

# **Contractual Savings Conference**

**November 3, 2003**



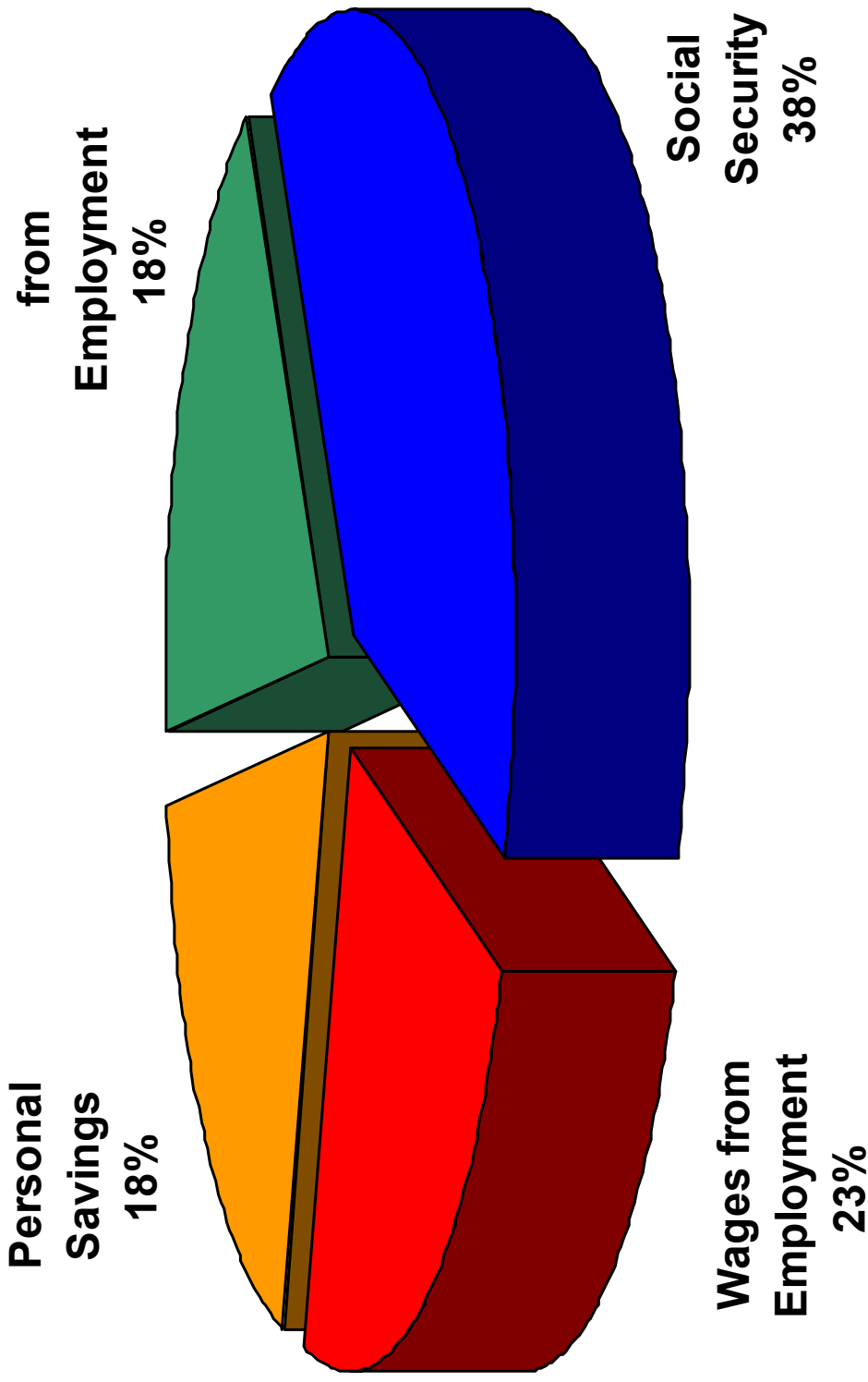
**Steven A. Kandarian**

**Executive Director**

**Pension Benefit Guaranty Corporation**

# Retirement Systems in the United States

## Sources of Retirement Income (2000)



# **History of Defined Benefit Pensions in U.S.**

- 1875:** First corporate pension plan (American Express)
- 1935:** Social Security Act
  - Rise of Unions – Wagner Act
- 1949:** Automobile and steel manufacturing pension plans
- 1963:** Studebaker bankruptcy
- 1967:** Senator Javits introduces Employee Retirement Income Security Act (ERISA)
- 1974:** ERISA signed into law
- 1987:** ERISA amended
- 1994:** ERISA amended
- 2003:** Current debate in Washington, DC

# **Pension Benefit Guaranty Corporation**

- **Insures the promised benefits of underfunded defined benefit plans of bankrupt employers**
- **44 million insured workers in 33,000 defined benefit plans**
- **Currently paying \$2.5 billion in annual benefits to 450,000 retirees in 3,200 terminated plans**

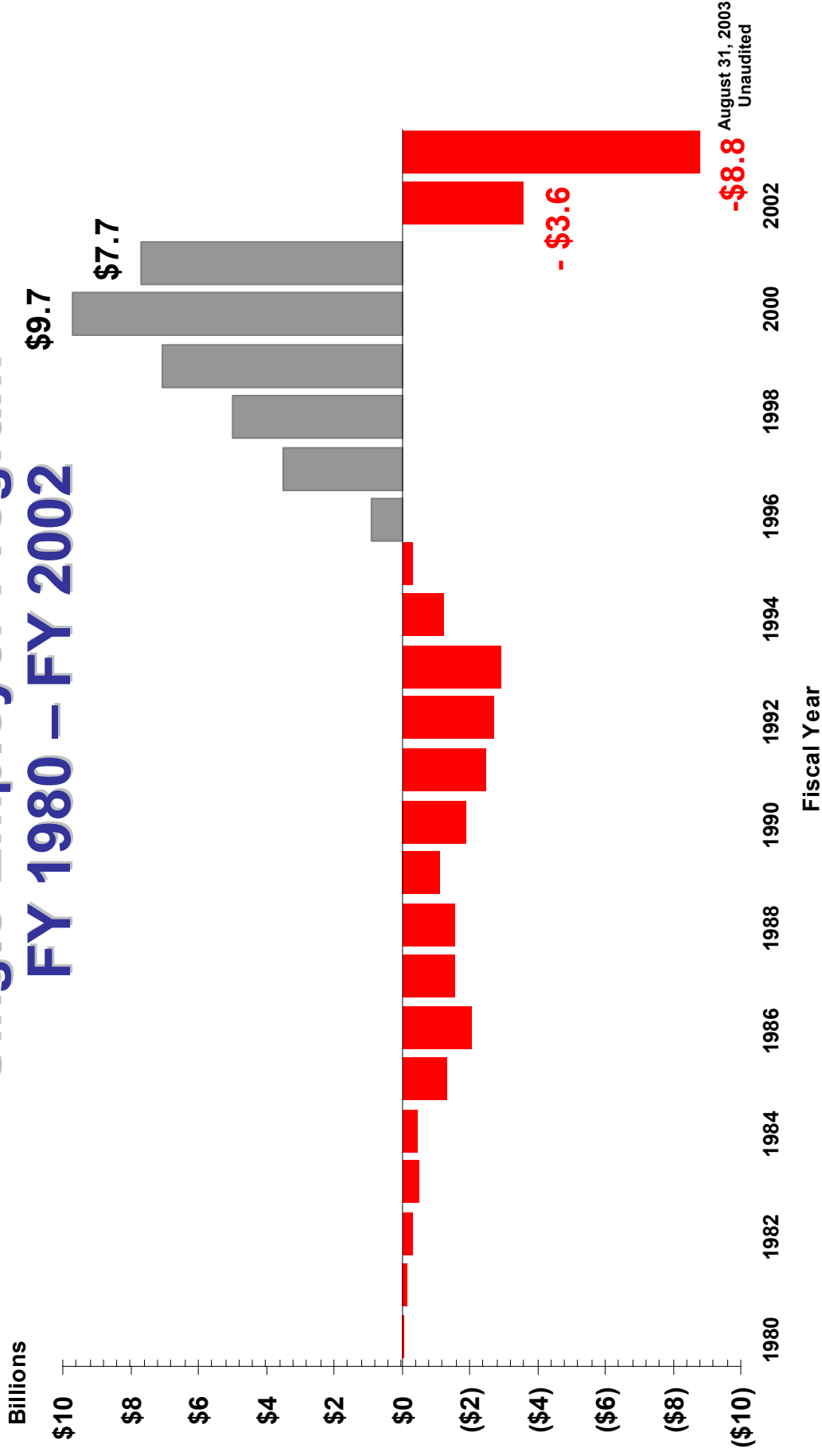
# The PBGC “Put”

- PBGC effectively has written a “put option” to the plan sponsors
- The value of the “put” depends on:
  - Credit worthiness of plan sponsor and
  - Volatility of plan assets (funded status)
- PBGC charges a \$19/participant plus 0.9% of plan underfunding for the “put” (premiums)

# **PBGC Funding Sources**

- **Premiums**
- **Investment returns**
- **Assets from trusteeed plans**
- **Recoveries from bankruptcy**

# PBGC Net Position Single-Employer Program FY 1980 – FY 2002



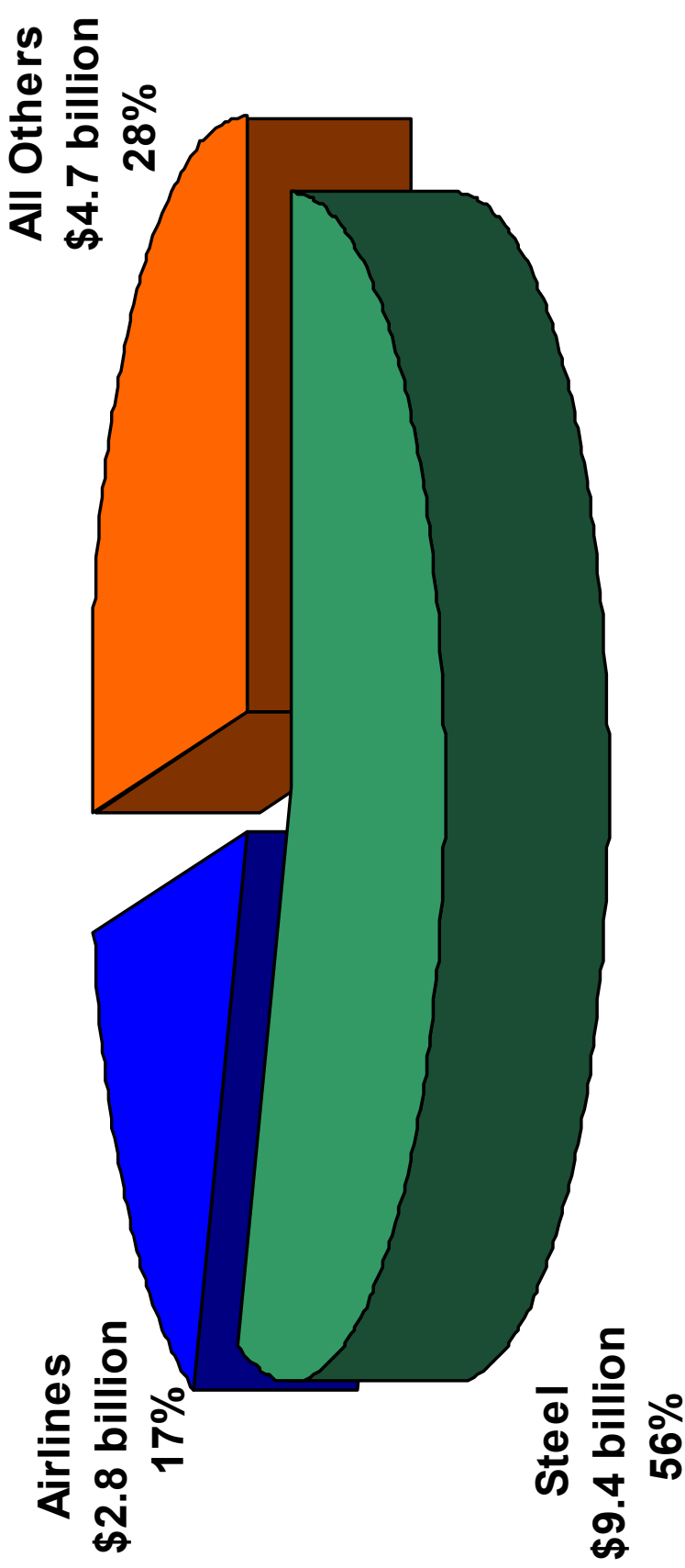
August 31, 2003  
Unaudited

Data does not include restored LTV plans in 1986

# Historic PBGC Claims

## PBGC Claims FY 1975 - 2002

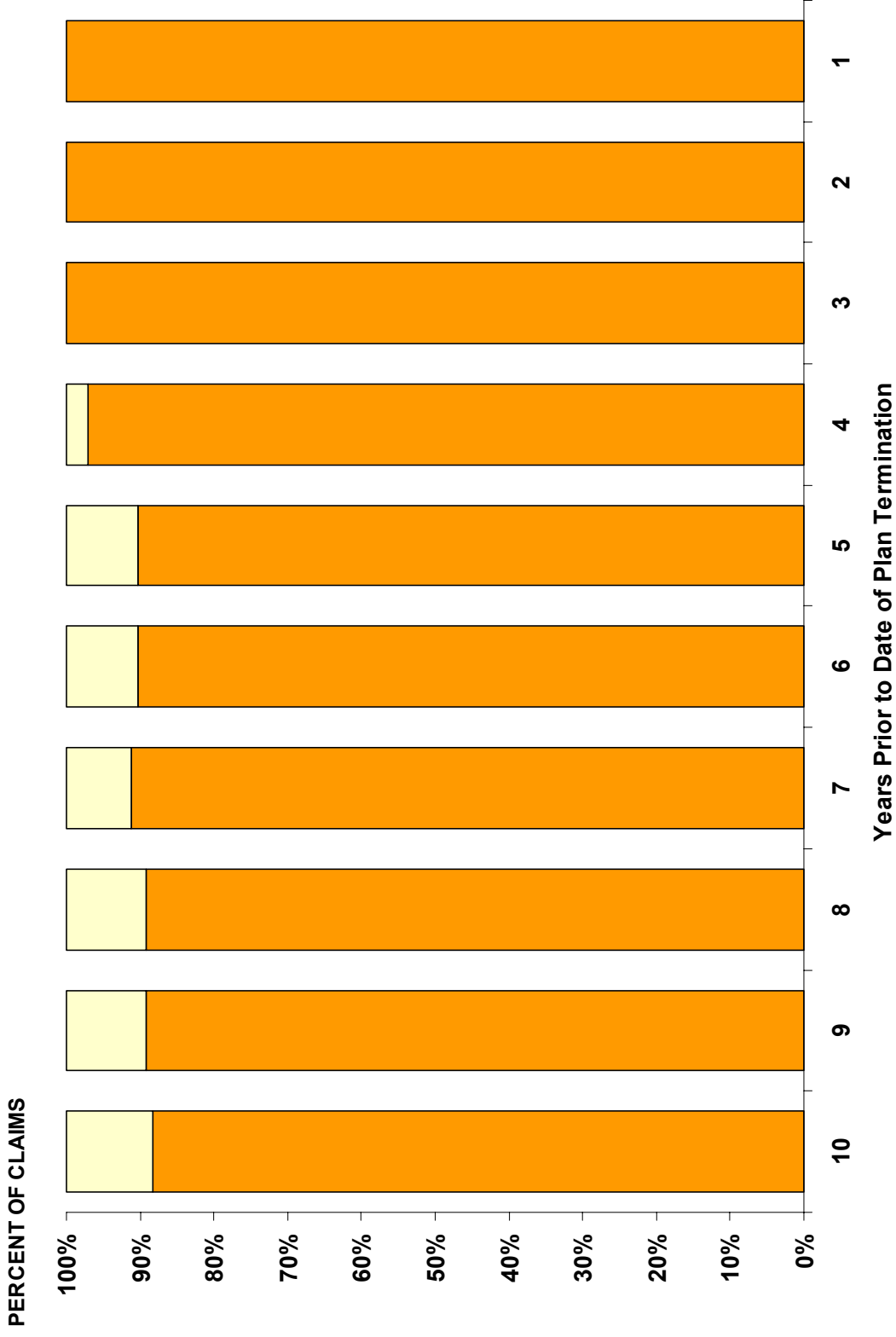
(including Bethlehem, National Steel and US Airways Pilots)



**Note:** Historically, Steel has represented less than 3% of participants covered by PBGC and Airlines less than 2%.

# Debt Ratings for Large Claims

■ Below Investment Grade    ■ Investment Grade



**NOTE: Based on 27 of PBGC's largest claims representing over 50% of all claims.**

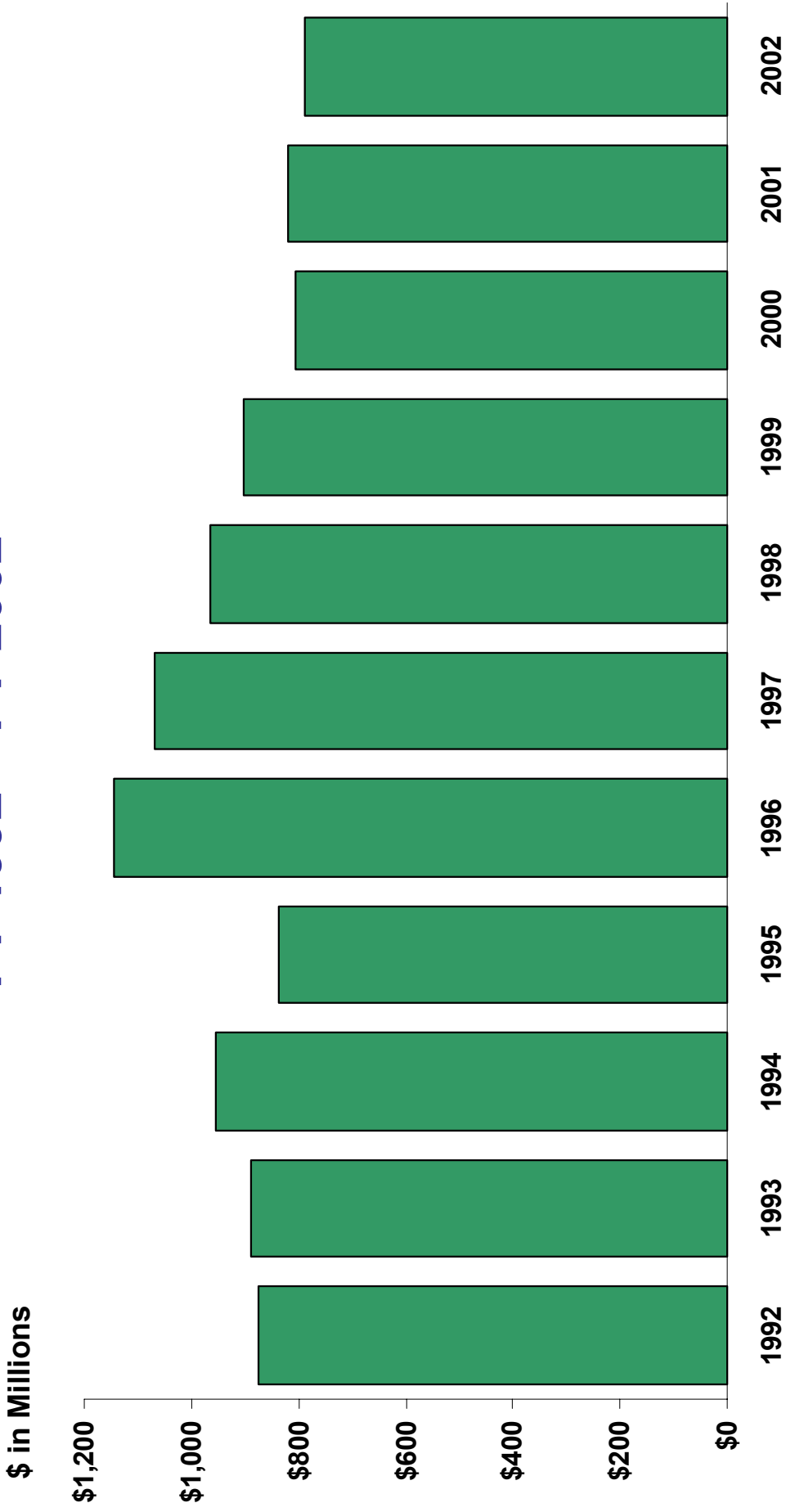
# Top 10 Firms Presenting Claims FY 1975 – Present

Top 10 Firms	Fiscal Year of Plan Termination	Claims (Billions \$)	Covered Participants	Funded Ratio*
Bethlehem Steel	2003	\$ 3.9	95,000	48%
LTV Steel	2002	1.9	79,600	50%
National Steel	2003	1.3	35,400	54%
Pan American Air	1991, 1992	0.8	37,500	31%
Trans World Airlines	2001	0.7	34,300	47%
US Airways Pilots	2003	0.6	6,000	71%
Eastern Air Lines	1991	0.6	51,200	65%
Wheeling Pitt Steel	1986	0.5	22,100	27%
Polaroid	2002	0.4	11,400	67%
Sharon Steel	1994	0.3	6,900	21%

\* Funded ratio at termination for PBGC benefits; participants lose additional benefits not covered by PBGC

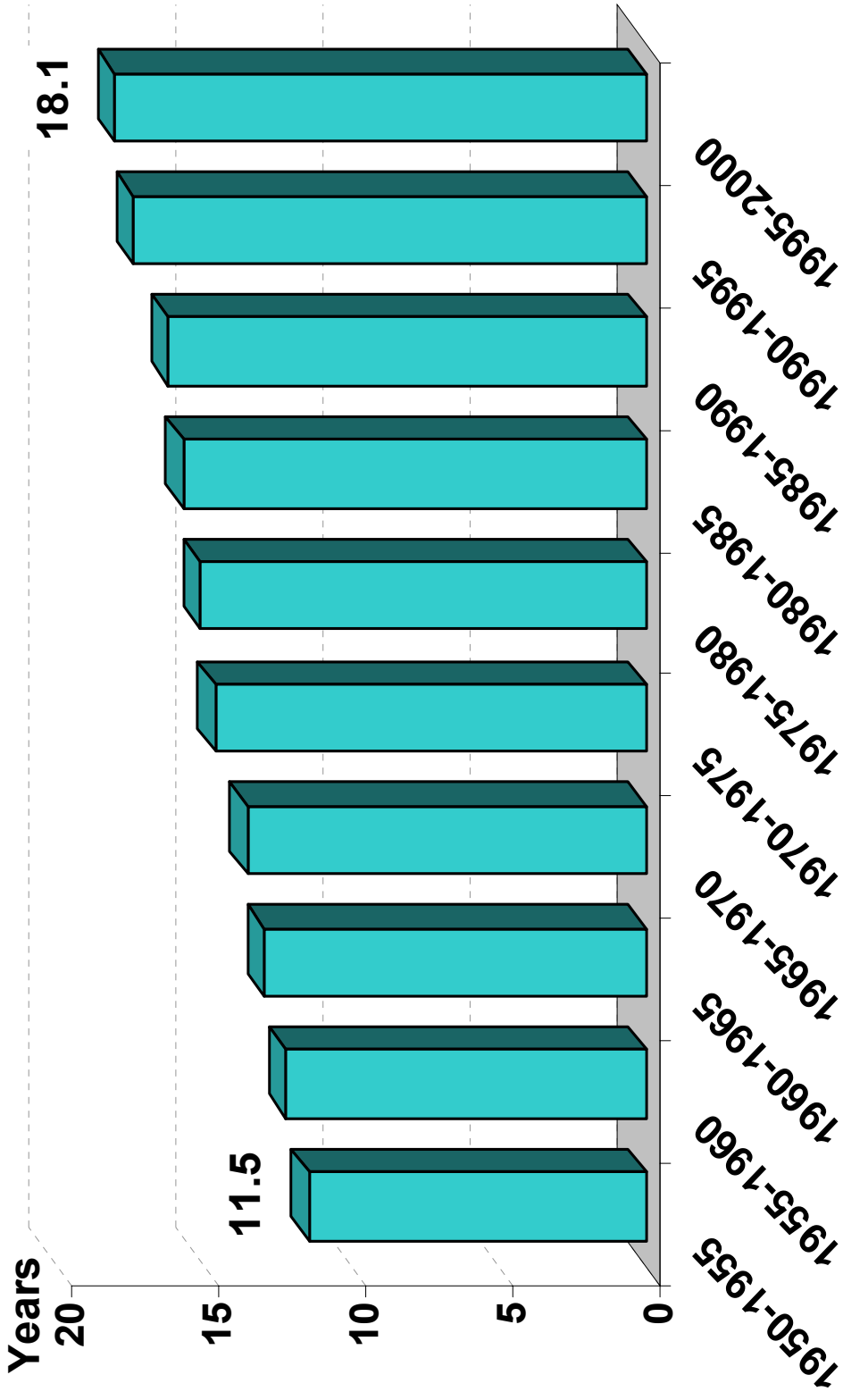
# Single-Employer Premium Income

FY 1992 – FY 2002



NOTE: The variable rate premium was capped until 1996

# Average Number of Years Spent in Retirement (Males)



# Wage Benefit Trade-Off

**Current  
Wages**

**Future Pension  
Benefits**

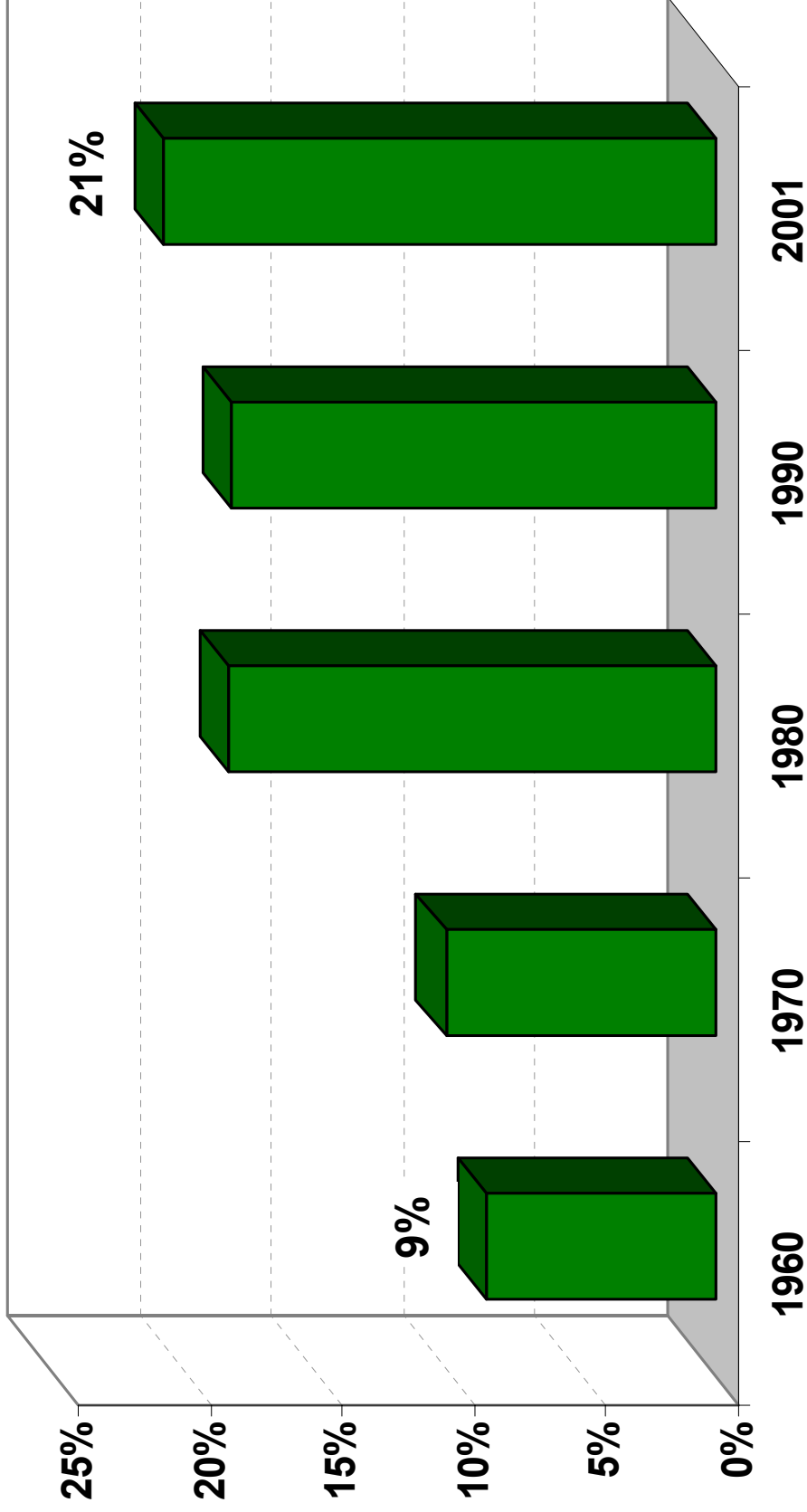
**Immediate  
Cost**

**Deferred  
Cost**

**No Cost  
Shifting**

**Potential Cost  
Shifting to PBGC**

# Trade as a Percentage of GDP\*



\* Calculated as  $[\text{Exports} + \text{Imports}] / [\text{GDP} + \text{Imports}]$

Source: Bureau of Economic Analysis Income and Product Accounts

**FAS 87**

**High expected  
return assumptions**

**Higher  
Reported  
EPS**

**Higher  
Stock  
Price**

**Executive  
Options More  
Valuable**

**More Risk  
In  
Assets**

**More  
Volatility**

**Pressure  
On  
Balance Sheet**

# Asset Allocation

## Typical Defined Benefit Plan

- 63% Equities
- 30% Fixed Income
- 7% Other

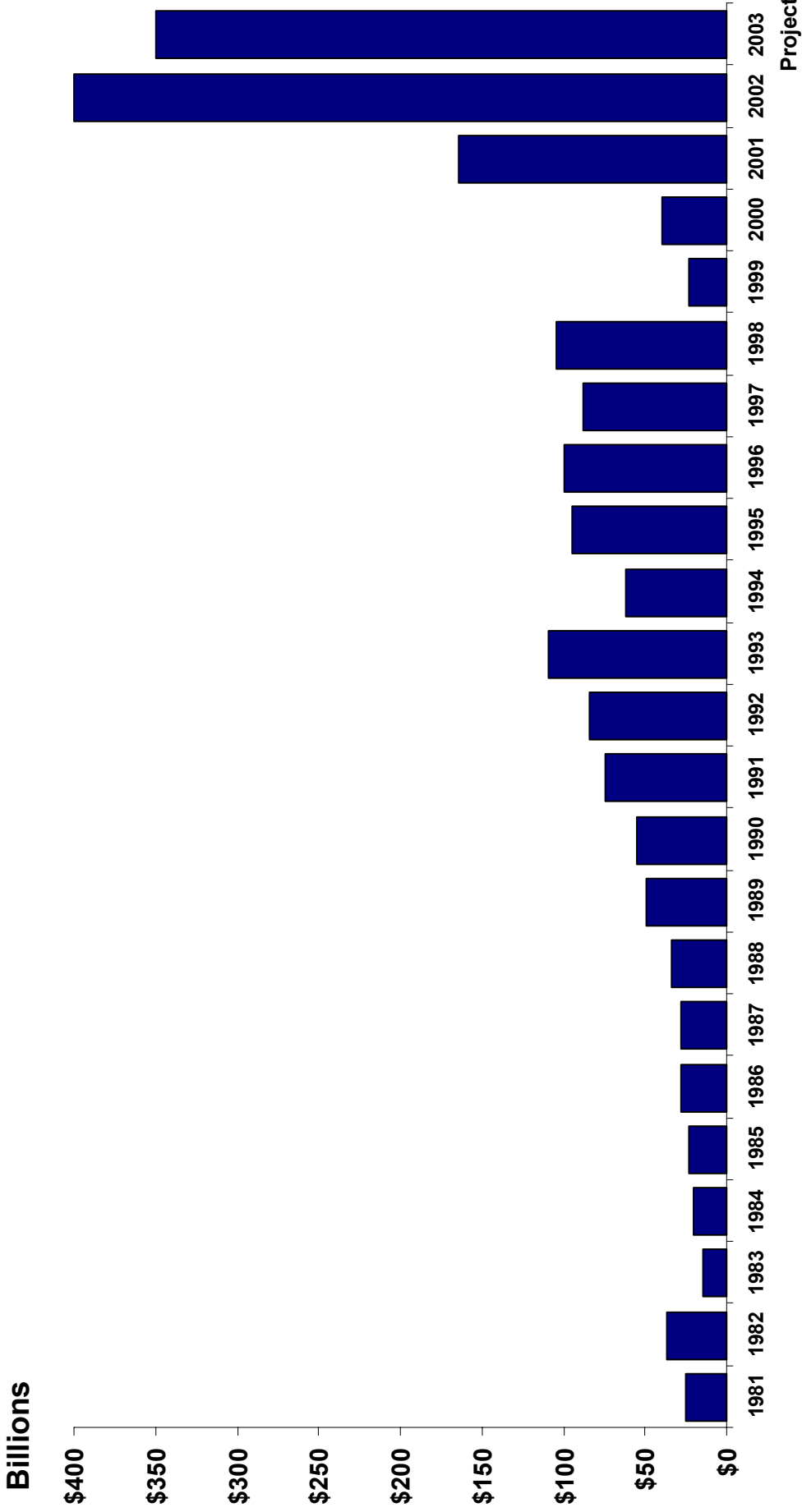
[Pensions & Investments Survey of Large Plan Sponsors]

## Private Insurance Company

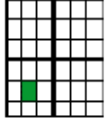
- 4% Equities
- 87% Fixed Income
- 9% Other

[American Council of Life Insurance]

# Total Underfunding Insured Single-Employer Plans



PBGC estimates from Form 5500 and Section 4010 Filings



## Asset / Liability Watch (Percentage Change)

	'00	'01	'02	'03
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**ASSETS**      -2.5      -5.4      -11.4      11.0

**LIABILITIES**      26.0      3.1      19.5      -3.3

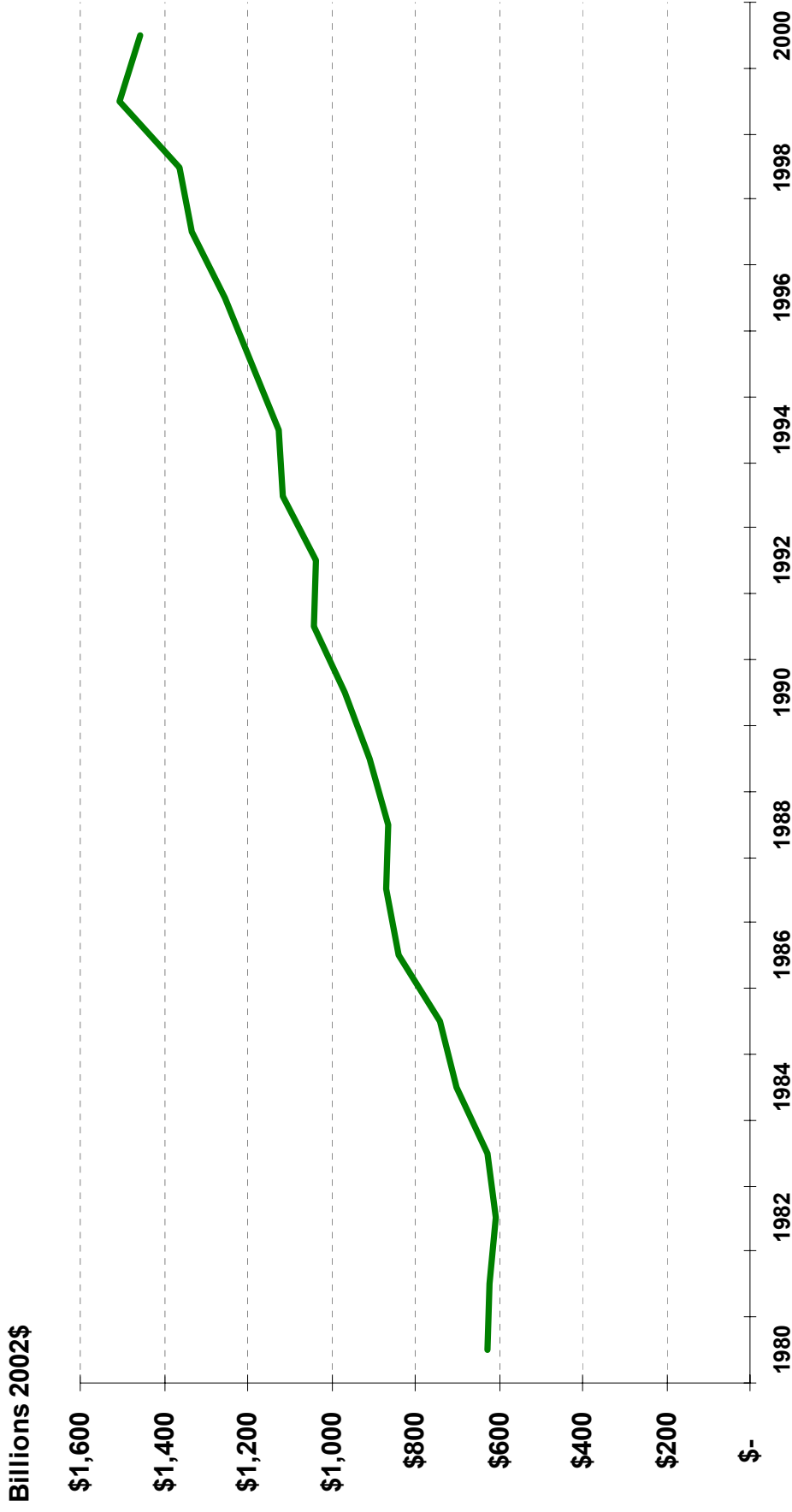
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**Assets - Liabilities**      -28.5      -8.5      -30.9      7.7

} **-60.15%**

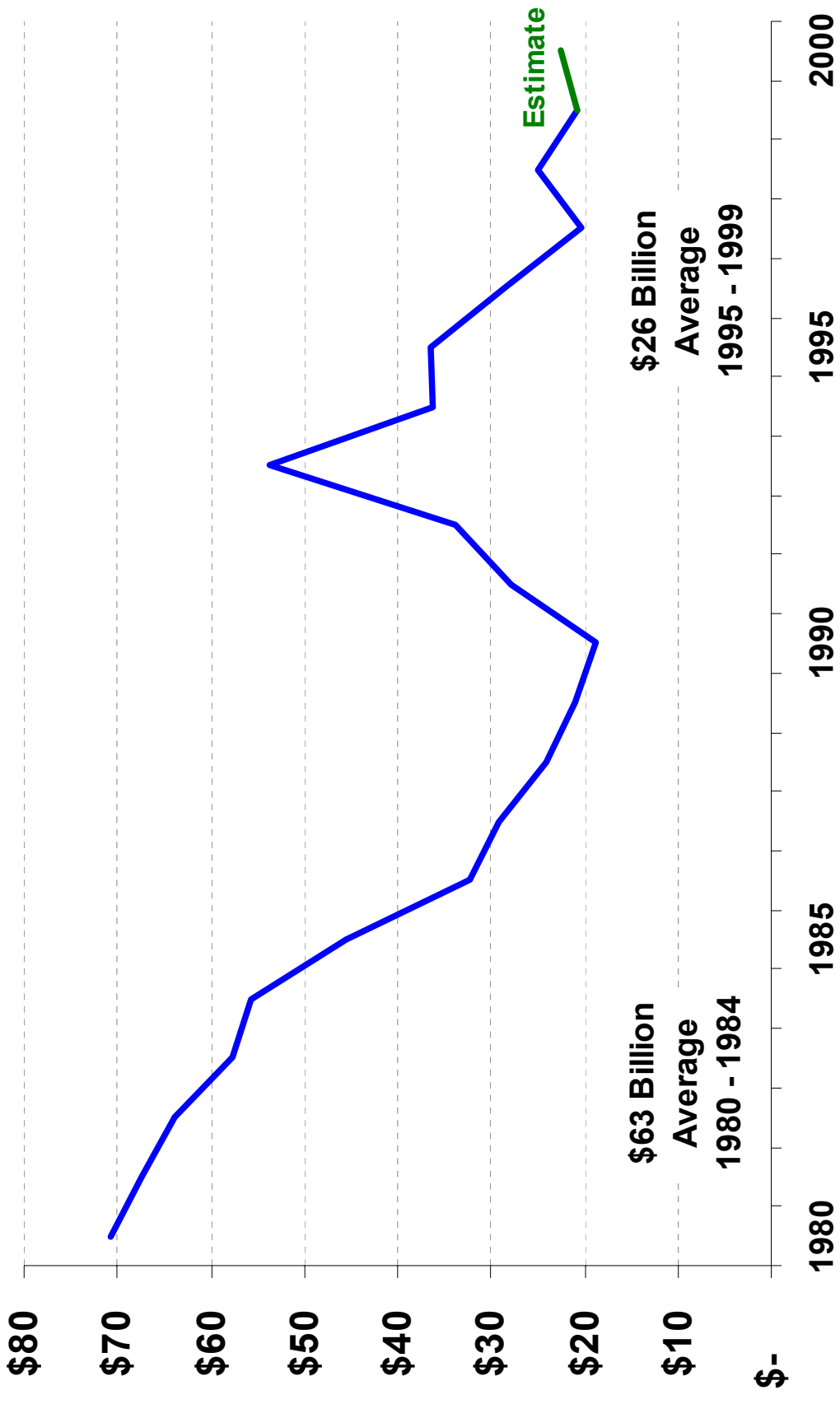
Index:	Cash	5%
	LB Aggregate	30%
	S&P 500	60%
	MSCI EAFE	5%

# Historic Single-Employer Liabilities 1980 - 2000



# Historic Single-Employer Contributions 1980 - 2000

2002 \$  
Billions



# Choices ...

- **Do Nothing (cyclical)**
- **Significantly Higher Premiums**
- **General Revenue Transfer**
- **Better Funded Plans**

# **Administration's Proposal**

- 1. Improve Accuracy of the Pension Liability Discount Rate**
- 2. Increase Transparency of Pension Plan Information**
- 3. Strengthen Safeguards Against Pension Underfunding**
- 4. Comprehensive Funding Reforms**