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# THE IMPACT OF SOCIO - ECONOMIC CHANGES ON EMPLOYEE BENEFITS

Moderator: RAYMOND E. PINCZKOWSKI, JR.
Panelists: THOMAS E. CAIN*
WILLIAM E. HEMBREE**
Recorder: LILY CHAO

- o Demographics and workforce composition
- o Lifestyles and attitudes
- o Cafeteria benefit programs
- o Defined contribution retirement plans
- o Health care

MR. WILLIAM E. HEMBREE: I'd like to cover two topics today: one is the social, demographic and economic changes occurring today and affecting our planning for overall employee benefits; the second is the influences that are changing our planning for medical care and health care cost containment.

For review, it is helpful for us to recognize some of the primary ways that the population and America itself is changing. Population growth is slowing. We're moving to the South and West. People are getting married later and that is affecting when and if they have children. There are more working women today than ever in the history of the United States. Women are entering the workforce, and in general, are more educated. Corporate farming, being what it is, probably will not see a great deal more people move out to the rural areas.

Family size is down, especially since the post-World War II era. In the "baby boom" period right after World War II, family size was about 3.8. By 1970, it dropped to about 3.1 and by 1983, to about 1.7. Studies not long ago indicated that fully 25 percent of those surveyed are planning no children whatsoever, another 25 percent, which with the

*Thomas E. Cain, not a member of the Society, is Vice President of Corporate Human Resources with Comerica, Inc.
** William E. Hembree, not a member of the Society, is Director of the Health Research Institute.

first group makes up 50 percent of the next generation of families, are planning only one child. That has implications for employee benefit planning and certainly for paying retiree medicare costs and the costs of the medical care programs. Birth rate is slowing down from eighteen per thousand to about fifteen per thousand over just a thirteen-year period. The population is better educated; more people have graduated from high school and college. Values and beliefs have changed. Lifestyle changes will affect employee benefits, in general, as well as health care and health care planning. The population is getting older.

Life expectancy at birth, is about 74.5 years today; at age sixty-five a person might expect to live nearly seventeen more years. The population over the next sixty years is expected to grow by 100 million people. It'll go from about 232 million to 328 million people. That growth is not proportionate between people who are under age sixty-five and people who are over age sixty-five. Under age sixty-five will grow from about 206 million to 261 million, and those who are over age sixty-five will grow from 25 million to about 67 million. This will have a great effect on the demographics of the social security system and, most notably, the medicare part of the social security system. When social security was first established in 1935, there were about ten active workers for every person over age sixty-five. That's dropped to about five per active worker. By the time we're all hoping to be out there fishing around the lake and having somebody else pay the social security bill, it'll be somewhere in the neighborhood of two to one. If people are paying 14 percent for social security today, when there are five active workers for each person over sixty-five paying, try to think what that might mean in terms of the tax rate necessary to support the social security and medicare systems when there might be somewhere in the neighborhood of two active workers for each of us who is over age sixty-five. While we'll be a voting block, we may not be a majority which should be a concern.

The impact of population aging on health care utilization is important. The number of hospital days used will increase from one-quarter billion to about one-half billion by the year 2040. The category over age sixty-five shows an increase from 105 million days being used today to about 312 million: fully a tripling of costs. One reason is that more people are living past sixty-five, and this is a continuing trend. In the year 2040, even in constant 1980 dollars, we can expect overall medical care costs to increase from 1980's $219 billion up to about $369 billion with a greatly disproportionate part in the over age sixty-five category.

People who are over age sixty-five use medical care, goods, and services to a greater extent than people who are under age sixty-five. Today, about 11 or 12 percent of the population is over age sixty-five, and yet that population uses abut 30 percent of all medical care expenditures in the country. They represent 35 percent of all hospital days, and by the time we get to the year 2040, when they will be about 21 percent of the population, we expect the over sixty-five category to account for about 50 percent of all expenditures for medical care. Almost half of all people in the over age sixty-five category live

in seven states: California, New York, Florida, Illinois, Ohio, Texas and Pennsylvania. Those states will have a disproportionately larger medicare load, as in Florida today. Seventeen percent of Florida's population is over age sixty-five. When this nation has 21 percent of its population over age sixty-five, Florida's problems will look like child's play. A very small proportion of medicare recipients are the ones who are the largest users of the medicare system. Six percent of all medicare recipients constitute about one third of all the medicare cost in any given year.

There's another trend that causes concern about what medical care costs will be ten, twenty, or thirty years from now. People are living longer. The chief causes of death one hundred years ago are no longer chief causes of death. Heart disease, cancer and stroke, which are essentially lifestyle-associated diseases, are the diseases that kill people today.

There are a number of surveys on beliefs about health. The Yankelovich poll that was done about one and a half years ago asked people what methods they believed were appropriate to control health care costs. One of the most predominant findings was the need to deal effectively with stress. As employers, we'll all be faced with dealing with peoples' lifestyle problems and issues, particularly in stress management. Eighty of the respondents to the Yankelovich poll said that stress was one of their greatest concerns. Stress and illness are related. Some respondents indicated that they were cutting back on health-related items to cope with inflation. Cancer is a definite concern. Heart disease mortality is going down, but cancer mortality is going up. People don't exercise enough. There's rejection of many traditional values; we're seeing alcoholism as an emotional weakness, not as a health problem. There is a lot of misconception on the part of the public that affects our medical care costs. One of the most important things that we as employers will do differently in the future is to educate employees about health. What is it that causes them to become ill in the first place? Crocker Bank in San Francisco, has an excellent preretirement counseling program that includes a discussion of the kinds of changes that happen to an individual. That's one of the most important and valued parts of their preretirement counseling program. People believe there is a fundamental need to deal with the reasons for high medical care costs, but that access to medical care should not deteriorate. These needs run counter to each other sometimes. New technology, lack of competition, and more use of medical care have raised costs. The respondents were quite willing to become part of cost containment activities listed in the study - cost sharing being one of them.

Physicians responded that they liked the present conditions and that a tax cap on employer premiums would probably be one of the best ways of getting health care costs under control.

There is a very important change taking place to the demographics of health care because of the aging of the population and people living longer, but just because people have a different and more responsible view toward their own health. Today's emphasis in health care is on

disease; trying to cure the disease once it occurs. Tomorrow's will be on wellness, health improvement, prevention, those types of activities.

Today's emphasis on surgery and drugs will change to an emphasis on health education. Today's emphasis on cure will change to a perspective, of prevention, of life-long learning, life extension, and quality of life. Technology will change from the coldness of new technology to the human touch, and more warmth and friendliness within the system; from use, almost exclusively, of physicians, to one of using many more non-physicians. And from a hospital or institutional-centered approach to the delivery of care, to one of much less use of hospitals. Many of these kinds of changes are responses to demographic changes, as well as the changes in people's lifestyles and their greater sense of self-reliance.

MR. RAYMOND E. PINCZKOWSKI JR.: The bottom line to my message in the retirement plan area is that the socio-economic changes are driving employers and employees away from the traditional defined benefit plan and toward the defined contribution plan. Indeed, the IRS statistics for the first nine months of 1984, showed that in terms of new plans and participants in new retirement plans, more than 80 percent were participants in defined contribution plans.

A major economic trend is the change away from the traditional, large, smoke-stack United States corporate employer. General Motors supported the removal of limits on Japanese car imports according to economists because GM wants to be able to build their own cars in Japan and import them to the United States; therefore, the removal of those limits was self-serving to GM. This is an example of a change toward a new economic climate. Change away from a traditional, large, smoke-stack United States. The general erosion of the close-knit social communities is an example of a sociological change. We had company towns with closer family ties and employer/employee relationships than today.

Employee attitudes have changed markedly in the past twenty-five years. Employees don't assume that they will stay with their current employer until retirement. In fact, they might not even stay until they are vested, which is a dramatic change from employee attitudes twenty and thirty years ago. In fact, employees perceive that many employers won't last as long as the employees. There is a geographic shift of employees to the sunbelt. People are changing occupations in the course of their work career and are changing employers for a new experience.

In short, employees desire cash and vesting now. That's not new, of course, but what is new is that employees are more vocal about it, and are being heard more clearly in the executive suites. Books like <u>Future Shock</u>, <u>Megatrends</u>, and <u>In Search of Excellence</u> tell us technological changes and a faster rate of change are having an important impact on the employee work force. They are contributing to the lessening of ties to and dependence upon the employer. Defined

benefit plans, of course, favor the older and longer service employees. They are designed to reward long service with a single employer and keep or tie the employee to the employer. This defined benefit plan philosophy runs counter to current sociological changes. Since employees have never really understood defined benefit plans, sociological changes are leading employees away from defined benefit plans and toward defined contribution plans.

Employees have socio-economic concerns about social security. They question whether society is going to continue to fund that program, and if benefit levels are going to be adequate. The initial social security replacement ratios upon retirement have actually been decreasing since 1981, and there is a lot of current concern about the federal deficit and freezing of social security's cost-of-living adjustments. This reflects a general concern about our economy. Alan Greenspan, the former chairman of the Council of Economic Advisors said that the cause of "merger-mania" is that stock prices are related to the present value of future dividend earnings of various companies. At today's high interest rates these stock prices are depressed. At these low prices an organization or individual can gain control of vast organizations and amounts of assets at very depressed prices. The bottom line to the merger-mania is control of these enterprises, rather than anything economically related to the intrinsic value of the stocks.

Similarly, employees want control of their assets and, defined contribution plans give them a much greater degree of control than defined benefit plans. An employee who is aware of these phenomena wants control of his assets to invest them at current high interest rates.

Defined contribution plans offer employees a chance for significant gains from good investment experience - not available in the typical defined benefit plan. More than 70 percent of employee-directed defined contribution plan investments, where employees are given an option among several investment options, go into guaranteed investment arrangements. Seventy percent may not sound like very much control or much of an entrepreneurial attitude on the part of employees, but you need to contrast that 70 percent with the virtual 100 percent in defined benefit plans. Employees have no investment opportunities in defined benefit plans. The 70 percent figure does indicate that there are a substantial number of employees interested in more aggressively directing the investment of their own money. Surveys indicate, however, that the 70 percent is steadily going down, indicating an increasing degree of interest on the part of employees in directing their own investments. Similarly, nearly 90 percent of IRA money initially went to the banks and savings and loan companies and was tied up in high interest certificates. Today banks and savings and loan companies are advertising aggressively because they are losing market share. That money is going into employee-directed investments other than high fixed-interest types of certificates. The government has substantially eased the rules for setting up employee-directed brokerage accounts for IRAs; it will be interesting to see how much more activity there is in employee-directed IRAs in the next few years.

President Reagan, ringing the bell to start trading on Wall Street, said that this is "the age of the entrepreneur, the age of the individual, this is where American prosperity is coming from now." This as further evidence of interest for employees to have more control over their own destiny and, greater interest in defined contribution plans. That's not to deny that the tax aspects of 401(k) plans for employee money are not important. They certainly are: current income tax savings, tax-free accumulation before retirement (even on after-tax employee contributions), and, ten-year forward averaging for distributions.

There is also an investment risk. In 1974, the equity markets dropped and gave up 25 percent of their market value. That risk is still there. Also, a new risk is that accountants will succeed in converting unfunded pension liabilities into balance sheet debt.

What about the extra benefit and administrative costs of defined benefit plans? In effect ERISA said that no act of generosity would go unpunished. Employers that don't have defined benefit plans are exempt from ERISA. Public sector employers are exempt from ERISA. But, an employer that has such a plan has minimum and maximum funding requirements, vesting requirements, investment restrictions, reporting and disclosure requirements, mandatory survivor benefits, and, if in a multi-employer plan, he has to worry about unfunded vested benefits and withdrawal liabilities. The essence of TEFRA, the Tax Reform Act and the Retirement Equity Act, is not much large costs for additional benefits, but rather a large cost for administration in terms of amending plans, notifying employees, and keeping track of such notices. Currently one worries about whether Pension Benefit Guaranty Corporation (PBGC) premiums will triple, whether one will be able to terminate a plan, and will asset reversions be restricted or prohibited? The lessening of inflation and the surge in the investment markets in the last five years leave most current defined benefit plans well funded. The question for the plan sponsor is "where will we put new money?" The famous economic law is that all decisions are made on the margin, and I suggest that this is exactly such a situation. Those decisions are being made in favor of defined contribution plans, rather than defined benefit plans or newer or increased defined benefit plans. More than 90 percent of the "Fortune 500" have already adopted 401(k) plans. The employer is basically asking why he should increase his financial risk and his inflation risk through his defined benefit plan; why he should incur more administrative expenses, and so on. Employees perceive little or no value in the defined benefit plan. The employees make that known in the executive suite. The employer then questions the value of his contributions to fund these benefits when the employees don't appreciate them, when he's underwriting the risks of inflation and of the investment markets, when he's worried about possible legislative tinkering and whether or not the accountants will convert his promises into long-term debt. The employer finds it easy to adopt a defined contribution plan. Typically it has lower risk and lower cost, and the employees will love him for it. It's especially easy when his competitors are also adopting such defined contribution plans.

MR. THOMAS E. CAIN: Comerica is a bank holding company which currently has eighteen banks and ten financial companies. It is

headquartered in Detroit, Michigan. Comerica has been in existence for 130 years, but it primarily serves the state of Michigan. Currently it has about 6,700 employees. Comerica implemented its flexible compensation or "cafeteria" plan on January 1, 1983. We call it Custom-Comp to communicate the idea that it gives employees the ability to customize their total compensation. Comerica's motivation for implementing the Custom-Comp program derived from several elements. We completed a relative value study, the results of which indicated that we weren't as competitive as we thought with our peers. For example, we didn't have a profit sharing or thrift plan. On employee morale, the employee attitude/opinion survey asked all kinds of prying questions like "is your pay enough?" and "is it too much?" Included in that survey were questions about benefits. It was clear that the staff did not perceive the value or cost of their benefits. Another consideration, of course, was health care costs and benefit costs in general. A cafeteria plan is an opportunity to regain cost control. In the Detroit area, companies pay for all benefits; there are no employee contributions. In health, dental, and so on, we pay for both the employees and their dependents. This is kind of mandated by the United Auto Workers for the Big Three and their suppliers. So part of our motivation, was to regain cost control.

But perhaps the most important element of our motivation was the honest realization that the millions that we were spending for benefits were not meeting individual needs. The attitude survey told us the employees didn't perceive it as a value. They didn't realize or appreciate that changing demographics in the workforce have a real impact on employers and certainly on banks.

The Census Bureau tells us that over 46 percent of women with children under age six are in the work force, and that 63 percent of women with children between the ages of six and seventeen are working. Over 50 percent of the work force is under age thirty-five. We looked very closely at our own Comerica demographics. Forty percent of our staff is single; 73 percent of our staff is female; 60 percent of our staff is under age thirty-five. The so-called traditional family, where Dad works and Mother is home with the children, makes up less than 8 percent of Comerica's population. When you really think about it, I guess, the older the company, the more likely that the benefit plans were designed for that so-called traditional family.

Another growing category appears to be the single parent. At Comerica, nearly 10 percent of our staff fall into that category. With our so-called fixed or standard benefit package, we were not meeting the individual needs of single parent families. Like any employer, Comerica has limited resources to spend for compensation: a piece for salary and a piece for benefits. Obviously, one reasonable solution is to not have a fixed benefit package but to simply give employees money and let them elect what they want which is an over-simplification of our cafeteria plan motivation.

The critical item in setting up a cafeteria plan is benefit design, so it's important to know your staff's demographics. At Comerica, we had a Blue-Cross/Blue-Shield medical plan and the typical major medical plan

with a one hundred dollar deductible and 80 percent copayment. We had had a great deal of pressure from our employees to increase that plan's benefits because other employers in the area have the same Blue Cross plan but endless riders to their plans that pay for everything.

Some employees wanted a more comprehensive plan, not realizing that our first-dollar medical plan was already generous. Some employees didn't want as comprehensive a plan once they realized the cost of it, or if they would have an opportunity to take a lower level of benefits plan and recapture some dollars. A third group didn't want any coverage at all. Remember that in an environment where the employer pays the full cost employees sign up for the medical plan whether they want it or not because they may lose something if they don't. So at opposite ends of the spectrum we had a cry for increased benefit levels and no plan at all, but if employees were going to give up the medical plan, they wanted something in return.

Prior to the implementation of our Custom-Comp program, everybody had at least two times their pay as a life insurance amount. In the Custom-Comp program, employees can choose as little as one-half times pay or multiples of one, two, three, or four times pay. Single employees predictably didn't want as much as they had had, they reduced the amount of their life insurance substantially. Young couples forming families increased their coverage, as did single parents. Older employees reduced their life insurance amount; they chose to take life insurance dollars and apply them to other benefits, like the 401(k) plan.

Prior to the implementation of our Custom-Comp program, everybody had a long-term disability (LTD) benefit of 60 percent of pay. The choices we offered them were as little as 50 percent of pay, the standard 60 percent, or they could have 70 percent of pay. Single people generally took less life insurance, but they increased their LTD coverage. Obviously, a single person has no beneficiary but if they are disabled they don't have anyone to support them.

For vacations, a very happy topic, we were a typical company with the number of days or weeks of vacation predicated on seniority. In our Custom-Comp program we let them buy or sell vacation days. They could buy or sell up to an additional week of vacation. Predictably the younger employees generally bought more time off. Older employees sold vacation to buy more of the 401 (k) plan. After three years of Custom-Comp enrollments, of the number of people entitled to three weeks vacation, almost an identical number bought a week as sold a week of vacation.

Remember the infamous IRS newsletter about reimbursement accounts? Reimbursement accounts were added to our Custom-Comp plan: one for health care and another for child care. Employees with a health care reimbursement account can pay their deductibles and co-payments. In our dental program, for example, the orthodonture is paid at 50 percent, so the other 50 percent is a very predictable expense for the employee. It's also an opportunity to get a tax advantage for benefits that are not covered. For example, we don't have a vision care plan at

Comerica. Many of our employees are young women who use the child care and dependent care reimbursement. We also have a lot of working couples and young couples, so reimbursement accounts aren't just a tax advantage for the individual. A reimbursement account included in a cafeteria plan gives the individual the opportunity to free up some other dollars. For example, if a young couple has a child in the day care center, our employee could give up the medical plan and put those dollars into a child care reimbursement account.

In January of 1983 we added a new 401(k) benefit to our Custom-Comp plan, which is a tax-sheltered way to save. There is a modest corporate match of 20 percent on the first $2,000, and a loan provision based on the temporary regulations to try to motivate younger employees to participate.

Benefit design is really a question of knowing and understanding your employees and then trying to fill their individual needs. Our employee reactions after two years and three months of our program are exceedingly positive. This in spite of the expectation of many of Comerica's management people, who said that employees would never be able to understand 401(k). Employees' reactions are that they love choice. 401(k) improved our rapport with employees, which is of intangible value. With a fixed benefit program, it's more of a teacher/student or parent/child relationship. When you give the employee the money to choose, you're treating them in a more adult way.

We repeated the attitude/opinion survey in one of our small banks right after the implementation of our Custom-Comp program in 1983 and the questions relating to benefits came out 98.2 percent positive. The fact that 98.2 percent of them would agree on anything was kind of startling. However, we are looking for that 1.8 percent to reassign to one of our competitor banks. At Comerica, we have regained control of benefit expenses. The corporation has the ability to meet a greater scope of employees' needs. If we can't buy every benefit for every employee, we can at least make them available. That element of choice permits employees to pick what best fits their needs.

In the current national debate over the federal budget deficit and the taxation of employee benefits, the worst case would be that all employee benefits would be taxed. If that occurred, employees everywhere would raise a loud cry, particularly those in fixed or standard benefit programs that they maybe didn't want, didn't need, and didn't choose. A flexible compensation or cafeteria plan shows that employers are aware of the changing demographics of the work force and socio-economic changes, and that flexible benefits provide an economically sound vehicle to deliver employee benefits.

MR. EDWARD H. FRIEND: What does the panel think opinion surveys will show in fifteen years, as the employee demographics change, employee groups age, and the equity markets drop another 25 percent, which would reduce the new defined contribution balances dramatically. Employees want choice and the opportunity to see those accounts grow, but we have to balance that with needs in the future. Defined

contribution balances will either over provide by building up sums of money far more than we intend to give the employee, or they will under provide. If they over provide, employers will be concerned about putting too much money into the programs for the retirement of employees. If they under provide, the employees will be clamoring for supplemental sums. The target is to replace preretirement income, inclusive of social security, and defined contribution plans just cannot do this. Employees are not interested in this fact. The employee today is interested in accumulation, and this puts a particularly heavy burden on actuaries who must design these creatures. The employee wants control, but with that control goes a significant amount of burden. Perhaps one of the answers to the matter of vesting is a price-adjusted benefit, something that this nation has never embraced. Canada and Great Britain are looking at this, but it's a very expensive proposition. But perhaps it's not as expensive as putting a lot of money into defined contribution plans which will build tremendous sums. There is concern over the possible bankruptcy or failure of the social security system. The Congress of this United States is not going to permit it to happen. Clearly there are going to be heavier burdens. We are going to increase the retirement age to sixty-five, to sixty-seven, to seventy, to get the proper proportions of retired and active workers.

MR. ROBERT J. MYERS: I noticed that Mr. Pinczkowski very carefully said that there was considerable public concern about the liability of the social security system; he did not say that he was concerned. I, of course, agree with Mr. Friend that the system is viable and will be in the future. Mr. Hembree pointed out the increasing load on the cash benefits and medicare portions of the social security program over the next fifty-five years, up to the year 2040. Because a considerable part of this increasing burden is going to result from increased life expectancy, wouldn't it make sense to define the definition of aged not on the static basis of sixty-five but rather on a more dynamic or flexible basis so that the largest part of the burden that you indicate won't really arise if people consider the normal retirement age to be seventy or so. We've taken a timid step in this direction, to make age sixty-seven the normal retirement age in 2027.

MR. HEMBREE: There is little question in my mind that the eligibility age for medicare will change. I think it'll move out because I'm not sure that as a nation we're going to be quite as willing to fund the costs of the medicare portion of social security as we have been in the past. Eligibility for benefits then could be based on a lot of things other than age.

Some people are able to accumulate enough wealth and resources during their lives to be able to pay much more of their bills than the medicare system presently pays. I think that lifestyle-associated disease will have something to do with how people collect on employer plans as well as under the social security system, so I completely agree that we are going to change the way that we have eligibility established for the medicare part of social security.

MR. GREGORY W. PARKER: Mr. Cain, does Comerica's cafeteria plan

have an adequate administrative system and if so, how long did it take you to develop that system?

MR. CAIN: The administration system was shared. We got some technical help from a consulting firm who shared responsibility because the implementation time was exceedingly short. Our management reserves huge periods of time to make decisions, and once they've made their decisions they decree instant implementation. So it was a rushed kind of effort. It was through the efforts of a consulting firm and our own people internally that we shared the responsibilities. Slowly, those responsibilities have moved inside.

MR. JOSEPH W. MORAN: Mr. Cain does the Comerica cafeteria benefit program include any provision for an employee option with respect to the degree of commitment of the employer relating to the postretirement health care coverage that might be needed on a contingent basis as a supplement to the medicare program, which in the future will be of an uncertain degree of adequacy? This may be the thing that would respond to Mr. Friend's concern about the overadequacy of benefits accrued from a defined contribution retirement savings program.

MR. CAIN: Active employees make no selections or determinations of what they'd have as a retiree, and they re-elect or make their selections each year. At Comerica, we had been paying, and continue to pay, health care costs for our retirees, so there was no piece in this cafeteria plan for them. In the future there may be.

MR. MORAN: I was not trying to address the question of what current retirees have as benefits now. It's whether current actives have any control within the cafeteria program over what they will have in the future as retirees.

MR. CAIN: No, they do not other than their degree of participation, for example, in the 401(k). There's currently nothing they can elect as an employee that would influence their group life insurance amount or their medical care coverage as a retiree.

MR. CHARLES L. TROWBRIDGE: I'd like to address the question about the relative advantages of defined benefit and defined contribution plans. Mr. Pinczkowski in effect is saying, that defined benefit plans are under real duress these days, and that defined contribution plans threaten to take them over almost entirely. Thirty years ago, when pension plans were new, the question whether an employer might adopt a defined benefit or a defined contribution plan was posed under somewhat different circumstances. A lot of long-time employers had never had any kind of retirement plan at all. A corporation which up to say, 1975, had no retirement plan would use a defined benefit plan as it obviously solves the retirement problems for those long service, old-age employees and money purchase or any kind of defined contribution plan certainly doesn't because the number of years that these employees have to retirement is very short. Choices were made for defined benefit plans, as opposed to defined contribution plans, in those days, partially because defined contribution plans just couldn't do the job. They could do the job for new employees, but they couldn't

do the job for old employees that were already there. Now contrast that with the situation today. Employers with long-service employees and no retirement plan of any kind just don't exist. New plans are being adopted by new employers who don't have any long- service employees. And employers who do have long-service employees have some kind of plan from the past. There are some employers who now have defined benefit plans that are thinking of changing to defined contribution plans. New employees like this better, and older employees, although they can't get any credit for their past service under this new defined contribution plan, will get past service benefits from the old one. So the situation is simply reversed; the strong reasons at one time against defined contribution plans simply don't exist anymore. The demographic situation is largely just the passage of time. Since pension plans have been around a long time, the demographics have really changed the argument. Mr. Pinczkowski mentioned that accountants and the FASB are attempting to change the accounting for defined benefit pension plans. He mentioned that it would cause a real difficulty with the balance sheet. The FASB proposal would devastate defined benefit pension plans, the worst by the tremendous charge in the early years of new defined benefit pension plans. The FASB proposal means that nobody in his right mind should adopt or improve a defined benefit plan. The trend is going to be to defined contribution plans. I fear defined contribution plans, however, as currently constituted, are just not retirement plans. Ninety-nine to 100 percent of the people at retirement, if given the choice, are going to take cash, and that's simply going to mean there are a lot of people retiring without any pensions. Not that they don't have dollars available, but something is going to happen to it. Not only do most defined contribution plans allow people to take cash, but most of them don't give the option to do anything else. The one defined contribution plan that I think attempts to solve this problem, the TIAA-CREF, has always made it impossible to take cash and required the life insurance option, and now the Supreme Court is pretty well causing trouble on that, too. If defined contribution plans are going to be the wave of the future, we ought to solve this problem of converting cash to life income at retirement.

Mr. PINCZKOWSKI: The choice between defined benefit and defined contribution need not always be black and white. While each plan sponsor's situation is unique and the mix of the two is up to the plan sponsor, a frequent outcome that I've observed is that the employer will lower the rate of prospective defined benefit accrual rates and replace them with a 401(k) type of defined contribution plan.

MS. MARIA TRASKA: What does this trend toward defined contribution plans mean for health care providers; how is it going to affect them? And also, what is the likelihood that Congress will make medical IRAs available to consumers and how will that affect health care providers?

MR. PINCZKOWSKI: I long ago gave up pretending to know what Congress was going to do.

*Ms. Maria A. Traska, not a member of the Society, is Business and Finance Editor of Hospitals magazine.

Medical IRAs make eminent sense but overcoming the structure in order to implement those kinds of sensible things is difficult. My own prediction is that they will come to pass, but not very soon.

MR. HEMBREE: We'll see medical IRAs one of these days. Interestingly, there is a great deal more out-of-pocket expense for medical care paid for in this country than people realize. I think that if there's a way of tax protecting some of those funds then that is going to be an efficient way of using the tax structure. That runs counter to the Treasury Department's need for revenue. You asked how a trend away from defined benefit plans and toward defined contribution plans would affect the medical care provider. The two, while both part of the overall employee benefit plan for a company, serve very different kinds of purposes. In terms of making capital available to the medical care marketplace, there might be some changes, but the shift from a defined benefit to a defined contribution plan hasn't any effect on the provider community, outside of them as an employer. A hospital as an employer is the same as everyone else.

MR. ALFRED J. LEBEL: Was Comerica concerned at all at the outset of this with the effect of antiselection on the cost of benefits? Were there any special steps taken to avoid or adjust for that? What experience have you seen in that regard for the last several years?

MR. CAIN: We thought we would minimize adverse selection in design by forbidding illness and death in certain plans. That seemed to be actuarially sound. In our life insurance plan in our first year we had six active employees die, which is very unusual. But of the six, four had elected the same level of life insurance in the Custom-Comp program as they had prior to it. The other two had elected less life insurance. We let them do as they wished on life insurance and long-term disability (LTD) in the first year. We forewarned them that there would be statements of health and that sort of thing, which we utilized for the medical plan and for life and LTD. All we have is two years of experience which is a very short period of time. So far, for our comprehensive medical plan that was improved, the differential that was charged for that plan over the standard plan has paid for that additional cost.

MR. CHARLES WALLS: Mr. Cain, are there any benefits in your Custom-Comp plan that are required in the sense that you don't permit the employees to go without certain particular benefits?

MR. CAIN: Yes, there are a few minimum benefits required. In life insurance the minimal amount is one-half times salary, for the practical reason of what would we do if they died at their desk with no life insurance? In the health plan there is a required catastrophic plan with a huge deductible. In LTD the minimum is 50 percent of salary coverage. On vacation they have to keep at least a week. Those are "core" or minimal benefits.

MR. JAMES J. CONNORS: Mr. Cain you mentioned your health carrier was Blue Cross/Blue Shield. Do you know whether they've had any difficulty in adjusting to your plan and keeping track of who has which

benefits? How did they link those changes into their computer system?

MR. CAIN: Michigan Blue Cross/Blue Shield did have difficulty. In our initial structure the Blue Cross/Blue Shield coverage remained the same. We redesigned the major medical portion for that reason. Blue Cross/Blue Shield is now responding a little better and are able to do more of the administrative work. But initially, our adjustments were only on the major medical plan.

MR. CONNORS: Who covered the major medical?

MR. CAIN: That was a self-funded, self-administered plan by Comerica.

MR. CONNORS: Do you keep track of which employee has which level of benefits in your own system?

MR. CAIN: We keep track internally for daily, ongoing administration, and we can pay monthly premiums and process claims for plans that are insured.

MR. PINCZKOWSKI: In designing your plan, did you set elemental or aggregate cost objectives and were they met?

MR. CAIN: The task was really simplified to some degree in Comerica's plan design because a fundamental premise was that there would be no take-away for the staff. Comerica's management was willing to continue the same level of expense. It was a question then for new and additional items that the employees would, in essence, pay for themselves.

MR. FRANK WECK: What does this trend away from defined benefit plans and toward defined contribution plans mean in some of the governmental plans such as military pensions and municipal pensions for firemen and police?

MR. PINCZKOWSKI: I don't know what will happen, but I'd prefer to have input from some of the audience who have more experience in the public sector.

MR. TROWBRIDGE: There is a trend toward defined contribution plans, but I think it's entirely in the private sector. The reasons why people would move from defined benefit plans to defined contribution plans just don't apply in the public sector. Social security is not going to go to defined contribution and neither are the public service plans or military. The main reason is that employer choice is affected by the ERISA rules and by tax considerations.

MR. THOMAS P. BLEAKNEY:The trend to defined contribution plans should be looked at in the sense of what has happened in public plans because public plans go back a couple of generations. In the 1920s there were a lot of public plans started here in the United States. They were defined contribution plans and they were matching employee money with elaborate contribution schemes, but they were defined

contribution plans. They didn't work. Most of them did not provide the amount of money on retirement which would provide the proper replacement ratios.

As a consequence, they changed over the years to defined benefit plans. What we have right now, is a switching. We're now roughly a generation after defined benefit plans have been set up in the private sector, so they now have a defined benefit plan as a back-up. Brand new defined contribution plans are going to work a while in the private sector because people who retire, to the extent that they take an annuity, are going to have adequate funds. My prediction is that they will not work in the long run. We will learn the same thing in the private sector that was learned rather painfully in the public sector. Defined contribution plans provide too much variability in the output at the time of retirement and therefore retiring employees will be clamoring for more benefits and the employer is going to recognize that he's going to have to supplement this.

MR. BRYAN GILLESPIE: What trends do you now see in health benefit being provided by employers, like deductibles, coinsurance amounts, out-of-pocket maximums, which are likely to be part of health care cost containment programs or are underway now or are likely to come into plans in the next five or ten years?

MR. HEMBREE: There was tremendous activity by employers to get health care costs under control by having employees more involved in the cost of medical care. What more involvement meant was that employees would have to pay a larger portion of the bills, would understand and appreciate the enormity of the cost, and would therefore buy differently. The response has been that those who are relatively small consumers or purchasers of medical care, those who are comatose, and those who are in their last thirty days of life, have a tougher time buying differently and responding to cost sharing approaches. I believe that in the last year or two we've seen the the hey-day of shifting cost to employees.

Many employers will now start to look for different ways to control health care costs, such as to control utilization than to control costs.

MR. MORAN: This is one facet of the emerging adversarial relationship between the health care industry on the one hand and the people that pay for services, primarily government and employers, on the other. You made the comment that it appears that the peak has already been reached in the degree of employees' involvement in the effort to pursue that relationship and the effort to try to keep the health care segment of the economy from continuing to grow at an accelerated rate. What do you see as the best vehicle for pursuing that effort if employee financial involvement is not the answer?

MR. HEMBREE: I didn't mean that employee financial involvement isn't part of the answer, but that the difficulty is that the employee financial involvement didn't go nearly as far as it probably should have, if employers want employees to buy very much differently.