

Study of Retiree Health VEBAs

Recent agreements between several automobile manufacturers and the UAW to establish and manage Voluntary Employees' Beneficiary Associations (VEBAs)* to fund retiree health care have focused attention on VEBAs. In response, The Segal Company conducted a study of 25 stand-alone retiree health VEBAs, which represent a significant share of all stand-alone retiree health VEBAs at the time the study was conducted in late 2007. (Stand-alone VEBAs are less common than company-run VEBAs.)

All of the retiree health VEBAs in the study are related to the manufacturing, retail or transportation industries, and almost all of the VEBAs are Segal clients. This report presents the findings of this *Study of Retiree Health VEBAs*.

KEY FINDINGS

The following are among the key findings of the study:

- Historically, bankruptcy has been the most common reason for the formation of retiree health VEBAs, although collective bargaining is becoming a more prominent trigger.

* A VEBA, a trust fund vehicle governed by Section 501(c)(9) of the Internal Revenue Code, permits an employer to set aside funds for specific purposes only (e.g., life, sickness, accident or other benefits) for its participants. VEBA contributions can include employer contributions, active employee contributions (after-tax), and other assets. VEBAs can be company-run or stand-alone. Retiree health benefits paid from a VEBA are tax-free.

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- Although many retiree health VEBAs are new, some have been in existence for decades.
- Retiree health VEBAs are not only for very large retiree populations.
- The number of participants covered by a retiree health VEBA may grow by design.
- Retiree health VEBA funding is not limited to upfront company contributions. Many VEBAs in the study have ongoing funding streams.
- VEBAs are not limited to traditional retiree major medical/hospitalization and prescription drug coverage. Many

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VEBAs in the study offer other types of benefits in addition to or instead of that coverage, including Part B premium reimbursement, life insurance or health reimbursement accounts.

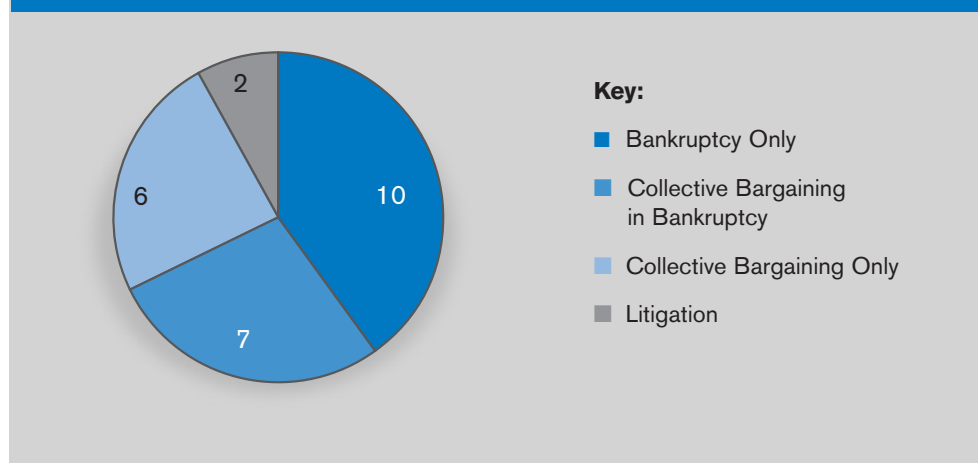
REASON FOR FORMATION

Bankruptcy alone was the reason for the formation of 10 of the 25 retiree health VEBAs in the study. Collective bargaining in bankruptcy accounted for an additional seven of the retiree health VEBAs. Graph 1 summarizes the reasons for the formation of all retiree health VEBAs in the study.

BOARD COMPOSITION

The *Study of Retiree Health VEBAs* found considerable variation in the composition of retiree health VEBA boards of trustees, which are sometimes called administrative boards or committees. Retiree health VEBA boards are more likely to include

Graph 1: Number of Retiree Health VEBAs by Reason for Formation



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retirees and union representatives than company appointees See Graph 2 for detailed data about the board composition of the retiree health VEBAs in the study.

ONGOING VS. TERMINATED

Most of the retiree health VEBAs in the study are ongoing (22), but three were terminated. The reasons for termination varied. In one instance, the VEBA was only intended to last for a limited period after which the company continued to provide retiree benefits. In another situation, the company had the contractual right to take over the VEBA, exercised that right, and by doing so had to guarantee benefit levels. In the third instance, the VEBA funds were exhausted.

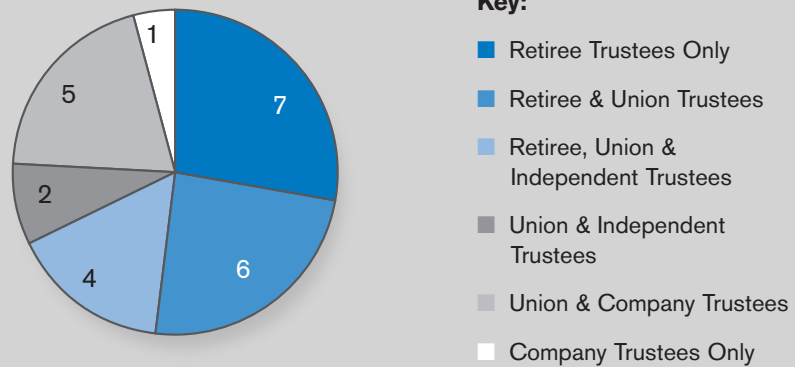
YEARS IN EXISTENCE

Confirming recent interest in retiree health VEBAs, almost one-third of the retiree health VEBAs in the study started in 2007 or will be starting in 2008. However, five of the retiree health VEBAs in the study have been around for at least 15 years. The oldest ongoing retiree health VEBA has been in existence for 26 years. Graph 3 shows the breakdown of the ongoing retiree health VEBAs in the study by years in existence.

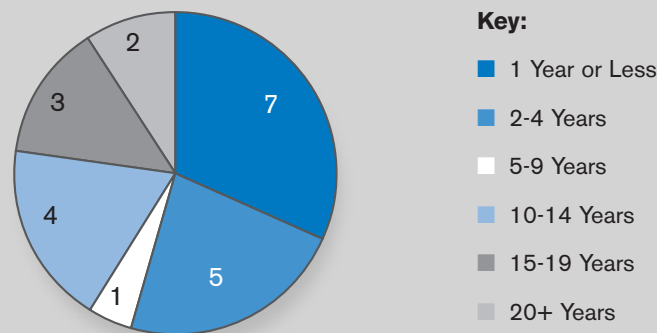
PARTICIPANTS

The number of participants covered by the ongoing retiree health VEBAs in the study varies widely. The largest covers 500,000 participants and the smallest covers 250. See Graph 4 for a breakdown by number of participants.

Graph 2: Number of Retiree Health VEBAs by Board Composition



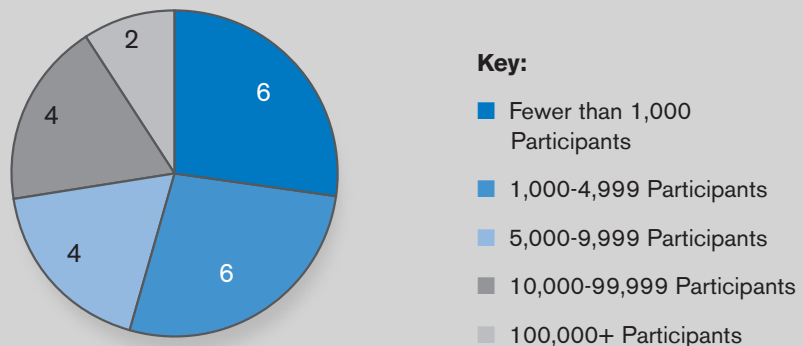
Graph 3: Number of Ongoing Retiree Health VEBAs* by Years in Existence**



* There are 22 ongoing retiree health VEBAs in the study.

** All three of the terminated retiree health VEBAs in the study had been in existence between five and nine years.

Graph 4: Number of Ongoing Retiree Health VEBAs* by Number of Participants



* There are 22 ongoing retiree health VEBAs in the study.

Most of the ongoing retiree health VEBAs (15 out of 22) provide coverage for a closed group of retirees only, however, seven health VEBAs allow active participants to retire into the plan.

ASSETS & INCOME

As with the number of participants, the assets held by the ongoing retiree health VEBAs in the study varies widely, from less than \$10 million to more than \$1.5 billion. Four retiree health VEBAs have assets of \$500 million or more. See Graph 5 for a breakdown by assets.

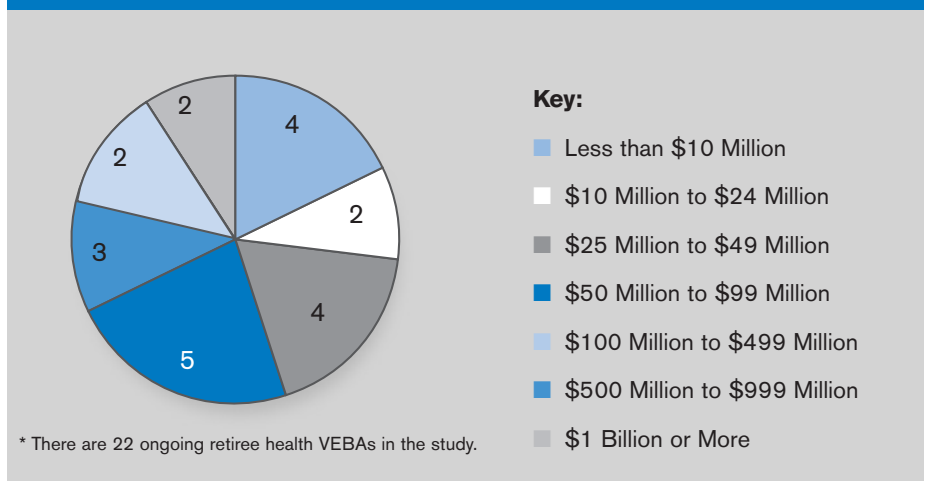
In addition to the current assets, nine of the ongoing retiree health VEBAs have either guaranteed or potential further income from a company. This additional income could come from fixed quarterly or annual payments, payments based on active hours worked or profit sharing.

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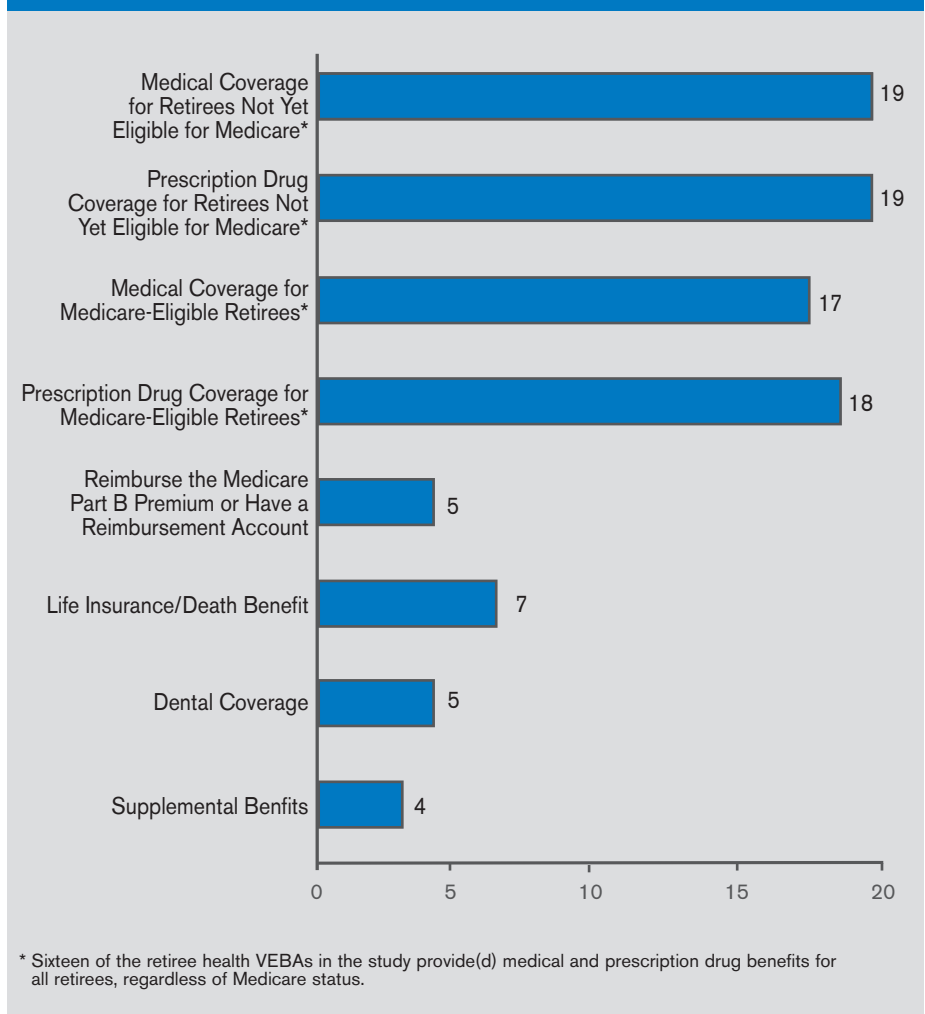
BENEFITS: OFFERINGS & IMPROVEMENTS

Almost all of the 25 retiree health VEBAs in the study (21) provide or, in the case of terminated retiree health VEBAs, provided health benefits for retirees not yet eligible for Medicare or Medicare-eligible retirees. The remaining four retiree health VEBAs provide supplemental benefits such as reducing retiree contributions, paying part of the deductibles and lowering drug copayments. Graph 6 shows the percentage of all retiree health VEBAs in the study offering various benefits.

Graph 5: Number of Ongoing Retiree Health VEBAs* by Assets



Graph 6: Number of Retiree Health VEBAs Offering Various Benefits



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Of the 22 ongoing retiree health VEBAs, 10 offer participants a choice among plans. Eight of the ongoing retiree health VEBAs have improved benefits in the last three years. The improvements included lower retiree contributions and lower drug copayments.

COMMENTARY & CONCLUSION

In a tough economy, it is not surprising that interest in retiree health VEBAs is growing. Large companies, particularly those with unionized workforces, are finding the ability to transfer retiree health liabilities to a stand-alone VEBA attractive from both a financial and accounting perspective. The beneficiaries of those plans appreciate the security

of having a funded benefit and greater say in benefit determination.

Despite these advantages, it is important to recognize that stand-alone retiree health VEBAs are not the solution in all situations. The tax advantages of a VEBA are only available for certain types of employers, funding of the VEBA has to be sufficient to provide benefits, and detailed financial information about company performance must be available.



To discuss the advantages and disadvantages of stand-alone retiree health VEBAs in particular circumstances, how to set up a retiree health VEBA and considerations for

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ongoing operations, contact your Segal Company consultant or one of the following experts:

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