JANUARY 2014

January saw the introduction of a pair of retirement savings plans. Proposed legislation from Senate Health, Education, Labor and Pensions Committee Chairman Tom Harkin, D-Iowa, would create hybrid accounts in which contributions would be invested through professionally managed funds, and benefits would be paid in the form of lifetime annuities. President Obama, meanwhile, announced the creation of "myRA" plans, which are similar to Roth IRAs, but in which all investments are in Treasury securities. Congressional approval is not needed, and the Treasury Department intends to make the first myRA plans available this year. Also in January, three senior California congressmen – Democrats Henry Waxman and George Miller and Republican Howard "Buck" McKeon – announced that they will not seek reelection this fall.

ISSUES AND EVENTS

Senate Committee Chairman Proposes New Retirement Plan

A Senate committee chairman on January 30 unveiled a proposal aimed at enhancing the nation's retirement system.

The "Universal, Secure, and Adaptable (USA) Retirement Funds Act" from Senate Health, Education, Labor and Pensions Committee Chairman Tom Harkin, D-Iowa, would create an optional retirement plan that combines aspects of traditional pensions and 401(k)-type plans.

"The 'USA Retirement Funds Act' offers a common-sense solution to the retirement crisis by giving the 75 million people without a retirement plan at the workplace the opportunity to earn a safe, portable, and secure pension benefit for life," Harkin said. "USA Retirement Funds would be 21st century retirement plans, run entirely by the private sector, that drastically reduce costs through professional management and risk sharing. Simply put, giving people without access to a quality employer-provided plan the opportunity to earn a retirement benefit would help ensure every American enjoys their golden years with the dignity and financial independence they deserve."

The proposal would create portable accounts with pooled investments. At retirement, participants would receive a defined monthly benefit for the rest of their lives that would be based on the total amount of contributions made by them or on their behalf and investment performance.

Employers with more than 10 employees would have to either enroll their employees in USA Retirement Funds or offer a similar plan. (A basic 401(k) plan would not be an acceptable alternative because it would not provide lifetime benefits.) Employees would be automatically enrolled at a rate of 6 percent of pay per year, but participants could change that amount or withdraw from the program. They could make pre-tax contributions of as much as $10,000 per year, and employers could contribute up to $5,000 per year, but no employer contributions would be required.

The proposal has been applauded by public pension funds and labor groups, as well as activists on retirement issues. CalPERS CEO Anne Stausboll wrote to Harkin to thank him for "addressing the critical issue of retirement security in our country."

"Your leadership and focus on the issues of retirement security will help further a much needed discussion about the importance to every American of planning, working and saving for a financially sound future," Stausboll wrote.

National Institute on Retirement Security (NIRS) Executive Director Diane Oakley said the proposal "represents a significant leap forward to improve the nation's retirement security for generations."

"The current retirement infrastructure does not work for nearly half of the workforce, which has no access to a retirement plan through their employer," Oakley said. "A wide body of research indicates that saving automatically via a payroll deduction enables more working Americans to prepare for retirement. This new proposal could go a long way to put Americans on a solid financial track for their future.

NIRS and Harkin have, at times, complemented each other on retirement issues. Harkin, who first proposed USA Retirement Funds in a July 2012 report has, on several occasions, cited statistics from NIRS detailing the state of Americans' readiness for retirement – or lack thereof – and NIRS has referenced USA Retirement Funds in its work.

Harkin, who is in the final year of his fifth term, is not seeking reelection this fall. He said in 2013 that, before he leaves Congress, "I'd like to get something like [USA Retirement Funds] done. It seems to me that the time is right."

Obama Announces Creation of 'myRA' Savings Vehicle

President Obama used part of his State of the Union speech on January 28 to announce that he has directed the Treasury Department to create a new retirement savings vehicle called a "myRA."

A myRA would be a type of savings bond that, Obama said, "encourages folks to build a nest egg."

"MyRA guarantees a decent return with no risk of losing what you put in," Obama said in the speech. "And if this Congress wants to help, work with me to fix an upside-down tax code that gives big tax breaks to help the wealthy save, but does little or nothing for middle-class Americans; offer every American access to an automatic IRA on the job, so they can save at work just like everybody in this chamber can."

Treasury Secretary Jacob Lew wrote in a January 30 column that myRA plans will be made available this year. Lew explained that there will be no fees and that all contributions – which will be made via payroll deduction and will not be tax advantaged – will be invested in a Treasury security, meaning they will be backed by the full faith and credit of the United States and, thus, will be essentially risk-free. Investments will earn the same interest rate as the Government Securities Investment Fund in the federal government's Thrift Savings Plan. That fund earned 1.5 percent in 2012 and averaged a 3.6 percent annual return between 2003 and 2012.

The accounts will be portable, and participants may withdraw their contributions at any time without taxes or penalties, but, as with Roth IRAs, withdrawals of earnings before age 59½ will incur taxes and, possibly, penalties. Annual contribution limits are also the same as a Roth IRA, currently $5,500. Participants may switch their accounts over to a Roth IRA at any time, and they will be required to do so when their balance exceeds $15,000, or the account has been open for 30 years. Only households with incomes of up to $191,000 will be eligible to participate.

Access to 401(k) plans or other retirement accounts are not disqualifiers for having a myRA account. Employers would not be required to offer the plans.

Young Adults Compose Less than One-Fourth of Exchange Enrollments

Less than a quarter of all people who had signed up for coverage in the state-level health insurance exchanges through late December were in the key 18-34 age group, according to a report released on January 13 by the Department of Health and Human Services (HHS).

The exchanges, also known as marketplaces, were created by the 2010 Patient Protection and Affordable Care Act to provide more options for individuals who cannot get affordable group coverage. Since, as of January 1, insurance companies cannot deny coverage based on pre-existing conditions, there are concerns that, if an insufficient number of young and healthy people enter the insurance market, a "death spiral" could result in which prices rise sharply and the risk pool becomes too old and too sick to be sustainable.

The HHS report states that nearly 2.2 million people enrolled in the exchanges between October 1 and December 28, with about 80 percent of that total having signed up in

December after problems with the online portal for the 36 exchanges operated by the federal government at www.healthcare.gov dampened enrollment numbers during October and November.

"Americans are finding quality affordable coverage in the marketplace, and, best of all, because coverage began on New Year's Day, the promise and hope of the Affordable Care Act is now a reality," HHS Secretary Kathleen Sebelius said. "Our outreach efforts have ramped up, so whether it's through public service announcements, events, our champions or other means, we are doing all we can to find, inform and enroll those who can benefit from the marketplace."

While HHS reported in early January that enrollment numbers had surpassed 2 million, the January 13 report provides the first demographic information about enrollees. It notes that 30 percent are under the age of 35, and 24 percent are between 18 and 34. One-third of enrollees are between 55 and 64 years old, and 55 percent are between 45 and 64.

The Kaiser Family Foundation estimated in a December report that the exchanges need to have young adults (ages 18-34) account for about 40 percent of enrollment, though it suggested that "premiums are not as sensitive to the mix of enrollment as fears about a 'death spiral' suggest, particularly with respect to age."

The report envisioned a "worst case scenario" of young adults accounting for 25 percent of enrollees. This, Kaiser concluded, would result in costs in individual market plans being about 2.4 percent higher than premium revenues.

"Insurers typically set their premiums to achieve a 3-4% profit margin, so a shortfall due to skewed enrollment by age could reduce the profit margin of insurers substantially in 2014," the report stated. "But, even in the worst case, insurers would still be expected to earn profits, and would then likely raise premiums in 2015 to make up the shortfall. However, a one to two percent premium increase would be well below the level that would trigger a 'death spiral,' which would occur if insurers needed to increase premiums substantially, in turn further discouraging young and healthy people from enrolling."

Kaiser and others have also noted that the people most in need of coverage – those who are older and sicker – would probably be the most likely to sign up early in the process, so the percentage of enrollees who are younger could increase by the time open enrollment for the exchanges ends on March 31.

Republicans, though, were hearing none of it, and were quick to pounce on the report as evidence of yet another failure of the health care reform law.

"There's no way to spin it: youth enrollment has been a bust so far," a spokesman for Speaker of the House John Boehner, R-Ohio, said. "When they see that Obamacare offers high costs for limited access to doctors – if the enrollment goes through at all – it's no surprise that young people aren't rushing to sign up."

Among other findings in the report:

- 1.2 million of the enrollees were in the 36 exchanges operated by the federal government, while just under 1 million were in the exchanges run by 14 states and the District of Columbia.
- Women accounted for 54 percent of enrollees.
- 60 percent of enrollees signed up for a "silver" plan; 20 percent for bronze; 13 percent for gold; 7 percent for platinum; and 1 percent for catastrophic coverage. Nearly 80 percent of enrollees are eligible for tax credits to help them pay for coverage.
- California had the most enrollees, with just under 500,000; Hawaii had the fewest, with 2,192.

Republican Senators Propose Health Care Reform Plan

Three Republican senators have unveiled what they informally call their "Obamacare Replacement Plan."

Sens. Richard Burr of North Carolina, Tom Coburn of Oklahoma and Orrin Hatch of Utah are seeking to replace the 2010 Patient Protection and Affordable Care Act (ACA) with the Patient Choice, Affordability, Responsibility and Empowerment (CARE) Act, which includes tax credits, a cap on the income tax exclusion for employer-provided health insurance and other reforms.

"Our nation's health care system was unsustainable before Obamacare, and the president's health care plan made things worse," Burr said. "That's why the Patient CARE proposal repeals Obamacare and focuses on targeted reforms that will lower costs and expand access to quality care. We can lower costs and expand access to quality coverage and care by empowering individuals and their families to make their own health care decisions, rather than empowering the government to make those decisions for them."

The proposal would, among other things:

- Repeal the ACA.
- Adopt "common-sense consumer protections," including a prohibition on lifetime coverage limits (as in the ACA); a requirement that insurers cover dependents up to age 26 (as in the ACA); and a loosening of the restriction on age-based rate variability (the ACA limits the ratio to 3-to-1).
- Prohibit insurers from dropping policy-holders based on health status or denying coverage based on pre-existing conditions, as long as an applicant has been continuously enrolled in a health plan for at least 18 months. Insurers would be required to provide coverage to such consumers "at standard rates." (The ACA prohibits all denials based on pre-existing conditions, even for individuals who have been uninsured.)

- Provide tax credits to small business employees and individuals with incomes of up to 300 percent of the federal poverty level to offset the costs of buying insurance. (The ACA provides tax credits to small businesses and individuals with incomes of up to 400 percent of the poverty level who are not eligible for affordable group coverage.)
- Enact reforms aimed at expanding the use of consumer-directed health care.
- Adopt a "capped allotment" approach to providing Medicaid funding to states, and require federal money to "follow the patient."
- Increase the transparency of health care costs, quality and outcomes.
- Cap the income tax exclusion for employer-provided health insurance at 65 percent of the cost of an average plan.

"We believe Americans who enjoy their employer-sponsored health insurance should be able to continue to receive employer-sponsored insurance," a summary of the proposal states. "Under our proposal, employers would retain the incentive to continue providing health coverage to their employees, because the provision of health coverage would still be deductible for the business. More importantly, our plan repeals the employer mandate which is one of the major drivers of erosion of employer-sponsored coverage under Obamacare. Therefore, this targeted approach would protect employer-sponsored health insurance."

CBO Releases New Estimates for SGR Reform Proposals

The Congressional Budget Office (CBO) in January released new cost estimates for the leading proposals to replace Medicare's sustainable growth rate formula.

The SGR, which was intended by Congress to automatically set Medicare's physician payment rates, annually threatens to slash the federal government's payments to doctors for services provided to Medicare patients. Congress has overridden the SGR calculations every year since 2003 in order to avoid payment cuts that, it has been feared, would drive doctors out of the Medicare program. Frustration has grown with the annual nature of the "doc fix," though, and momentum for enacting a permanent solution grew in 2013. Before leaving Washington for its winter recess in December, Congress approved a three-month SGR fix that blocked a 25 percent rate cut that was scheduled to go into effect the first of the year, giving lawmakers until March 31 to complete work on a permanent measure.

Three congressional panels have drafted their own versions of SGR reform, with the proposal from the House Ways and Means Committee being the least expensive, according to the CBO. That plan, which would replace the SGR with an approach that provides for a 0.5 percent increase each year through 2016, then freezes payments while giving doctors and other health care providers the opportunity to earn performance-based incentive payments, would cost $121 billion over the first 10 years. The committee approved the proposal by a 39-0 vote on December 12.

The CBO put the price tag for a reform plan from the House Energy and Commerce Committee, meanwhile, at $146 billion over the first decade. The Energy and Commerce

bill, which that panel approved by a 51-0 vote in July, would replace the SGR with "an improved fee for service system in which providers report quality measures that will lead to better care in a more efficient manner." It would provide for annual payment increases of 0.5 percent for five years as Medicare and providers transition to a quality incentive program. The CBO had previously estimated that this measure would cost $175 billion, but it reduced the projection based on certain changes to laws and regulations, including revisions to the conversion factor for the 2014 physician fee schedule from the Centers for Medicare and Medicaid Services (CMS).

Both the Ways and Means bill and the Energy and Commerce bill have the number H.R. 2810.

The Senate Finance Committee, on December 12, approved by voice vote, legislation (S. 1871) that would freeze payment levels while encouraging doctors to move into alternative payment models based on value rather than volume. This plan, according to the CBO, would cost $150 billion over the first 10 years.

None of the bills includes a plan for covering the cost of an SGR replacement, and the "pay-for" issue is likely to be the most challenging area in which to reach consensus.

Court Upholds Tax Credits in Federally-Run Exchanges

A federal judge has dismissed a lawsuit challenging the legality of providing tax credits to people who buy insurance through exchanges operated by the federal government.

The 2010 Patient Protection and Affordable Care Act created state-level insurance exchanges to provide a marketplace for the purchase of individual coverage by people who are not able to get group coverage. The federal government operates exchanges through www.healthcare.gov in 36 states that chose not to establish them, and 14 states and the District of Columbia run their own exchanges. The health care reform law provides for tax credits to offset the cost of premiums paid by exchange consumers with incomes of up to 400 percent of the federal poverty level.

A group of individuals and small business owners filed a lawsuit in May 2013 regarding an IRS rule issued a year earlier that provides tax credits to eligible individuals in all of the exchanges, whether run by a state or the federal government. The plaintiffs argued that this conflicts with the "plain language" of the law, which authorizes tax credits for consumers in "an Exchange established by the State," so, they asserted, consumers in the 36 states with federally-operated exchanges should not be eligible for tax credits. Without the tax credits, those states would also not be subject to certain Affordable Care Act requirements, such as minimum benefits standards and the employer mandate.

United States District Court Judge Paul Friedman concluded in a January 15 ruling that the IRS rule “is consistent with the text, structure, and purpose of the Affordable Care Act.”

“In sum, the Court finds that the plain text of the statute, the statutory structure, and the statutory purpose make clear that Congress intended to make premium tax credits available on both state-run and federally-facilitated Exchanges,” Friedman wrote. “What little relevant legislative history exists further supports this conclusion and certainly – despite plaintiffs’ best efforts to suggest otherwise – it does not undermine it.”

The Competitive Enterprise Institute assisted in the coordination and funding of the lawsuit, and CEI General Counsel Sam Kazman said that the ruling “delivers a major blow to the states that chose not to participate in the Obamacare insurance exchange program.”

“It is also a blow to the small businesses, employees and individuals who live in those states as well,” Kazman said. “In upholding this IRS regulation that is contrary to the law enacted by Congress, this decision guts the choice made by a majority of the states to stay out of the exchange program. It imposes Obamacare penalties on employers and on many individuals in those states, penalties that Congress never authorized, putting their livelihoods and the jobs of their employees at risk. Worst of all, it gives a stamp of approval to the administration’s attempt to substitute its version of Obamacare for the law that Congress enacted.”

The plaintiffs have filed for an expedited appeal with the U.S. Court of Appeals for the District of Columbia Circuit.

Democrats Counter GOP Claims on Lost Coverage

A California congressman and fellow Democrats on December 31 released a report that concludes that fewer than 10,000 people will lose coverage in 2014 as a result of the health care reform law.

Republicans have argued that the 2010 Patient Protection and Affordable Care Act’s (ACA) minimum benefits requirements have led to policy cancellations and higher prices in the individual market that could result in as many as 5 million people losing their insurance coverage next year.

Democrats on the House Energy and Commerce Committee, though, say that those claims are “baseless,” and the actual number will be far below that estimate. Their report asserts that the Republican claim suffers from three major flaws:

- It ignores the efforts of insurance companies to re-sign individuals who received cancellation notices. (The administration announced in November that it would allow the renewal of policies that fall short of the ACA’s minimum benefits requirements for 2014.)

- It assumes that no individuals who had private insurance will sign up for insurance through the new health insurance exchanges or Medicaid.
- It overlooks the availability of low-cost catastrophic coverage. (The administration announced in December that people who have had policies cancelled will be eligible for hardship exemptions that will enable them to meet the requirements of the ACA's individual mandate by purchasing catastrophic coverage plans.)

"When these factors are taken into account, a much different picture emerges," the report states. "While there is no central repository of data on insurance coverage in the individual market, the number of individuals who will lose individual coverage and be unable to renew pre-ACA coverage, enroll in subsidized coverage, or access a catastrophic plan is sure to be small. Of the reported 4.7 million people who receive cancellation notices, half should have the option to renew their 2013 coverage. Of the remaining 2.35 million individuals, approximately 1.4 million should be eligible for tax credits through the marketplaces or Medicaid. Of the remaining 950,000 individuals, fewer than 10,000 people in 18 counties in a single state would lack access to an affordable catastrophic plan. This is less than 0.2% of the estimate made by opponents of the Affordable Care Act."

Energy and Commerce Committee Ranking Democrat Henry Waxman of California said that the report "shows that people will get the health insurance coverage they need, contrary to the dire predictions of Republicans."

Another recent study, meanwhile, came up with its own conclusion regarding 5 million people being without coverage, but it is very different from Republican complaints. The ACA expanded Medicaid eligibility to all adults with incomes of up to 138 percent of the federal poverty level, but the 2012 U.S. Supreme Court decision that upheld the constitutionality of most of the law ruled that states cannot be required to broaden the program. Half the states, plus Washington, D.C., have expanded Medicaid, and half have not, resulting in 4.8 million people who could have had coverage under the program this year not being able to get it, according to the Kaiser Family Foundation. (Texas accounts for more than 20 percent of that total.)

"These continued coverage gaps and their varied impacts across groups will result in millions of poor adults remaining uninsured and likely lead to widening racial and ethnic as well as geographic disparities in coverage and access to care," the report stated.

Regulators Revise Volcker Rule to Accommodate Community Banks

Federal financial regulators have revised the Volcker rule to provide a fix sought by community banks.

The Volcker rule, which was included in the 2010 Dodd-Frank Act, is intended to prohibit most proprietary trading by banks. The Commodity Futures Trading Commission (CFTC), the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve, the Office of the

Comptroller of the Currency (OCC) and the Securities and Exchange Commission (SEC) approved the rule on December 10, nearly 17 months after the original deadline.

The American Bankers Association (ABA), whose membership includes mostly community banks, filed a lawsuit on December 24 that challenges a provision of the rule that targets certain collateralized debt obligations (CDO) that are commonly held by smaller banks. These complex financial instruments are composed of trust-preferred securities (TruPS), and, if such investments are prohibited, the ABA asserts that 275 small banks will lose $600 million by having to immediately recognize losses in their current holdings. The lawsuit argues that regulators did not conduct an adequate cost-benefit analysis of the provision.

Under pressure from the community banking industry and lawmakers in both parties, the five agencies that drafted the original rule on January 14 approved an interim final rule that exempts holdings of TruPS CDOs that meet three conditions:

- The TruPS CDO was established, and the interest was issued, before May 19, 2010.
- The banking entity reasonably believes that the offering proceeds received by the TruPS CDO were invested primarily in qualifying TruPS collateral.
- The banking entity's interest in the TruPS CDO was acquired on or before December 10, 2013.

The rule goes on to define "qualifying TruPS collateral" as any trust-preferred security or subordinated debt instrument that meets one of the following conditions:

- Was issued prior to May 19, 2010, by a depository institution holding company that, as of the end of any reporting period within 12 months immediately preceding the issuance of such trust-preferred security or subordinated debt instrument, had total consolidated assets of less than $15 billion.
- Was issued prior to May 19, 2010, by a mutual holding company.

In announcing the change, the regulators noted that Dodd-Frank "provides for the grandfathering of trust preferred securities issued before May 19, 2010, by certain depository institution holding companies with total assets of less than $15 billion as of December 31, 2009, and by mutual holding companies established as of May 19, 2010."

The ABA cheered the revision, with the group's president, Frank Keating, saying the association "commends the regulators' speed and judiciousness in revisiting the impact of the Volcker rule. Their action today should allow banks to avoid taking millions of dollars in unexpected and unnecessary write downs."

Although the ABA withdrew a request it had made in its lawsuit for "emergency relief," Keating said that the group is "deferring a decision on dismissal of the litigation to allow time to consult with our membership and finalize our analysis of the impact and implications of the interim final rule."

Securities Industry and Financial Markets Association President and CEO Kenneth Bentsen said that more Volcker rule changes are needed.

"While we welcome the relief provided to certain holders of TruPS CDOs, we believe that regulators must address the larger problem of the inclusion of senior debt securities issued by collateralized loan obligations (CLOs) in the Volcker rule's prohibitions," Bentsen said. "If this situation is not remediated, corporate borrowers could face higher credit costs, and banks will likely suffer unnecessary losses wholly unrelated to the risk of the CLOs themselves, but rather due to the technical language of the final Volcker rule. We continue to encourage regulators to issue guidance clarifying that banks may hold CLO debt securities."

House Financial Services Committee Ranking Democrat Maxine Waters of California said that the revision "will provide important relief to community banks with investment portfolios that include assets backed by trust-preferred securities. Our nation's regulators should be applauded for this quick and effective policy clarification that, without weakening the Volcker rule, addresses the concerns of community banks and Democratic lawmakers."

Waters and 21 other Democratic members of the Financial Services Committee wrote to regulators on January 7 to assert that, "we believe regulators have the authority to exempt banks with less than $15 billion in assets from the requirement to divest of TruPS CDOs, providing important relief to the community banking sector."

Sen. Joe Manchin, D-W.V., (S. 1912) and Rep. Shelley Moore Capito, R-W.V., (H.R. 3819) introduced bills in January aimed at providing Volcker rule relief to community banks.

Separately, a pair of House Republicans wrote to SEC Chairman Mary Jo White on January 13 to chide the Commission for failing "to conduct any economic analysis in promulgating" the Volcker rule.

Financial Services Committee Chairman Jeb Hensarling, R-Texas, and that panel's Capital Markets and Government Sponsored Enterprises Subcommittee Chairman Scott Garrett, R-N.J., noted in the letter that estimates of the cost of the rule are "$100 million in private-sector mandates" or higher.

"Further, as various commenters and press reports have noted, the liquidity and depth of the corporate bond market – where thousands of U.S. businesses that created millions of jobs go to raise funds – will likely be adversely impacted by the Volcker rule," they wrote. "As a result, U.S. capital markets used by businesses and investors to hedge their exposures could see wider spreads and decreased liquidity thereby increasing business risk."

Hensarling and Garrett asked White to provide "a response detailing the legal justification for not conducting an economic analysis" of the Volcker rule.

The SEC's two Republican commissioners, Michael Piwowar and Daniel Gallagher, noted the lack of an economic analysis when they voted against the rule on December 10.

Senators Back Corporate Political Spending Disclosures in Letter to SEC

A group of 17 Democratic senators, including one from California, wrote to the chairman of the Securities and Exchange Commission on January 9 to say that they are "disappointed" that the SEC does not plan to work on a rule in 2014 to require disclosure of corporate political spending.

The letter, which was organized by Sen. Bob Menendez of New Jersey and includes Sen. Dianne Feinstein of California as a signer, expressed "hope that omission of this matter from the [SEC's] 2014 agenda ... is not due to pressure from those who seek to benefit from unregulated and undisclosed corporate political spending."

"If the omission merely reflects considerations of timing and the SEC's crowded agenda, we respectfully ask that this important investor protection measure remain a priority for the SEC and would appreciate an update as to when the Commission anticipates addressing the issue," they wrote.

The SEC announced in December 2012 that it was considering implementing a rule that would require publicly-traded corporations to disclose their political contributions to shareholders. The commission has received about 700,000 comments on the proposal, more than have been submitted regarding any other issue in its history. The measure is opposed by many Republican lawmakers as well as the U.S. Chamber of Commerce and some other business groups. The five-member commission appears to have two supporters of the proposal and two opponents. Chairman Mary Jo White has been non-committal on the matter, though she has indicated that she does not consider it to be a priority.

The senators' letter stated that, "The ability of corporate executives to spend company resources for political purposes without shareholders' knowledge raises significant investor protection and corporate governance concerns."

"Without transparency, executives are free to spend funds invested by shareholders without accountability or monitoring," they wrote. "They might use corporate resources to support political candidates whose positions are directly adverse to shareholder interests, such as a candidate who supports repealing corporate disclosure and shareholder voting protections. An executive might also spend money invested by shareholders to further his or her own personal ambitions unconnected to the best interests of the company – for example, by supporting the campaign of a candidate who the executive hopes will appoint him or her to political office. Whether executives want to use their personal funds for these purposes is up to them, but they should not be able to also use shareholders' money, especially without shareholders' knowledge."

In the House, 79 members of Congress (including several California members), led by Rep. Michael Capuano, D-Mass., sent a similar letter to White on January 9.

"A corporation's money belongs to the shareholders," they wrote. "While we believe that shareholders ultimately deserve a voice and a say if their money is going to be spent on political activity, a positive first step would be disclosure of such spending. This is a straightforward and necessary action."

Menendez in April introduced the "Shareholder Protection Act" (S. 824), which would:

- Require a majority of shareholders to authorize an overall political budget before general treasury funds could be spent on political activities.
- Require a Board of Directors vote to authorize all expenditures of more than $50,000 within the overall budget approved by shareholders.
- Require the disclosure of corporate political spending to shareholders, the SEC and the public on a quarterly basis, and online disclosure of board approval of significant expenditures within 48 hours.
- Rep. Michael Capuano, D-Mass., proposed the same legislation (H.R. 1734) in the House in April. Neither bill has made it out of committee. Menendez and Capuano also unsuccessfully proposed the measure during the previous session of Congress.

Yellen Confirmed as Federal Reserve Chairman

The Senate on January 6 confirmed Janet Yellen to become chairman of the Federal Reserve.

With the 56-26 vote, Yellen, who is now the Fed's vice chair, will become the first woman to lead the nation's central bank after Chairman Ben Bernanke's term ends on January 31.

Yellen is approaching the job with optimism, having told *Time* in a post-confirmation vote interview that appears in the magazine's January 20 issue, "I think we'll see stronger growth this year" and saying she is hoping for 3 percent growth in 2014.

"The recovery has been frustratingly slow, but we're making progress in getting people back to work, and I anticipate that inflation will move back toward our longer-run goal of 2 percent," Yellen said.

Following the confirmation vote, House Financial Services Committee Ranking Democrat Maxine Waters said that "the U.S. Senate has not only made history, but has put in place a Federal Reserve leader who will be a careful steward of our nation's economy."

"Ms. Yellen's unique understanding of the impact of the Federal Reserve's policies on the middle class will ensure the crucial pursuit of both stable prices and low unemployment," Waters said. "Her judgment on the economy has been validated time and again. Before the crisis, she saw the bubble for what it was and predicted disaster in the banking system.

When the crisis actually happened, she advocated for the urgent need to implement financial reform quickly in order to avoid another meltdown, which was vitally important to staunch the bleeding."

Yellen told members of the Senate Banking, Housing and Urban Affairs Committee during a nomination hearing on November 14 that she supports the Fed's aggressive actions to stimulate the economy and that she credits "the wise and skillful leadership" of Bernanke for helping to "stabilize the financial system, arrest the steep fall in the economy and restart growth."

Yellen is regarded as a supporter of "loose" monetary policies aimed at lowering unemployment, and she has broad support among liberals. Many conservatives, though, fear that a Yellen-led Federal Reserve will drive up inflation.

Waters and 37 Democratic colleagues, all of them women, including 14 from California, wrote to Obama in July to ask him to consider Yellen, a professor emeritus at the University of California at Berkeley, as Bernanke's replacement.

CalPERS Asks Lawmakers to Oppose Mandatory Arbitration Provisions Favored by Some Corporations

CalPERS on December 12 wrote to lawmakers to express concern about "efforts to force shareholders into any system which limits their rights or ability to seek legal remedies against issuers involved in corporate malfeasance."

Noting that some public companies have begun inserting mandatory arbitration clauses in investor advisor agreements, corporate bylaws and other contracts, CalPERS Senior Portfolio Manager Anne Simpson wrote in a letter to leaders of the Senate Judiciary Committee and the Senate Banking, Housing and Urban Affairs Committee that such requirements negatively affect the ability of shareholders to hold companies accountable for misdeeds.

"Such provisions force all shareholder disputes into arbitrations controlled by the very same corporations against whom the claims are being brought and these forced arbitration clauses typically require shareholders to waive their rights to participate in any collective or class action," Simpson wrote. "In sum, forced arbitration schemes, particularly schemes that bar class action, cannot supplant judicial enforcement of fiduciary duties owed to shareowners."

Simpson asked the lawmakers to support potential efforts by the Securities and Exchange Commission (SEC) to use authority granted to it by the 2010 Dodd-Frank Act to prohibit such arbitration provisions in investor advisor agreements and to formalize the SEC's policy against mandatory arbitration provisions in corporate bylaws and governing documents. The SEC has not yet used the authority it gained in Dodd-Frank.

On December 11, the Council of Institutional Investors (CII) wrote to two SEC division directors to "bring to your attention a recent potential trend in corporate governance that may not only impair shareowners' rights, but also threaten to undermine the integrity of our public markets generally."

"It is our understanding that some corporations may have already begun to explore forced arbitration provisions in their chartered bylaws as a potential vehicle to limit shareowner rights," CII General Counsel Jeff Mahoney wrote. "As you are well aware, bylaw provisions can be adopted unilaterally by corporate boards without shareowner approval. As a result, forced arbitration provisions in corporate bylaws represent a potential threat to principles of sound corporate governance that balance the rights of shareowners against the responsibility of corporate managers to run the business."

Mahoney asked that the SEC "continue to remain vigilant in exercising its well-founded and long-held opposition to such provisions as being contrary to the anti-waiver provisions of the federal securities laws."

In April, SEC Commissioner Luis Aguilar said that "the Commission needs to be proactive" in prohibiting mandatory arbitration provisions.

"My main concern with pre-dispute mandatory arbitration is the denial of investor choice," Aguilar said at a North American Securities Administrators Association conference. "Investors should not have their option of choosing between arbitration and the traditional judicial process taken away from them at the very beginning of their relationship with their brokers and advisers."

Also in April, Sen. Al Franken, D-Minn., along with 14 other senators and 22 members of Congress, wrote to SEC Commissioner Mary Jo White to "express our strong belief" that the SEC should use its new authority.

"To our disappointment, in the almost three years since the Dodd-Frank Act's enactment, the Commission has largely disregarded this important mandate," they wrote. "The time is ripe for the Commission to act ... to protect the investing public and prevent further abuse of forced arbitration contracts. ... We are deeply concerned that the Commission's failure to respond to the dangers posed by widespread forced arbitration will weaken existing investor protections."

Democratic Reps. Jared Huffman and Judy Chu were the only members of the California delegation to sign the Franken letter.

Social Security Trust Fund to Be Exhausted by 2031: CBO

Social Security's trust fund will be exhausted in 18 years, the Congressional Budget Office (CBO) projected in December.

Social Security's expenditures started exceeding its revenues (excluding trust fund interest) in 2010, and CBO estimated that the program will run a deficit equal to about 12 percent of its tax revenues each year during the next decade. As more baby boomers retire, that number will grow to more than 30 percent by 2030. To cover the shortfall, the Social Security Administration will have to draw down increasing amounts of funds from the program's trust fund – actually two funds for retirement insurance and disability insurance that are commonly considered to be combined – until the fund has a zero balance, which CBO projects will occur, in the absence of legislative changes, in 2031.

CBO estimated that Social Security's 75-year shortfall is equivalent to 3.36 percent of taxable payroll, a big jump from the 1.95 percent that was estimated in 2012. More than 40 percent of the increase results from CBO using different projections of life expectancy, and nearly 30 percent results from changes in income tax rates that were enacted in January of this year.

In fiscal year 2013, Social Security expenditures totaled $808 billion, nearly a quarter of all spending by the federal government. It took in $745 billion, more than a fourth of all federal revenues.

In May, Social Security trustees released a report that projected that the program's trust fund will last until 2033. It estimated that the program's actuarial deficit over the next 75 years will be 2.72 percent of taxable payroll, 0.05 percentage points higher than in the 2012 report.

Requiring all newly-hired state and local public-sector workers to participate in Social Security is frequently mentioned as a possible partial solution to the program's financial problems, including at a May 23 hearing of a subcommittee of the House Ways and Means Committee. Studies have shown, though, that this measure would eliminate just 8 percent of Social Security's long-term deficit, while imposing new fiscal demands on states and localities that could lead to higher taxes or cuts in government services and could also destabilize existing public pension retirement plans.

RELATED NATIONAL AND INDUSTRY NEWS

Report Recommends Reforms to Address 'Troubling' Public Pension Funding Issues

A new report that is critical of public pensions recommends that funds reduce their discount rates and levels of investment risk.

"Strengthening the Security of Public Sector Defined Benefit Plans" from the Nelson A. Rockefeller Institute of Government begins by asserting in its first sentence that, "The condition of state and local government pension funding is troubling." It reports underfunding of "$2-4 trillion," and cites multiple problems with public funds, including "a deeply flawed funding approach," "inaccurate financial reporting" and "incentives to take investment risk."

The report includes five recommendations:

- **Use a risk-free discount rate:** "Discounting at risk-free rates is likely to result in at least a $2 trillion increase in reported liabilities for state and local governments in the United States. The estimate of annual pension expense – what governments would have to pay if they were to fully fund pensions without taking investment risk – is likely to increase by more than $100 billion. This change would not be a funding requirement; rather it would be disclosure of pertinent information. This is as it should be: governments, taxpayers, and others should know the full cost of promises that have been made, and what it could take to fund those promises without risk. Full disclosure could be the basis of political support and a predicate for legislative changes."
- **Increase disclosure of the consequences of investments:** "When investment returns fall short, they can require very large increases in contributions, and governments make these contributions if they are to keep their side of the bargain. But large increases in required contributions invariably come when governments are least able to afford them, and crowd out other services and investments of government, or require tax increases. And they erode public support for public sector pension benefits, and for the public sector workforce."
- **Apply external downward pressure on levels of investment risk:** "Because public pension funds have approximately two-thirds of their assets in equity-like investments, have become increasingly large, and have increasingly maturing memberships, the potential consequences of this risk are far greater now than in the past. There must be external pressure to moderate these risks."
- **Ensure regular payment of "realistic actuarially determined contributions based on realistic assumptions":** "If governments and pension funds will not do this on their own, the federal government should consider creating incentives to encourage this."
- **Consider federal "options for ensuring a smoother functioning system of state and local pension plans":** "if states and standards-setting bodies do not go far enough on their own, the federal government should consider more intrusive action to monitor and police state and local government retirement systems. Congress may wish to employ small carrots and large sticks to encourage transparency in pension fund reporting, disclosure of investment risk, and discipline in pension contributions [sic]."

"If governments and pension funds follow these recommendations, required pension contributions are likely to rise significantly [sic], depending on the risk tolerance of the governments involved," the report stated. "The sooner governments begin this process, the more time they can take to get on a path toward safer and more secure funding of benefits. This will undoubtedly create pressure to cut services, raise taxes, and even lower benefits. It certainly will create pressure to reduce benefits for new hires. But the alternative is to continue blithely, ignoring risk, simply hoping things turn out well, with great risk of paying much more or, at the municipal level, becoming insolvent."

California Congressional Delegation News

Three Veteran California Lawmakers to Retire from Congress

Three California congressman with more than a century of combined experience announced in January that they will not seek reelection this year.

House Energy and Commerce Committee Ranking Democrat Henry Waxman said on January 30 that he will retire after 40 years in Congress.

"The reason for my decision is simple," Waxman said. "After 40 years in Congress, it's time for someone else to have the chance to make his or her mark, ideally someone who is young enough to make the long-term commitment that's required for real legislative success. … Public office is not the only way to serve, and I want to explore other avenues while I still can."

Waxman, who represents California's 33rd District in Los Angeles County, has been a leader on health care and environmental issues. He was a driving force behind the 2010 Patient Protection and Affordable Care Act, and a key 1984 law that increased the availability of generic drugs – the Hatch-Waxman Act – bears his name.

House Education and the Workforce Committee Ranking Democrat George Miller, who represents part of the San Francisco Bay area in the 11th district, announced on January 13 that he will leave Washington after 40 years.

"I'm proud of what I have been able to accomplish on behalf of children and families, working people and the environment, in my district and for our country, especially passage of national health care reform," Miller said.

Three days later, House Armed Services Committee Chairman Howard "Buck" McKeon, a Republican who represents parts of Los Angeles County and Ventura County in the 25th district, said that he will retire from Congress after 22 years.

"For me, it's time to walk away," McKeon said.

Waxman and Miller are the House's last two continuously serving members of the Watergate class of 1974.

California Senator Co-Founds Climate Change Group

A California senator on January 9 said she is helping to launch a new effort aimed at getting Congress to enact climate change legislation.

Senate Environment and Public Works Committee Chairman Barbara Boxer, D-Calif., and Sen. Sheldon Whitehouse, D-R.I., announced the formation of the Climate Action Task

Force. The senators said that the group will seek, among other things, to enact legislation that would implement a cap-and-trade framework for carbon emissions, support President Obama's Climate Action Plan, protect states that have implemented carbon taxes and promote energy efficiency and enhanced fuel economy.

"The goal is to wake up Congress. ... We believe that climate change is a catastrophe that is unfolding before our eyes, and we want Congress to take off the blindfolds," Boxer said.

Boxer and Whitehouse appear to have the support of the Senate's Democratic leadership.

"I'm pleased that these and other senators are coming together to bring greater attention to climate change and extreme weather and the need to do something about it," Senate Majority Leader Harry Reid, D-Nev., said.

Boxer sponsored cap-and-trade legislation in 2009. Whitehouse in January 2013 formed the bicameral Task Force on Climate Change with House Energy and Commerce Committee Ranking Democrat Henry Waxman of California.