Administration Single-Employer Pension Reform Proposal

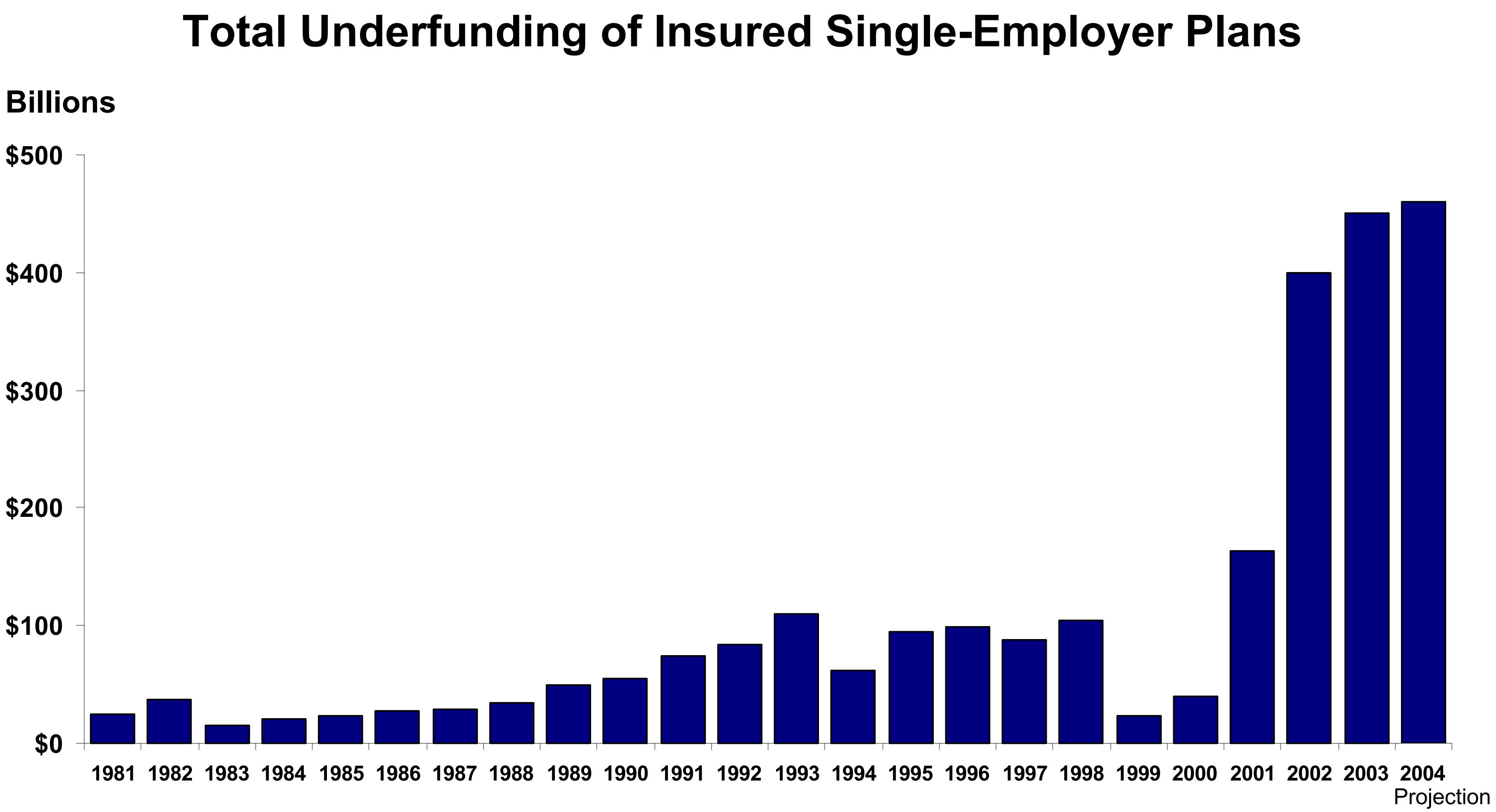
Challenges Facing the Defined-Benefit Pension System

- The pension insurance system is broken and threatening workers, healthy plan sponsors, and taxpayers
- There are three keys to fixing the system:
  - **Reform funding rules** – to induce employers to fully fund their plans
  - **Reform insurance premiums** -- to better reflect costs and risks
  - **Improve disclosure** -- to better inform workers, investors and regulators

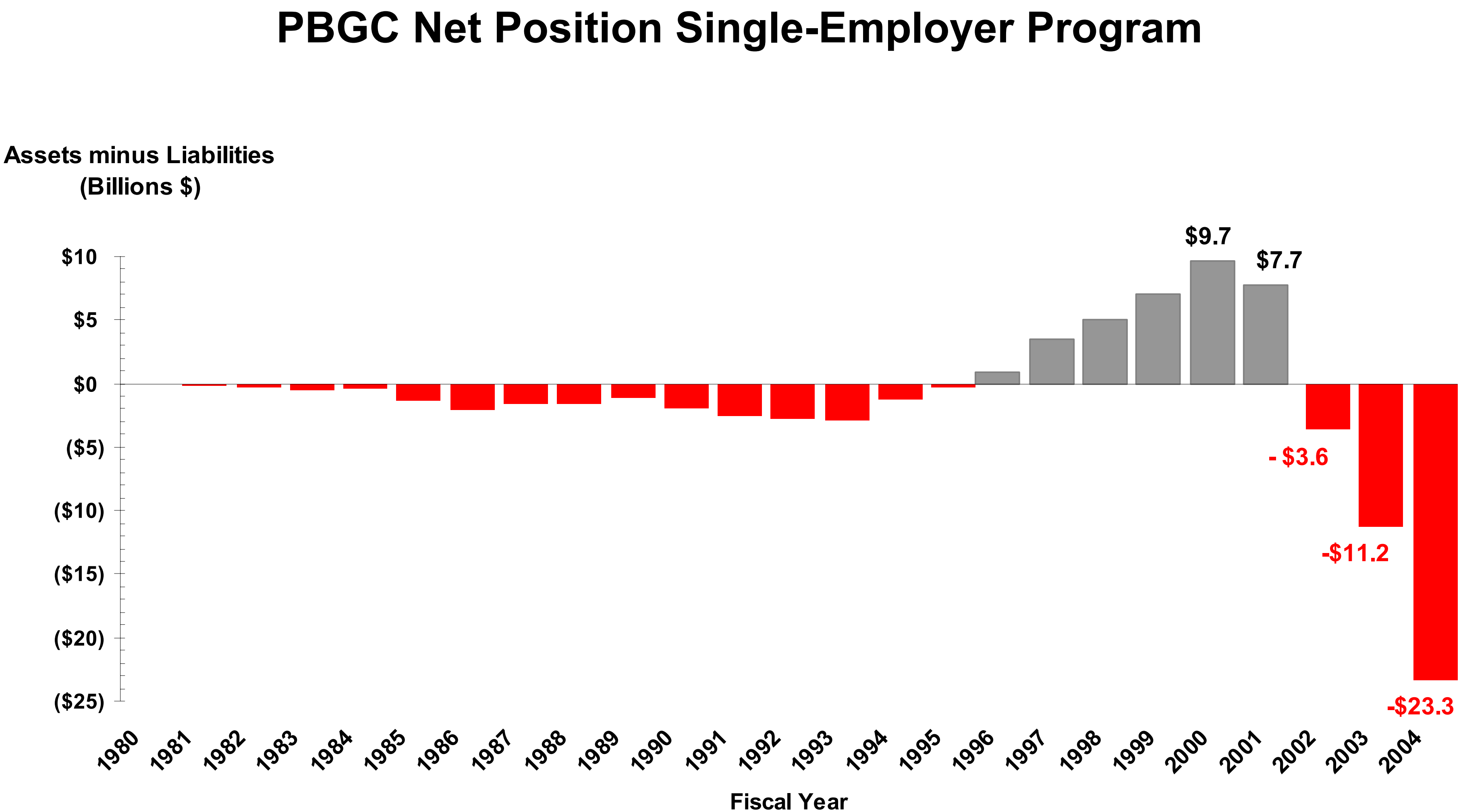
Our Goals

- Protect workers
- Avoid a taxpayer bailout of PBGC

Problem: Underfunding has skyrocketed…



…and PBGC has fallen into a deep hole



Summary: The Administration Single-Employer Pension Reform Proposal

One single, accurate measure of liabilities valued according to current duration-matched yield curve of corporate bond rates
Assumptions that appropriately reflect the plan’s risk of termination
Plans given a reasonable period of time to reach their funding targets
Sponsors allowed to make additional deductible contributions during good economic times
Underfunded plans or financially weak sponsors restricted from increasing unfunded benefits
Premiums that meet PBGC’s long-term funding needs
Better disclosure of plan information to workers, markets, and regulators
Clarify the treatment of hybrid (cash-balance) plans to expand pension options
Improve PBGC’s standing to enforce contributions on firms in bankruptcy

The Administration proposal would simplify the system by replacing multiple measures of pension liabilities with one basic concept

Current Practice

Actuarial Liability

Current Liability

RPA Current Liability	OBRA Current Liability	Gateway Liability

Administration Proposal

Single Conceptual Measure of Liabilities Based on Benefits Earned to Date

Assumptions modified as needed to reflect the risk of termination posed by the plan

Under the Administration proposal, a plan's funding target would be based on the plan's Ongoing or At-Risk liability, depending on the sponsor's financial health

Company Status		Funding Target
Investment Grade (Baa or better)	→	Target assumes it is an Ongoing plan
Junk bond credit status less than 5 years	→	Target in between Ongoing and At-Risk status
Junk bond credit status 5 years or more	→	Target assumes it is an At-Risk plan

In an Ongoing plan, employees are assumed to retire and to choose lump sums as they have in the past. In an At-Risk plan, the rules will assume that employees will take lump sums and retire as soon as they can

Empirical evidence shows that a firm's time spent in junk bond status is a strong indicator of the likelihood of plan termination

The Administration proposal gives plans a reasonable period of time to address underfunding

- Under the Administration proposal, plans would annually contribute enough to address their funding shortfall over a reasonable period of time

The Administration proposal would allow plan sponsors to make additional deductible contributions during good economic times

Minimum Required Contribution	Maximum Deductible Contribution
- Pursuant to funding target (not including future salary increases)	- May pre-fund projected salary increases - May fund to include a "volatility cushion" equal to 30% of their funding target

The Administration proposal requires employers to pay for additional benefits immediately if the sponsor is financially weak or has a significantly underfunded pension plan

Percentage Points Below Required Funding Level (Target)	Bankrupt Sponsor	Junk Grade Sponsor (At-Risk Liability Target)	Investment Grade Sponsor (Ongoing Liability Target)
0 to 19	▪ No benefit increases ▪ No lump sums ▪ No accruals	▪ No new restrictions	▪ No new restrictions
20 to 39	▪ No benefit increases ▪ No lump sums ▪ No accruals	▪ No benefit increases ▪ No lump sums	▪ No benefit increases
40 or worse	▪ No benefit increases ▪ No lump sums ▪ No accruals	▪ No benefit increases ▪ No lump sums ▪ No accruals ▪ No preferential funding of executive compensation	▪ No benefit increases ▪ No lump sums

The Administration proposal would reform the PBGC premium structure

- **Flat rate premiums** will be adjusted (initially to $30) to reflect the growth in worker wages since 1991, when the current $19 figure was set. Going forward, the flat rate premium will be indexed for wage growth
- **Risk based premiums** will be charged to each plan based on underfunding relative to its funding target. The risk-based premium rate will be adjusted periodically by the PBGC's Board so that premium revenue is sufficient to cover expected losses and improve PBGC's financial condition

The Administration proposal would improve the content and timeliness of disclosure

Better Content

- Require plans to disclose funding status relative to funding target annually
- Require funding trend data in participant disclosure

Greater Transparency

- Make certain financial information filed with PBGC by underfunded plans publicly available

More Timely Information

- Accelerate filing deadline for certain plan funding reports
- Accelerate disclosure of information to workers

Administration proposal would protect plans in bankruptcy

- Allow PBGC to perfect its lien against missed contributions while plan sponsor is in bankruptcy

- Notify participants when plan sponsor files for bankruptcy, including effect on plans

What is the Administration doing to help employers and workers expand retirement choices?

- Hybrid plans (e.g., “cash balance” plans) combine the best of defined benefit and defined contribution
  - Plans are portable
  - Employees understand and appreciate benefits
  - Investment risk borne by employer
  - Insured by the PBGC

- Enact the Treasury proposal to a create legal and regulatory environment that supports continuation and adoption of hybrid plans

- Establish Employer Retirement Savings Accounts (ERSAs) that will simplify the rules surrounding employer-provided portable savings plans

- Increase worker access to investment education

- Allow workers in defined contribution plans to diversify out of company stock after three years

Summary:

- **The Administration single-employer pension reform proposal would make defined-benefit plans a more viable option for employers and workers by achieving:**
  - Sounder long-term pension funding
  - Reduced risk to workers and to the pension insurance system
  - Increased transparency and simplified measurements
  - Improved incentives for sound pension funding and greater flexibility for employers to fund up in good times
  - Opportunities for sponsors to reduce volatility in required pension contributions
  - Premiums that meet PBGC's long term funding needs
  - Reduced risk to the taxpayers of having to bail out the PBGC