal has not been introduced as legislative language.

Recent Developments: None.

Government Pension Offset (GPO) and Windfall Elimination Provision (WEP)

Board Position: The Board supports efforts by Congress to minimize the effects of the GPO and WEP, pending additional assessment of the economic impact of GPO and WEP on CalPERS' current and future beneficiaries.

Proposals:

H.R. 4391, Public Servant Retirement Protection Act

Summary: Would replace WEP with a formula in which Social Security retirement benefits for individuals with pensions from non-covered jobs would be adjusted in a manner proportional to the level of his or her participation in Social Security. Cost estimates are not yet available.

Status: Introduced on May 19 by Rep. Kevin Brady (R-TX).

Recent Developments: The House Ways and Means Social Security Subcommittee held a hearing on the bill on July 20.

HR 75, Social Security Guarantee Plus Act of 2003

Summary: Representative Clay Shaw (R-FL) has reintroduced his comprehensive Social Security reform bill that includes provisions to modify the Government Pension Offset (GPO). It would reduce the Social Security spousal benefit deductions from an amount equal to two-thirds of the public pension to one-third of the public pension.

Status: The bill, H.R. 75, was introduced and referred to the House Ways and Means Committee on January 7, 2003.

Recent Developments: None.

S. 349, Social Security Fairness Act of 2003

Summary: Senator Dianne Feinstein has reintroduced her measure that would eliminate the Government Pension Offset (GPO) and Windfall Elimination Provision (WEP) laws.

Status: Introduced on February 11, 2003, and referred to the Senate Finance Committee.

Recent Developments: None.

H.R. 594, Social Security Fairness Act of 2003

Summary: Sponsored by Rep. Howard “Buck” McKeon (R-CA), this is the House companion bill to S. 349 that would eliminate the Government Pension Offset (GPO) and Windfall Elimination Provision (WEP) laws.

Status: Introduced on February 5, 2003, and referred to the Ways and Means Committee.

Recent Developments: Rep. Jim Turner (D-TX) has filed a “discharge petition,” which would force a debate and floor vote on the bill if he can obtain the signatures of 218 House members. As of late August, the petition had 192 signatures.

S. 363, Government Pension Offset Reform Act:

Summary: Senator Barbara Mikulski (D-MD) reintroduced her bill to reduce the GPO reductions in Social Security benefits which are required in the case of spouses and surviving spouses who are also receiving certain government pensions. The offset would be equal to the amount by which two-thirds of a retiree's total income (pension plus spousal or survivor's benefit) exceeded \$1,200, adjusted for inflation.

Status: Introduced on February 11, 2003, and referred to the Senate Finance Committee.

Recent Developments: None.

H.R. 887, Government Pension Offset Reform Act

Summary: Introduced by Rep. William Jefferson (D-LA), the bill would reduce the GPO reductions in Social Security benefits payable to a spouse, surviving spouse, or parent receiving monthly payments from a federal or state pension plan. It declares that such benefit reductions shall be equal to the

lesser of: (1) the amount by which the total amount of the combined monthly benefit (before reduction) and monthly pension exceeds \$2,000, adjusted for inflation; or (2) an amount equal to two-thirds of the amount of any such monthly pension plan payment.

Status: Introduced on February 25, 2003, and referred to the Ways and Means Committee.

Recent Developments: None.

H.R. 743, Social Security Protection Act of 2003

Summary: The bill from Rep. Clay Shaw (R-FL) primarily addresses fraud and abuse in the Supplemental Security Income (SSI) program but includes a provision closing the GPO last day loophole. The law now allows workers who are outside Social Security to avoid GPO by spending just the last day of their careers in a job covered by both Social Security and their retirement system. Shaw's bill increases the threshold for exemption from one day to five years for individuals who retire on or after July 1, 2004. The bill also requires public employers to notify new hires about GPO and WEP, have them sign forms certifying that they had been notified and send copies of the forms to the retirement systems that will cover the employees.

Status: Passed by both the House and Senate.

Recent Developments: The President signed the measure into law on March 2, 2004.

S. 439, Social Security Protection Act of 2003

Summary: Introduced by Sen. Jim Bunning (R-KY), this companion bill to H.R. 743 (above) primarily addresses fraud and abuse in the Supplemental Security Income (SSI) program but includes a provision closing the GPO last day loophole. The law now allows workers who are outside Social Security to avoid GPO by spending just the last day of their careers in a job covered by both Social Security and their retirement system. Bunning's bill would increase the threshold for exemption from one day to five years.

Status: Introduced on February 25, 2003, and referred to the Finance Committee.

Recent Developments: A companion bill, H.R. 743, was signed into law on March 2, 2004. (See above.)

H.R. 2011, Windfall Elimination Provision Reform Act

Summary: Sponsored by Rep. Barney Frank (D-MA), this bill would exempt from WEP any retiree whose combined monthly income – pension plus Social Security benefit – did not exceed \$2,000. WEP would be phased in at higher incomes.

Status: Introduced on May 7, 2003, and referred to the Ways and Means Committee.

Recent Developments: None.

S. 1011, Windfall Elimination Provision Reform Act

Summary: Sponsored by Sen. John Kerry (D-MA), this bill would exempt from WEP any retiree whose combined monthly income – pension plus Social Security benefit – did not exceed \$2,000. WEP would be phased in at higher incomes.

Status: Introduced on May 7, 2003, and referred to the Finance Committee.

Recent Developments: None.

H.R. 2611, Military Retirees Government Employment Act of 2003

Summary: Sponsored by Rep. Michael Michaud (D-ME) this bill would exempt military retirees from WEP.

Status: Introduced on June 26, 2003, and referred to the Ways and Means Committee.

Recent Developments: None.

Pension Portability and Reform

Board Position: The Board supports federal efforts to improve portability of public pension assets, increase public pension contribution and distribution limits, and provide additional options for purchasing service credits.

Proposals:

S. 2424, National Employee Savings and Trust Equity Guarantee Act of 2003

Summary: The primary purpose of this legislation was to provide pension plans an alternative to the 30-year Treasury rate on which to base liability calculations. The bill would resolve a concern over the effect of proposed regulations on minimum distributions from defined benefit plans (under Code §401(a)(9)) that would have had an adverse impact on many state and local government pension plan laws pertaining to such things as cost-of-living allowances (COLAs) and alternative forms of benefit payments. Under the provision, public plans would be deemed to have satisfied the requirements of Code §401(a)(9) if they adhere to a good faith compliance of the statutory language. The bill also makes a few technical, but critical, changes to clarify the ability of public employees to purchase service credit in their state or local defined benefit plans in order to build for their

retirement security. Another provision would lower the separation from service exception to age 50 for public safety workers so they would not be subject to the 10 percent early distribution penalty tax.

Status: This Finance Committee bill was approved by the panel on September 17, 2003.

Recent Developments: The Finance Committee released its report on the bill on May 14.

H.R. 1776, Pension Preservation and Savings Expansion Act

Summary: Reps. Rob Portman (R-OH) and Ben Cardin (D-MD) introduced this pension reform and portability legislation to make permanent the pension changes enacted three years ago. Portman and Cardin wrote the language in the 2001 tax cut bill that increased maximum contribution levels to defined contribution (DC) pension plans and eased the portability between various DC accounts, such as 401(k)s, 403(b)s and IRAs. Those measures, like others in the 2001 bill are scheduled to sunset in 2010. In addition to making those reforms permanent, the new bill would also:

- simplify the administration of defined benefit plans;
- improve the ability of public sector workers to purchase service credits;
- make enhancements to DROP plans;
- raise the age for required distributions from 70½ to 75;
- provide tax incentives to encourage retirees to choose annuities over lump-sum payments;
- and allow retirees to pay health care premiums with pre-tax pension money.

Status: Introduced on April 11, 2003, and referred to the House Ways and Means Committee. A modified version of the bill was reported out of committee on July 18, 2003. The provision on retiree health premiums was dropped.

Recent Developments: Bill sponsors Portman and Cardin are considering introducing a new pension reform measure that would contain elements from H.R. 1776, but essentially replace it.

Pension Protections

Board Position: The Board supports federal efforts to provide greater retirement security to private sector 401(k) plan participants.

Proposals:

H.R. 1000, Pension Security Act of 2003

Summary: Introduced by Rep. John Boehner (R-OH), this bill would give 401(k) plan participants more information about their accounts, increased access to

investment advice and the opportunity to diversify company stock holdings after working for the company or holding the stock for three years. The bill amends ERISA, a federal law that does not apply to governmental plans, but the Ways and Means Committee may add its own pension protection plan to it that could have some impact on public sector defined contribution plans.

Status: The House passed its bill on May 14, 2003.

Recent Developments: None.

Expensing of Stock Options

Board Position: The Board supports federal efforts to improve corporate disclosure and accountability.

Proposals:

S 182, Ending the Double Standard for Stock Options Act:

Summary: This bill was reintroduced by Sen. Carl Levin (D-MI) and Sen. John McCain (R-AZ) and would disallow tax benefits for stock option compensation unless disclosed in corporate financial statements.

Status: The bill was introduced on January 16, 2003, and referred to the Finance Committee.

Recent Developments: The Financial Accounting Standards Board (FASB) on March 31 proposed a rule that would require companies to expense stock options.

H.R. 1372, The Broad-Based Stock Option Plan Transparency Act of 2003

Summary: Introduced by Representatives David Dreier (R-CA) and Anna Eshoo (D-CA) it would increase transparency in the use of employee stock options by requiring the SEC to adopt rules to require public companies to increase their disclosures about their use of stock options plans. It would also prevent for three years any government mandate for companies to expense stock options.

Status: The bill was introduced on March 20, 2003, and referred to the Financial Services Committee.

Recent Developments: The Financial Accounting Standards Board (FASB) on March 31 proposed a rule that would require companies to expense stock options.

S. 979, The Broad-Based Stock Option Plan Transparency Act of 2003

Summary: Introduced by Senators Barbara Boxer (D-CA) and John Ensign (R-NV), this is the Senate companion bill to H.R. 1372 described above.

Status: The bill was introduced on May 1, 2003, and was referred to the Senate Banking Committee.

Recent Developments: The Financial Accounting Standards Board (FASB) on March 31 proposed a rule that would require companies to expense stock options.

S. 1890, Stock Option Accounting Reform Act

Summary: Introduced by Senator Michael Enzi (R-WY) with Senator Barbara Boxer (D-CA) as an original cosponsor, this measure would require companies to account for the expense of stock options given to their five highest-paid executives and would prohibit the Securities and Exchange Commission (SEC) from recognizing a stock-options expensing rule from the Financial Accounting Standards Board (FASB) while the Commerce and Labor Departments study the economic impact of an expensing rule that would cover stock option grants to all employees. The legislation is aimed at preempting FASB's efforts to enact a broad-based expensing rule.

Status: The bill was introduced on November 19, 2003, and referred to the Senate Banking Committee.

Recent Developments: The Financial Accounting Standards Board (FASB) on March 31 proposed a rule that would require companies to expense stock options.

H.R. 3574, The Stock Option Accounting Reform Act

Summary: Introduced by Rep. Richard Baker (R-LA), this is a companion bill to S. 1890 (see above).

Status: The bill is awaiting a committee assignment in the Senate.

Recent Developments: The House passed the bill 312-111 on July 20. The Financial Accounting Standards Board (FASB) on March 31 proposed a rule that would require companies to expense stock options.

Mandatory Social Security

Board Position: The Board opposes efforts to mandate participation of newly-hired state and local government employees in the Social Security program.

Proposals:

H.R. 3055, Social Security Solvency Act of 2003

Summary: This Social Security reform bill would restore long-term solvency to Social Security by creating optional private accounts within the program, increasing the retirement age, loaning Social Security \$900 billion from the federal government's general fund and forcing all newly-hired state and local workers to participate in Social Security.

Status: The bill was introduced by Rep. Nick Smith (R-MI) on Sept. 10 and is before the House Ways and Means Committee.

Recent Developments: None.