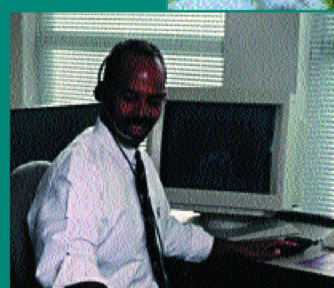
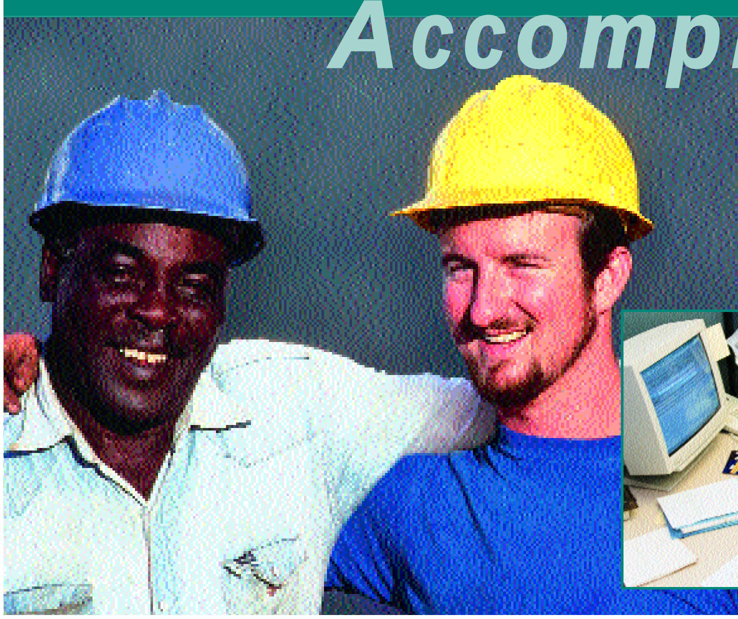
PENSION BENEFIT GUARANTY CORPORATION

PBGC
U.S. GOVERNMENT AGENCY

# A Year of Important Accomplishments



1996 ANNUAL REPORT



# Contents



The Pension Benefit Guaranty Corporation protects the pensions of more than 42 million working men and women in about 50,000 private defined benefit pension plans, including about 2,000 multiemployer plans. These pension plans provide a specified monthly benefit at retirement, usually based on salary or a stated dollar amount and years of service. The Employee Retirement Income Security Act of 1974 established PBGC as a federal corporation.

PBGC receives no funds from general tax revenues. Operations are financed by insurance premiums set by the Congress and paid by sponsors of defined benefit plans, investment income, assets from pension plans trusteed by PBGC, and recoveries from the companies formerly responsible for the trusteed plans.

PBGC's mission is to operate as a service-oriented, professionally managed agency that protects participants' benefits and supports a healthy retirement plan system by:

- encouraging the continuation and maintenance of private pension plans,
- protecting pension benefits in ongoing plans,
- providing timely payments of benefits in the case of terminated pension plans, and
- making the maximum use of resources and maintaining premiums and operating costs at the lowest levels consistent with statutory responsibilities.

# Highlights

- For the first time in PBGC history, the single-employer insurance program posted a yearend surplus. With no major plan terminations during the year and significant income from premiums and equity investments, assets exceeded liabilities by $869 million. The multiemployer insurance program also remained financially strong.
- PBGC paid $792 million in benefits to nearly 200,000 people during the year. Another 240,000 people will receive benefits when they retire in the future.
- While pension underfunding increased in 1995 in large part because of a decline in interest rates, reforms for premiums paid by underfunded plans increased premium revenues by more than 35 percent to nearly $1.2 billion to keep the insurance program strong. Other reforms from the Retirement Protection Act of 1994 are in place to address the underfunding over time.
- PBGC recorded strong gains on its equity investments with total investment income exceeding $900 million, which contributed to the agency's improved financial condition.
- PBGC has or will become trustee of 2,348 underfunded pension plans, including 255 terminated during the year.
- The Early Warning Program achieved more than $1 billion in additional protection for the benefits of nearly 200,000 people through agreements with 11 companies.

*(Dollars in millions)*

| | 1996 | 1995 |
|---|---|---|
| SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS COMBINED | | |
| **Summary of Operations** | | |
| Premium Income | $ 1,168 | $ 860 |
| Loss from Plan Terminations | $ 118 | $ 169 |
| Investment Income | $ 927 | $ 2,039 |
| Actuarial Charges | $ 633 | $ 1,563 |
| **Insurance Activity** | | |
| Benefits Paid | $ 792 | $ 763 |
| Retirees | 199,700 | 182,300 |
| Total Participants in Terminated and Multiemployer Plans | 441,000 | 392,000 |
| New Underfunded Terminations | 255 | 124 |
| Terminated/Trusteed Plans (Cumulative) | 2,348 | 2,094 |
| **Financial Position** | | |
| SINGLE-EMPLOYER PROGRAM | | |
| Total Assets | $ 12,043 | $ 10,371 |
| Total Liabilities | $ 11,174 | $ 10,686 |
| Net Income | $ 1,184 | $ 925 |
| Net Position | $ 869 | $ (315) |
| MULTIEMPLOYER PROGRAM | | |
| Total Assets | $ 505 | $ 477 |
| Total Liabilities | $ 381 | $ 285 |
| Net Loss | $ (68) | $ (5) |
| Net Position | $ 124 | $ 192 |

## Chairman's Message

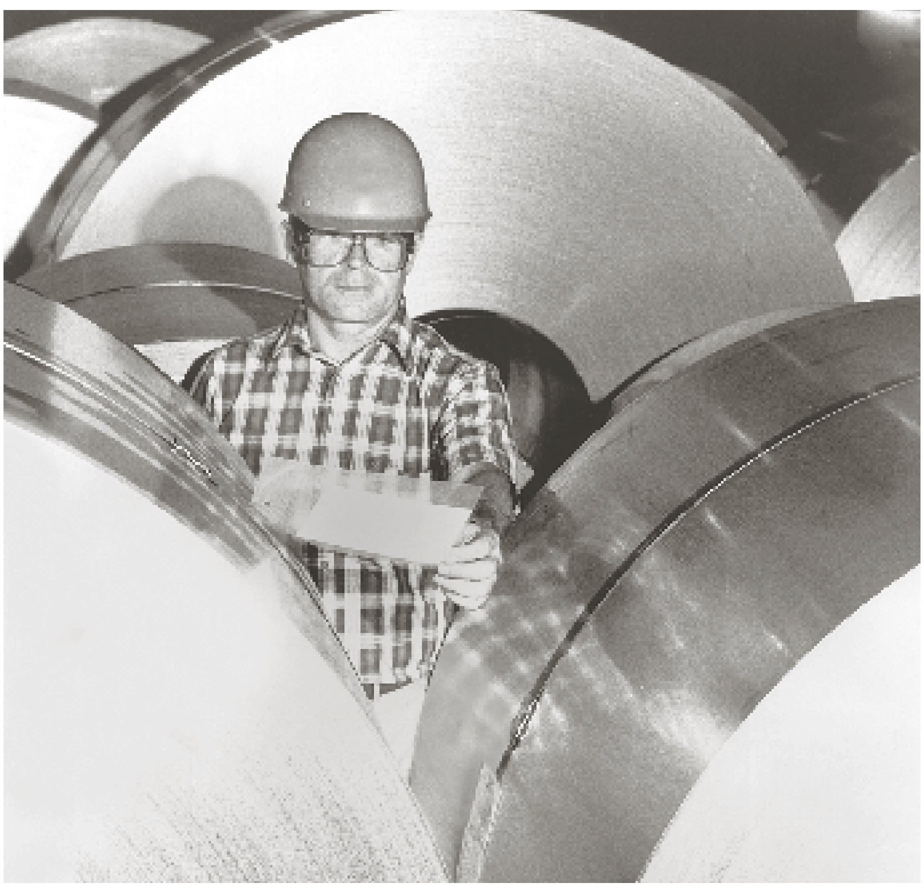
"...a year of important accomplishments for PBGC."

The financial strength of the Pension Benefit Guaranty Corporation, which we report this year, should reassure employers, workers, and retirees whose benefits we protect. The agency's financial results capped a year of important accomplishments for PBGC. Through careful management and effective enforcement, we are building a sound pension insurance system to keep retirement secure for present and future generations of American workers.

Reforms now in place have brought PBGC to a healthy financial position and will improve pension funding over time. Still, the need for vigilance remains. Economic changes and any weakening of pension funding can undermine the pension promise.

Retirement security is a central issue for working people today. The financial progress of the insurance system and our commitment to improve funding of pensions will help make their retirement dreams come true.

Cynthia A. Metzler
*Acting Secretary of Labor*
*Chairman of the Board*



# Executive Director's Report

In 1996, the Pension Benefit Guaranty Corporation reached a milestone sought since its creation in 1974 — a financial surplus. The news that PBGC has eliminated its longstanding deficit stands out in a year of important accomplishments in many areas. We achieved financial strength, proactive enforcement, responsive customer service, and technological advance.

## Strengthening Financial Programs and Systems

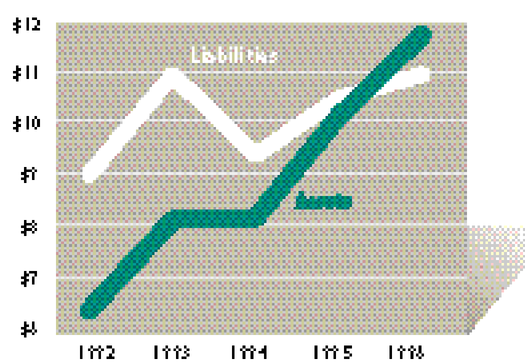
With a yearend surplus of $869 million for the insurance program for single-employer plans, and a continuing surplus for the multiemployer plan insurance program, we are reporting a positive bottom line for the first time in PBGC history. Strong premium revenues, sustained returns on our equity investments, and low losses from plan terminations were key contributors to the single-employer program's net income of nearly $1.2 billion. Through sound financial management and adherence to strict business standards and procedures, we have a solid foundation for the future.

"...companies are finding that addressing pension issues early makes good business sense."

PBGC's improved financial condition reflects the initial impact of the Retirement Protection Act, which was intended both to improve gradually the funding of underfunded single-employer pension plans and to strengthen PBGC. While pension underfunding persists and, because of the unusually low interest rates, increased during 1995 to $64 billion, the reforms are in place and working to address it.

The funding reforms were designed to reach their full effect over a period of years, with transition rules to ease the initial impact of the reforms on employers. The phase-out of the cap on premiums paid by underfunded plans, particularly at a time when underfunding increased, had an immediate effect, generating increased premium revenues to help keep PBGC sound. New requirements to inform workers about pension underfunding and other compliance reforms also have strengthened PBGC's hand in dealing with the continuing pension underfunding.

Single-Employer Program Assets and Liabilities
(Dollars in billions)




Intensive efforts over the past few years have equipped PBGC with highly effective and reliable financial programs and systems. As a result, we have again received an unqualified audit opinion on our financial statements. Major overhaul of PBGC's financial management has been accomplished and we continue to bring new systems online to ensure that our resources and procedures keep pace with the growing demands on the agency.

## Maintaining a Proactive Enforcement Program

More and more, companies are finding that addressing pension issues early makes good business sense. Companies now are approaching PBGC in advance of transactions to structure protections for their pension plans. PBGC is also finding that companies are providing additional funding for their pension plans rather than be subject to the new notice and reporting requirements established by the Retirement Protection Act for significantly underfunded plans.

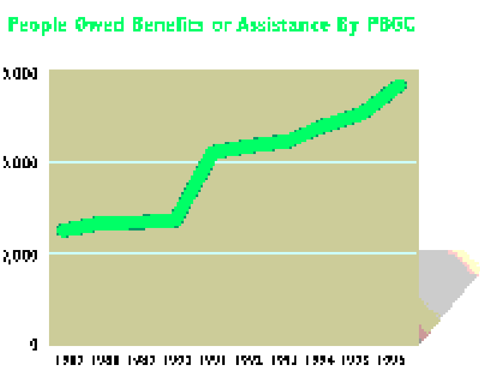
“...working harder, faster, and better to provide the answers and pay the benefits...”

Under the Early Warning Program, PBGC uses sophisticated information technology and financial analyses to identify and monitor the companies whose underfunded pension plans pose risks to workers and retirees and to the pension insurance program. This information enables PBGC to take early action to prevent losses that could occur if corporate transactions jeopardize pensions. During the past year, this program generated more than $1 billion in additional contributions and other protections for underfunded pensions of nearly 200,000 people. In addition, PBGC took preventive action that shored up the Amalgamated Insurance Fund, a multiemployer pension plan covering 70,000 workers and retirees in the men’s suit industry. This was the first agreement of its kind, protecting the pensions of an entire industry.

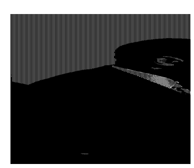
The agency took further steps throughout the year to implement the reforms. PBGC used a negotiated rulemaking process with the business community and other affected groups for the first time to develop proposed changes in the way companies must report events that may threaten workers’ pensions, including several reportable events added by the new law. When the final reportable event rules were issued in December 1996, Vice President Al Gore’s National Performance Review awarded another Hammer Award to PBGC, its fourth overall, for the agency’s use of negotiated rulemaking.

## Providing Responsive Service and Improved Benefit Processing

PBGC staff, using the latest in automated and telecommunication technology, are working harder, faster, and better to provide the answers and pay the benefits on which our customers depend. We assumed the pension obligations of about 50,000 additional people and still achieved greater productivity and customer service through reengineering of insurance operations. We maintained last year’s record pace in issuing individual benefit determinations. The Customer Service Center, which began operations as the year began, answered nearly 93,000 telephone inquiries during the year.




PBGC instituted a number of service improvements. Easy access to PBGC press releases, publications, and regulations is now possible through the Internet following our establishment of a World Wide Web Home Page. We began an annual newsletter for people who are owed a benefit by PBGC but have not yet started to collect it, much like our semiannual newsletter for retirees, to keep them informed about actions of the insurance program that affect them. We also issued a new booklet called “Divorce Orders & PBGC,” to help attorneys and others who prepare domestic relations orders in a divorce or legal separation to divide pension benefits payable by PBGC.



The Pension Search Program took on new responsibilities as PBGC continued to find thousands of previously unlocatable people owed benefits from terminated underfunded plans. The agency started a missing participant clearinghouse for companies terminating fully funded plans, which had been authorized by the Retirement Protection Act, and located addresses for several hundred of the nearly 1,000 missing persons identified by more than 120 companies. Then, shortly after the year ended, the U.S. Department of Labor and PBGC unveiled the Pension Search Directory to link the hardest-to-find people with their benefits. The directory, which listed 2,700 people owed about $10 million in benefits, is available on the Internet and from organizations and unions that are partners in the search.

*Executive Director Martin Slate, seated center, with Deputy Executive Directors (left to right) Ellen A. Hennessy, Chief Negotiator; Joseph Grant, Chief Operating Officer; N. Anthony Calhoun, Chief Financial Officer; and John Seal, Chief Management Officer*

*PBGC dedicates this Annual Report to Martin Slate, who died on February 24, 1997, as this Report was going to print. The Report reflects Mr. Slate's priorities and achievements during his tenure at PBGC.*

PBGC also received a Hammer Award for its efforts to reinvent customer service to better inform, reassure, and respond to workers and retirees about their pensions. The award highlighted the agency's information outreach to increase pension awareness among people in underfunded plans; townhall-style informational meetings that reached nearly 8,000 people in plans newly taken over by PBGC; and the new Customer Service Center.

## Closing Thoughts

During 1996, PBGC made substantial progress in preparing the pension insurance program to meet the needs of the coming century. For the first time in the agency's history, both PBGC insurance programs are fully funded, with assets that exceed benefits owed to more than 440,000 people.

This year's financial gains mark a significant step forward but by no means assure that PBGC is financially secure at last. Tens of billions of dollars of underfunding remain in plans covering millions of people and PBGC remains vulnerable to substantial losses from plan terminations, losses that could mean the return of the agency's deficit.

As millions of Americans approach their retirement years, our nation's working men and women need to be assured that the pensions they labored long and hard to attain will be there for them. This Administration's commitment to retirement security, and PBGC's progress in building a financially strong insurance program, provide hope for the future.

Martin Slate

Martin Slate
*Executive Director*

# Insurance Operations

The single-employer plan insurance program posted its first yearend financial surplus as losses from terminations of underfunded plans remained low despite an increase in completed plan terminations. PBGC's third five-year study of its separate insurance program for multiemployer plans found the program financially strong and recommended an increase in the program's benefit guarantee to offset the effect of wage inflation since 1980 on the value of the guarantee.

"The single-employer... program posted its first yearend financial surplus..."

## Single-Employer Program

Through its single-employer program, PBGC oversees the terminations of fully funded plans and guarantees payment of basic pension benefits when underfunded plans must be terminated.

**Standard Terminations:** An employer may end a fully funded plan in a standard termination by purchasing annuities or paying lump sums to participants. Standard terminations are subject to legal requirements governing notifications to participants and to PBGC and payment of benefits. PBGC may disallow standard terminations that do not comply with the requirements.

The number of standard terminations filed with PBGC declined again in 1996, to slightly more than 3,800. The agency permitted completion of nearly 3,100 standard terminations.

PBGC audits a statistically significant number of completed terminations to confirm compliance with the law and proper payment of benefits. These audits generally have found few and relatively small errors in benefit payments, which plan administrators are required to correct. The errors primarily are due to the use of incorrect interest-rate assumptions in valuing lump-sum distributions to plan participants.

**Distress and Involuntary Terminations:** Defined benefit plans that are not able to pay all promised benefits may be terminated either by the company responsible for the plan or by PBGC. An employer wishing to terminate an underfunded plan generally may do so only if the employer is being liquidated or if the termination is necessary for the company's survival. The employer must first prove to PBGC, or to a bankruptcy court if appropriate, that it and each of its affiliated companies meets one of the financial distress criteria set by law.

An underfunded plan also may be terminated involuntarily by PBGC when necessary to protect the interests of the participants or of the insurance program. PBGC must terminate any plan that does not have assets available to pay current benefits.

The reorganization of insurance operations, in conjunction with a change in PBGC's approach to termination of troubled underfunded plans, has enabled PBGC to shorten the time needed to complete the termination of underfunded plans. Under the new organizational structure, PBGC has dedicated more resources specifically to examining troubled plans and determining whether termination is justified. As a result, PBGC is moving more quickly to terminate underfunded plans requiring such action and the agency completed the termination of 255 underfunded plans during 1996, more than twice as many as were terminated the previous year. The vast majority were involuntary terminations by PBGC, generally because the sponsoring employer had gone out of business. Many of these plans had been under consideration for termination for a period of time and their actual termination dates occurred in earlier years, when the circumstances leading to their termination first arose.

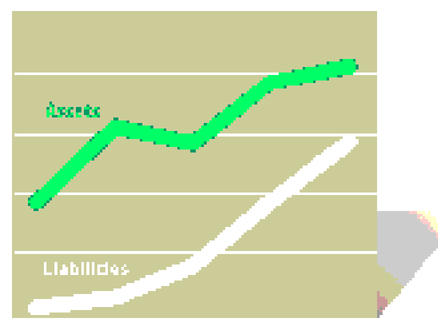
Terminations during the year included large plans from such diverse companies as Foster Grant, Inc., a Massachusetts manufacturer of sunglasses; Gulf USA, Inc., a company in Idaho with interests in mining and natural resources; McLouth Steel Products Corporation, a Michigan steelmaker; and United Merchants and Manufacturers, Inc., of New Jersey, a manufacturer and distributor of brand-name clothing.

**TRUSTEED PLANS:** During 1996, PBGC became trustee of 233 single-employer plans, many of which had termination dates in earlier years. The agency assumed responsibility for an additional 50,000 people in these plans. At yearend, PBGC was in the process of becoming trustee of an additional 122 single-employer plans. In all, including 10 multiemployer plans previously trusteed, a total of 2,348 terminated plans were trusteed or were being trusteed as of the end of the year. This total also reflects the elimination of one single-employer plan included in last year's total, which no longer required PBGC to become trustee.

## Multiemployer Program

The multiemployer program, which covers approximately 8.6 million workers and retirees in about 2,000 insured plans, is funded and administered separately from the single-employer program and differs from the single-employer program in several significant ways. The multiemployer program covers only collectively bargained plans involving more than one unrelated employer. For such plans, the event triggering PBGC's guarantee is the inability of a covered plan to pay benefits when due at the guaranteed level, rather than plan termination as required under the single-employer program. PBGC provides financial assistance through loans to insolvent plans to enable them to pay guaranteed benefits.

Multiemployer Program Assets and Liabilities




The significant reforms enacted in 1980 created several safeguards for the program, including a requirement that employers that withdraw from a plan pay a proportional share of the plan's unfunded vested benefits. These safeguards have permitted PBGC to maintain multiemployer premiums at a constant, reasonably low level.

The program continued to be financially healthy, with assets of $505 million, liabilities totaling $381 million for future benefits and nonrecoverable future financial assistance, and a net surplus of $124 million. The surplus reflected a net loss of $68 million for 1996 that stemmed from an increase in the allowance for nonrecoverable future financial assistance. This increase resulted from PBGC's estimate of the future costs of its agreement to assume a portion of the liabilities of the Amalgamated Insurance Fund if the plan is unable to meet statutory funding requirements in the future. Despite this year's loss, the program is strong and expected to remain so.

**Plan Underfunding:** Based on data as of the beginning of 1994 — the most recent information available — multiemployer plans had total assets of $202.8 billion and liabilities of $223.8 billion. Underfunding among these plans totaled about $30 billion; the underfunded plans had an average funding ratio of 81 percent, virtually the same as in the previous year. Overfunding among multiemployer plans totaled about $9 billion. The amount of underfunding reflected the low interest rates that prevailed in 1993, which substantially increased the value of plans'benefit liabilities, and does not capture subsequent changes in many plans' funding levels since 1993.

**Financial Assistance:** The multiemployer program has received relatively few requests for financial assistance. Since enactment of the reforms in 1980, PBGC has provided assistance to only 16 of the 2,000 insured plans, with a total value of approximately $33 million net of repaid amounts. In 1996, only 12 of these plans were still receiving assistance of about $5 million annually.

**Program Administration:** The 1980 reforms require PBGC to conduct a study of the multiemployer insurance program every five years to assess whether changes in the program's guarantee or premium level are necessary. PBGC's third study, sent to the Congress in June 1996, showed that the program is financially sound and is projected to maintain a surplus, with no change in premium level, under a wide range of economic scenarios. This confirmed similar findings in the two earlier studies.

The study also found that the real value of the program's modest benefit guarantee, which has remained unchanged since it was set in 1980, has been severely eroded by wage inflation and recommended that the Congress increase the guarantee for plans that become insolvent in the future. Under the program's current guarantee, the benefits of less than 1 percent of all workers and retirees would be fully insured by PBGC if their plan runs out of money. With the recommended change, nearly 75 percent of covered participants would receive their full benefits through PBGC's insurance. The guarantee increase would require no change in the multiemployer premium rate. The higher guarantee level was included in pension reform legislation submitted during the year by the President, but no legislative action was taken on the recommendation in 1996.

# Defined Benefit Pensions

The growing financial strength of the pension insurance program, reforms to improve pension funding, and the aging of "baby boomers" draw attention to the value of defined benefit pension plans. Defined benefit plans offer the advantage of a predictable retirement income backed by federal insurance. They also can contribute to employee motivation, productivity, and retention, a plus for plan sponsors.

The number of insured pension plans has decreased from more than 112,000 in 1985 to 47,500 in 1996. This decline primarily reflects small plan terminations and plan mergers. The number of large plans (5,000 or more participants) has increased from 928 in 1985 to 1,124 in 1996. The total number of participants covered by the insurance program has increased from about 39 million to 42 million over the same period.

"PBGC plays an important role in encouraging defined benefit plans..."

The growth of defined benefit plan participation has been affected by the reduction in employment in areas that have traditionally favored these plans (large firms, manufacturing sector, union workers). As the work force continues to age, the popularity of these plans may increase. PBGC plays an important role in encouraging defined benefit plans by providing security for participants' benefits.

## Single-Employer Program Exposure

As of the end of 1995, the vast majority of single-employer plans — about two-thirds — remained fully funded, with assets of all plans totaling about $1.13 trillion compared to vested liabilities totaling about $1.09 trillion. Pension underfunding of about $64 billion persisted although many of the underfunded plans, which had total assets of $415 billion and total liabilities of $479 billion for vested benefits, were sponsored by financially healthy firms.

While a core of pension underfunding persists, a major difference is that reforms of the Retirement Protection Act are in place to address the underfunding over time. Also, in removing the cap on premiums paid to PBGC by underfunded plans, the reforms provided an immediate response to the increased underfunding so that PBGC would remain strong.

PBGC determines pension underfunding based on interest and mortality assumptions that would have been used to purchase an annuity at the end of the year. Because of the filing and collection dates, the latest available information on pension underfunding is for the prior year. Underfunding rose from $31 billion largely because the interest rate PBGC used to determine the underfunding fell from 7.15% at the end of 1994 to 5.3% at December 31, 1995. This was the lowest yearend rate and the largest one-year decline in interest rates in PBGC's history. This interest rate reflects both the Treasury rate and other factors that make up the cost of an annuity on the market.

Pension underfunding in 1995 remained spread across all industries. The steel industry accounted for 16 percent of the underfunding, and another 16 percent was found in the automobile and transportation equipment industries. Underfunded plans covered about 15 million workers and retirees, some 7 million of whom were in plans that were funded 90 percent or more. Many of these plans had been fully funded and were drawn into the underfunding category by the abnormally low interest rate.

To measure how much of the current total underfunding may result in future claims, PBGC categorizes underfunding into three loss contingency classifications that follow generally accepted accounting principles and are based on the financial condition of plan sponsors. The classifications are probable, reasonably possible, and remote.

Probable claims are those that are likely to occur in a future year based on conditions that existed at PBGC's fiscal yearend. PBGC estimates and records them as liabilities as they are determined, as required by financial accounting standards. Since the estimated losses on these claims already have been recorded, the claims are not included as part of the current underfunding.

PBGC's reasonably possible claims arise from underfunded plans maintained by companies that may present risks to the insurance program and to workers and retirees, including companies with below-investment-grade bond ratings as of September 30, 1996. Total underfunding in these plans ranged from $22 billion to $26 billion.

The remaining underfunding was in plans categorized as remote claims. Pension underfunding in these plans is not presently a risk to participants or PBGC.

## Financial Forecasts

ERISA requires that PBGC annually provide an actuarial evaluation of its expected operations and financial status over the next five years. PBGC historically has extended these forecasts to cover 10 years.

PBGC's forecasts are subject to significant uncertainty since the amount of PBGC's future claims depends on many factors, including current underfunding among insured plans, any further erosion in funding, bankruptcies among plan sponsors, and recoveries from these bankrupt sponsors. These factors are influenced by future economic conditions, investment results, and the legal environment that the Congress and the courts create for PBGC's insurance program. Over the longer term, PBGC also will be affected by labor force trends, global trade, and employers' preferences for the variety of pension plans available.

PBGC's current methodology for the 10-year forecasts relies on an extrapolation of the agency's claims experience and the economic conditions of the past two decades. The forecasts do not reflect a full range of economic conditions and do not measure the high degree of uncertainty surrounding PBGC's future claims. To address the limitations of the forecast methodology, PBGC is developing a simulation model, called the Pension Insurance Modeling System (PIMS), to examine its financial condition under a full range of economic scenarios. Until PIMS is complete, PBGC is continuing to rely on its current methodology.

**TEN-YEAR FORECASTS:** PBGC's annual losses from underfunded single-employer plans have been variable and unpredictable throughout its history, with the largest losses tending to accompany large plan terminations. As a result, net losses have been higher in the most recent 10-year period, during which a number of major plan terminations occurred, than in the prior 12-year period.

PBGC has prepared three 10-year forecasts (A, B, and C) of its single-employer program using its current methodology to give a long-term view of the expected status under different loss scenarios. PBGC expects its history of significant annual variations in losses to continue. These forecasts include the significant improvement in PBGC's financial condition expected to result from the acceleration of plan funding and increase in PBGC's variable-rate premium receipts provided under the Retirement Protection Act. The improvements to plan funding over the long term, while reducing PBGC's revenues, also will reduce PBGC's exposure to loss.

Forecast A is based on the average annual net claims over PBGC's entire history ($481 million per year) and assumes the lowest level of future losses. Forecast A projects steady improvement in PBGC's financial condition, although the rate of improvement declines over time, and a surplus of $3.7 billion at the end of 2006.

Forecast B, which assumes the mid-level of future losses, is based upon the average annual net claims over the most recent 10 fiscal years ($571 million per year). It reflects the impact on PBGC's claims experience from the provisions of the Single-Employer Pension Plan Amendments Act of 1987, which significantly modified the requirements for termination of an underfunded plan. Forecast B projects net income levels that, while lower than Forecast A, still lead to a surplus of $2.5 billion at the end of 2006.

Forecast C is highly pessimistic and reflects the potential for heavy losses from the largest underfunded plans by assuming that the plans that represent reasonably possible losses will terminate uniformly over the next 10 years in addition to a modest number of lesser terminations each year. (Reasonably possible losses are discussed in Note 9 to the financial statements.) This forecast assumes $2.1 billion of net claims each year, resulting in the return and steady growth of PBGC's deficit throughout the 10-year period to $21.8 billion.

The 1996 forecasts share several assumptions. Average annual net claims and projected claims are in 1996 dollars. The present value of future benefits is valued at 6.55% and using other actuarial assumptions consistent with assumptions used to value the present value of future benefits in the financial statements as of September 30, 1996. PBGC's assets are projected to earn 6.55% annually. Benefits for plans terminating in the future are assumed to grow at 5.25% annually until termination. Plan funding ratios are assumed to increase at 1.5% per year from historical averages and recoveries from plan sponsors are assumed to be constant at 10% of plan underfunding. In a change of methodology, Forecast B was based on the average annual net claims over the most recent 10 fiscal years rather than upon average annual claims since 1982. The number of participants in insured single-employer plans is assumed to remain constant. The flat-rate portion of the single-employer premium is assumed to remain constant at $19 per participant. Receipts from the variable-rate portion of the premium are projected on the basis of a constant 30-year U. S. Treasury bond rate of 7.03%. Assumed administrative expenses through 2002 are consistent with PBGC's 1998 President's Budget submission and are projected to grow 5.25% each year thereafter.

## Responsive Services

Reassurance. Clear and complete answers to questions, without delay. Quick calculation of, and notification about, guaranteed benefits. Timely payments without interruption. These are the basic needs of the people to whom PBGC owes benefits, needs that PBGC is working to satisfy. PBGC significantly improved productivity and service with reengineered plan termination and benefit processing operations.

> "...significantly improved productivity and service with reengineered... operations."

### Benefit Processing

PBGC's responsibility for benefit payments begins immediately upon becoming trustee of a terminated plan. Top priority is given to maintaining uninterrupted benefit payments to existing retirees and commencing payments to new retirees without delay. Concurrently, PBGC staff also begin intensive efforts to notify plan participants of PBGC's trusteeship and to obtain essential data and records on each individual participant, a difficult task frequently complicated by inadequate plan and employer records.

PBGC pays estimated benefits to retirees until it has confirmed necessary data and valued plan assets and recoveries from the plan's sponsor. PBGC then calculates the actual benefit payable to each participant according to the specific terms of that person's plan, statutory guarantee levels, and the funds available from plan assets and employer recoveries. Benefit calculation can be an intricate process since each trusteed plan is different and must be separately administered.

By the end of the year, PBGC was responsible for the current and future pension benefits of about 441,000 participants from single-employer and multiemployer plans. These include nearly 200,000 retirees who received benefit payments totaling $792 million.

Yet, even with a 13 percent increase in the number of people to whom it owes benefits, PBGC continued to provide individual benefit determinations on the accelerated pace set in 1995. In 1996, PBGC issued nearly 66,000 benefit determinations, slightly exceeding the number issued one year earlier.


*PBGC's customer service has been recognized by awards.*

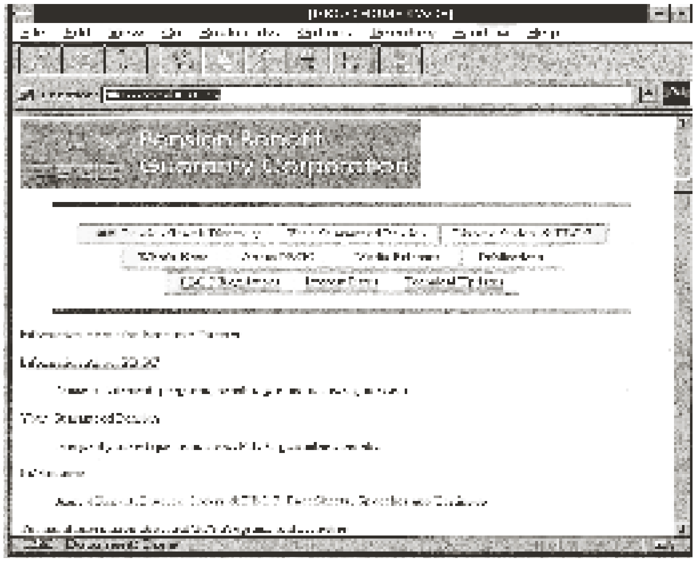
**Appeals of Benefit Determinations:** PBGC's Appeals Board reviews appeals of certain PBGC determinations. Almost all of the appeals are from people disputing benefit determinations. Due to PBGC's increased production of benefit determinations, the agency received more than 1,400 appeals in 1996, a record total. Typically, about 2 percent of all benefit determinations are appealed. Most appeals are resolved by appeals department and other PBGC staff without full Appeals Board review, as was the situation for 700 cases in 1996. The Board met to decide 212 appeals, 84 of which required changes in benefits primarily as a result of new facts, correction of calculation errors, or a different interpretation of plan provisions.

## Customer Service

New systems and procedures put in place in the past year are enabling the agency to provide more and better information more quickly to more people.

The Customer Service Center, implemented at the beginning of the year, is both a symbol of this progress and a key factor in PBGC's improved service. In the center's first year of operation, each customer service representative handled about 10,000 calls. With information readily available from PBGC's various automated databases, response times averaged less than 90 seconds per call. During the year, PBGC enhanced the Customer Service Center's telephone system to allow staff to transfer a call immediately to one of PBGC's regional benefit offices, thereby assuring that the caller receives direct assistance from the office responsible for that person's benefit without additional telephone calls.

**Service Improvements:** The Customer Service Center, with its toll-free telephone number, was the first step in making PBGC more accessible to the people it serves. The agency implemented additional measures during the year to make information more widely available. PBGC opened a Home Page on the Internet's World Wide Web, making up-to-date agency information and materials available electronically to anyone with a personal computer that can use Internet browser software.




The Home Page, which can be found at **http://www.pbgc.gov**, provides users with access to important agency information and materials. These include publications, press releases, regulations, and other materials such as frequently asked questions about the pension insurance program, technical information on interest rates, and interpretations of recent legal changes. PBGC also began sending an annual newsletter to people who have not yet begun receiving their benefit payments to let them know their promised pensions remain safe with PBGC and to give them information that will assist them in reaching the agency when they change their address or are ready to retire.

"The Home Page... can be found at http://www.pbgc.gov"

PBGC published a new informational booklet, entitled "Divorce Orders & PBGC," to help those who prepare domestic relations orders dividing PBGC-paid pension benefits in a divorce or legal separation. The new booklet reviews ERISA's requirements for qualified domestic relations court orders, discusses treatment of the alternate payees who may receive some of the benefit under such an order, and provides two types of model orders that may be used to draft domestic relations orders for submission to PBGC.

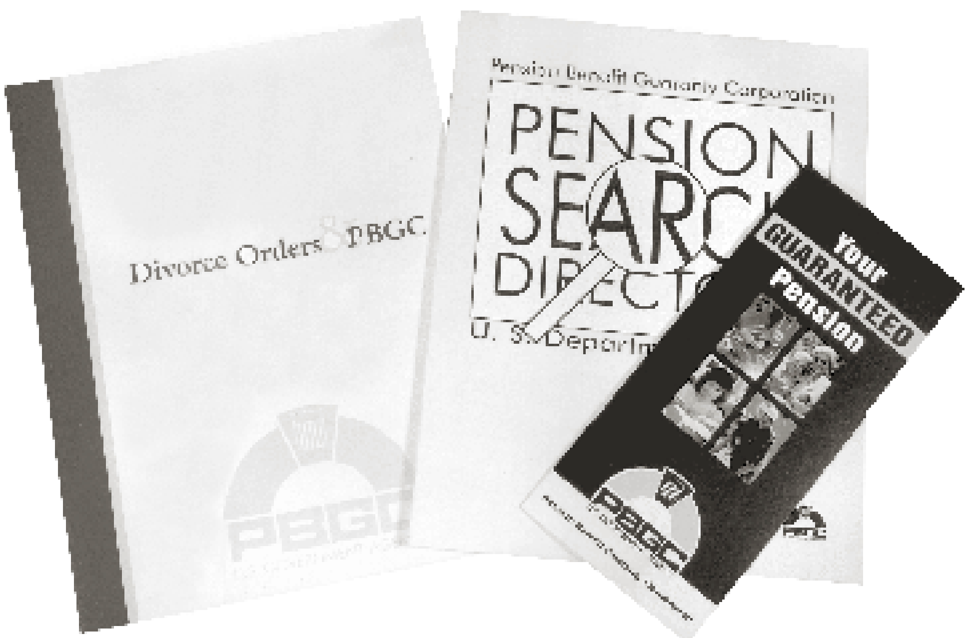
PBGC's rapid progress in improving service has been made possible by developments in the agency's technological base. The new automated optical imaging, participant record, and case administration systems provide PBGC staff with modern computerized systems that allow rapid access to needed documents and information on each person and pension plan under PBGC administration.

The agency's field operations have benefitted from this technological progress. Over the years, PBGC has made arrangements to open a number of small offices across the country to provide service to local concentrations of participants from larger terminated plans. Installation of a nationwide data communications network provided each office with direct links to PBGC's primary automated systems and data, ensuring efficiency and speed of service throughout the agency's operations. Each office also has its own optical imaging equipment. PBGC has been working to consolidate the field offices into strategically located regional centers to reduce operating costs without reducing service to participants. The second regional center, which began operation shortly after the year ended, is also being set up for disaster recovery with duplicate computerized plan and participant files in case the originals in Washington become lost or destroyed.

**Pension Search Program:** PBGC's ongoing efforts to find people missing from plans taken over by the agency continued to show success as the agency also began assuming payment obligations from employers for workers who are missing from terminating fully funded plans. In the past year, the agency located the addresses for another 16,000 previously unlocatable workers and retirees in terminated underfunded plans that PBGC now administers, bringing the total number found to more than 55,000 since PBGC initiated the original program four years ago.

PBGC initiated new programs in 1996 to broaden the search for missing workers. The first involved the new clearinghouse authorized by the Retirement Protection Act and established in January 1996 to assist employers who are terminating fully funded plans. These terminations cannot be completed until all benefits are distributed, and employers have long experienced difficulty in making arrangements with insurance companies and banks to ensure that missing participants receive the benefits owed them. The people who have been missed often have had no idea where to look for their benefits. Now, companies and their workers can turn to PBGC's Pension Search Program. In the first year of the clearinghouse's operation, 124 companies asked PBGC to find nearly 1,000 missing people, 750 of whom are due nearly $1.4 million in benefits. The other 200 people are covered by annuity contracts that will pay their benefits when they are found. By yearend, PBGC had found addresses for nearly 400 of the missing people, and 21 had returned benefit applications to the agency.

In a complementary effort, announced in December 1996, the Department of Labor and PBGC issued a "Pension Search Directory" that lists missing people who not even PBGC has been able to find and identifies the companies that had sponsored their pension plans and the dates the plans terminated. The directory may be viewed on the Internet at **http://www.dol.gov** or directly at **http://search.pbgc.gov** and is being publicized nationwide with the assistance of more than 20 organizations and unions. The initial directory provided information on 2,700 people who had worked for 565 companies and earned more than $10 million in benefits. In the first week after the announcement of the directory, the Internet listing received more than 60,000 "hits" and PBGC logged nearly 8,000 telephone inquiries through which it matched more than 180 callers to names in the directory. The directory will be updated with new names quarterly on the Internet.



## Proactive Enforcement

The Early Warning Program remained the centerpiece of PBGC's nationwide efforts to ensure that companies fund their pensions and honor their pension promises to their employees. When necessary, PBGC has continued to go to court to protect the retirement security of America's working men and women.

"...PBGC negotiators obtained settlements valued at more than $1 billion..."

### Early Warning Program

The Early Warning Program, which proactively prevents pension losses, continued to produce valuable settlements as the agency broadened the program's reach. Over the past year, PBGC financial analysts and actuaries closely monitored more than 500 companies with pension plans underfunded by at least $25 million. When they identified transactions or events that could jeopardize the pensions, they worked with the company involved to structure an agreement that would protect the interests of the company, its workers, and the pension insurance program. Through these efforts PBGC negotiators obtained settlements valued at more than $1 billion with 11 companies, providing contributions and other protections for the pensions of nearly 200,000 workers and retirees.

New reporting requirements imposed by the Retirement Protection Act already have strengthened the program. Several of the settlements achieved in 1996 resulted from information obtained through advance reports of certain transactions that now must be submitted by privately held or foreign companies with more than $50 million in underfunding. In other cases, companies contributed tens of millions of dollars to their plans to raise their funding above the underfunding threshold and avoid the reporting requirements.

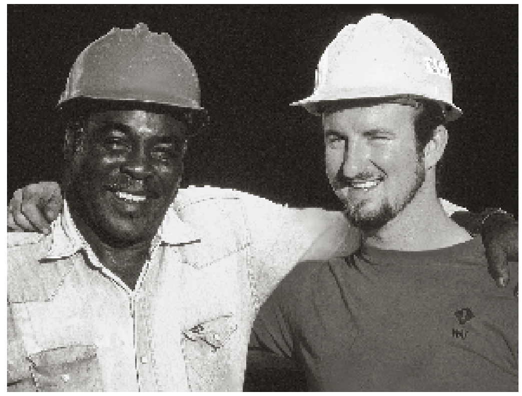
During 1996, PBGC broadened the program's scope to include additional single-employer plans as it began monitoring about 200 companies with pension plans that are underfunded between $5 million and $25 million and widened its focus to include plan mergers and spinoffs as well as corporate transactions.

**MICHELIN NORTH AMERICA, INC.:** Michelin's subsidiary, Uniroyal Goodrich Tire Company, had eight pension plans that covered some 28,000 workers and retirees and were underfunded by more than $450 million. Under an agreement reached in November 1995, Michelin added $380 million in cash to the Uniroyal Goodrich pension plans and will make additional contributions according to a six-year funding schedule. The company also planned to merge the eight Uniroyal Goodrich plans with another overfunded pension plan, producing a single plan covering more than 42,000 people that would be fully funded for vested benefits. In return for the additional contributions, PBGC agreed to release Michelin from certain of the advance reporting requirements.

**GULFSTREAM AEROSPACE CORPORATION:** Gulfstream planned a public offering of common stock and substantial new debt to raise capital with which to redeem the company's existing preferred stock and bank debt. The company's three pension plans, which covered more than 5,600 workers and retirees, were underfunded by about $50 million. PBGC received advance notice of the transaction and stepped in to ensure that the leveraged company provided funding for its pension obligations.

Under a preliminary agreement concluded in early October 1996, Gulfstream will accelerate funding of its plans by adding $120 million over five years, making the plans fully funded for vested benefits.

**CENTURY ALUMINUM COMPANY (RAVENSWOOD ALUMINUM CORPORATION):** For four years, Ravenswood had headed PBGC's annual listing of the 50 companies with the largest underfunded plans, with the poorest funding level of any of the companies listed. Ravenswood's two pension plans, covering about 2,700 people, had combined underfunding of about $100 million and enough assets to pay only about 29 percent of the total benefits owed. Under the April 1996 agreement, the company will add nearly $100 million to its pension plans over four years, $40 million of which is above the normal funding requirement. PBGC will hold a first security interest in all of Ravenswood's real property, plant facilities, and equipment until the pension underfunding is less than $10 million or its parent corporation, Century Aluminum, meets certain financial tests. In return for the negotiated pension protections, Century Aluminum's corporate parent, Glencore, was able to sell more than 20 percent of its interest in Century Aluminum to the public, thereby releasing the parent from future responsibility for Ravenswood's pensions.



**HAYES WHEELS INTERNATIONAL, INC./MOTOR WHEEL CORPORATION:** Hayes Wheels and Motor Wheel planned a merger for the summer of 1996 that PBGC believed would unreasonably increase its risk of loss from the companies'severely underfunded pension plans. In June 1996, the companies agreed to add a total of $54 million in cash to their plans over three years, and $6 million more to the Motor Wheel pensions each subsequent year, to protect the pensions of their 5,200 workers and retirees. Hayes Wheels has provided letters of credit to guarantee these contributions. After three years, the Hayes Wheels pensions will be almost fully funded and the Motor Wheel pensions will be almost 70 percent funded.

**KEYSTONE CONSOLIDATED INDUSTRIES, INC.:** Keystone required PBGC's permission to borrow funds for an acquisition of DeSoto, Inc., because of debt limitations imposed on Keystone when it received a minimum funding waiver from the Internal Revenue Service in 1985. In August 1996, PBGC agreed to allow Keystone to increase its indebtedness for the merger with DeSoto in return for the companies' agreement to consolidate four Keystone pension plans underfunded by more than $80 million with an overfunded DeSoto pension plan. The companies also agreed to make additional contributions to the consolidated plan covering 9,700 people should that plan's underfunding increase. The consolidation will reduce Keystone's underfunding to less than $30 million while the combined pensions will be 90 percent funded, resulting in a better pension arrangement overall.

**AMALGAMATED INSURANCE FUND:** The Amalgamated Insurance Fund, a multiemployer plan covering about 70,000 workers and retirees, had been under strain for several years as business failures in the men's suit industry reduced the number of employers contributing to the plan from 575 in 1986 to just 200 in 1996. The plan was underfunded by about $250 million. With the contraction of the industry, the funding obligations were increasingly burdensome and the remaining employers were considering a mass withdrawal from the plan. In such an event, PBGC would be required to assume financial responsibility for the plan. Under an agreement reached at yearend, the plan will continue with employers making annual contributions at their current rate. If those contributions fail to support the plan, PBGC will separate out and assume responsibility for the liabilities of the bankrupt employers, while solvent employers will continue to fund the remaining portion of the plan at the current rate. Employers who continue with the plan will have limitations on their liability if problems occur in the future. As a result of the agreement, workers will continue to earn benefits, retirees will collect full retirement benefits, and funding of the plan will improve, reducing the potential loss for the insurance program each year that the plan continues.

"Many pension issues can be settled through negotiations... others require resolution by the courts."

## Litigation

Many pension issues can be settled through negotiations but others require resolution by the courts. At the end of the year, PBGC had 81 active cases in state and federal courts and 788 bankruptcy cases.

**Piggly Wiggly Southern, Inc.:** Through a routine audit following the 1988 termination of a fully funded Piggly Wiggly pension plan, PBGC determined that the company significantly undervalued participants' lump sum benefits by using inappropriate interest rate assumptions. As a result of the incorrect valuation, many of the 2,500 plan participants failed to receive their full benefits and the company was able to recover a $2.7 million reversion of "excess assets" from the plan. When Piggly Wiggly refused to pay the additional pension benefits owed, PBGC filed suit in district court to enforce its audit findings. The district court ruled in favor of PBGC, Piggly Wiggly appealed, and, in March 1996, an appellate court affirmed the lower court's ruling. The litigation was concluded in July when the appellate court denied the company's petition for rehearing by the full court. PBGC estimates that the amount owed is $1.5 million.

**Smith Corona Corporation:** Smith Corona, in bankruptcy reorganization since July 1995, asked the bankruptcy court in August 1996 to allow termination of its salaried and hourly pension plans, each of which was underfunded by about $15 million. PBGC opposed the company's request before both the district and bankruptcy courts. PBGC's opposition in court, which included evidence demonstrating that the salaried plan could be maintained by the company, led to a negotiated agreement in December that will end the litigation. Under the agreement, which is subject to court approval, the reorganized Smith Corona will continue the salaried plan and PBGC will terminate and take over the plan for hourly workers. Nearly all of the company's 4,700 workers and retirees will receive their full benefits, either under the pension plan continued by the company or from PBGC's guarantee.

**Collins v. PBGC; Page v. PBGC:** These consolidated class-action suits were filed on behalf of participants in plans that terminated before December 31, 1981, without having been amended to adopt ERISA's minimum vesting standards. The plaintiffs sought a court ruling requiring PBGC to guarantee their benefits as if their plans had been amended. PBGC had determined at the time their plans terminated that only those benefits vested under the express terms of their plans were guaranteeable. PBGC's settlement with the plaintiffs was announced in December 1995 and received final court approval the following summer. Under the settlement, people who had 10 or more years of service, or their survivors, generally will receive about 80 percent of the benefits they did not receive at the time their plans terminated. Other people with between five and nine years of service will receive lesser amounts from a separate fund. About 40,000 people may be affected. The overall cost of the settlement, including administrative costs, is projected at around $100 million.

**Copperweld Steel Company:** PBGC continued to pursue bankruptcy claims to recover amounts due PBGC and Copperweld's three terminated pension plans, which covered about 3,000 workers and retirees. In October 1995, Copperweld sold its assets as part of a confirmed plan of reorganization

that required the company to establish a full cash reserve against PBGC's $8.8 million unpaid minimum funding contribution claims and a partial reserve against PBGC's $52 million unfunded benefit liabilities claims.  The company's liquidation trustee contests the extent to which PBGC's minimum funding contribution claims made on behalf of pension plans are entitled to priority under the Bankruptcy Code and whether the factors prescribed in PBGC's regulations appropriately measure PBGC's unfunded benefit liabilities claims for terminated pension plans that are trusteed by PBGC.  These issues are central to PBGC's ability to recover its losses from bankrupt employers.  PBGC and the liquidation trustee have filed and argued summary judgment motions in the bankruptcy court and are awaiting the court's decision.  Trial on any outstanding issues is expected to take place during 1997.

**CF&I Steel Corporation:** PBGC continued to pursue its claims against the reorganized CF&I for a CF&I plan that was underfunded by about $221 million when terminated in March 1992.  In a November 1994 ruling, a district court denied priority to most of PBGC's claims for minimum funding contributions owed to CF&I's plan and for the plan's underfunding.  The court also remanded the case to the bankruptcy court for reconsideration of the amount of PBGC's underfunding claim, ruling that the bankruptcy court erred in "deferring" to PBGC's interest rate assumption.  The bankruptcy court subsequently revalued PBGC's claim for unfunded benefit liabilities from about $221 million to about $123 million based on a "discount rate" that differed from the assumptions prescribed by PBGC's regulation.  PBGC has appealed this ruling to the district court.

**White Consolidated Industries, Inc.:** White continued to contest PBGC's claims for the estimated $120 million underfunding in pension plans that White transferred to Blaw Knox Corporation in 1985.  PBGC is alleging that a principal purpose of White in entering into the transaction was to evade pension liabilities.  PBGC has taken over all the Blaw Knox plans either because they ran out of money or because they would have been abandoned after Blaw Knox ceased business and sold its assets in 1994.  The case remained pending before a district court at yearend, with trial scheduled for March 1997.

## Rulemaking

As part of the President's Regulatory Reinvention Initiative, PBGC clarified and simplified its regulations to make them easier to use, in the process reducing the volume of regulations by 20 percent. The agency eliminated a number of obsolete regulations and renumbered the remaining regulations to track the statutory sections they implement.

The Retirement Protection Act identified four new corporate events that must be reported to PBGC by all companies, and PBGC added two more under authority given it by the new law. The agency's first use of negotiated rulemaking quickly developed the necessary changes to reporting rules on events that may jeopardize workers' pensions and the pension insurance program. A 14-member committee representing employers, workers, retirees, pension practitioners, and PBGC negotiated proposed amendments to address the new requirements and to provide some reporting relief. PBGC also developed optional reporting forms that simplify companies' initial information filings. With negotiated rulemaking, PBGC was able to publish the proposed amendments in July 1996 and issue final rules in December.

Another Retirement Protection Act reform established a new requirement for annual submission of financial and actuarial reports by corporate groups with severely underfunded pension plans. PBGC published final rules implementing this requirement in December 1995. During that same month, the agency issued other final regulations implementing the new missing participants program.

The agency also published final rules in 1995 to implement the new requirement that participants in underfunded plans be notified annually about the funding status of their plan and the limits on PBGC guarantees. The notice requirement applied only to large plans for 1995 and was extended in 1996 to companies with small plans covering 100 or fewer people. PBGC began monitoring companies' compliance with the requirement through a random survey of about 600 companies with large underfunded plans, which confirmed that the notices were being sent, and also required companies to certify compliance as part of their annual premium filing to PBGC.

# Technology and Management

PBGC worked to strengthen programs and operations in all areas of the agency through improved automation and training while it adopted refinements to further improve financial management.

## Technology Advances

"New automated systems... upgrading PBGC's ability..."

New automated systems for participant information management, premium accounting, and legal management began operations during the year, significantly upgrading PBGC's ability to rapidly process and retrieve critical information. The participant information management system incorporates innovative software for automated creation of correspondence and forms that PBGC will be seeking to patent. An optical imaging system converts documents to computerized images and marks a profound advance in the agency's record management. PBGC has scanned more than 10 million pages of documents and has begun scanning new documents as they are received.

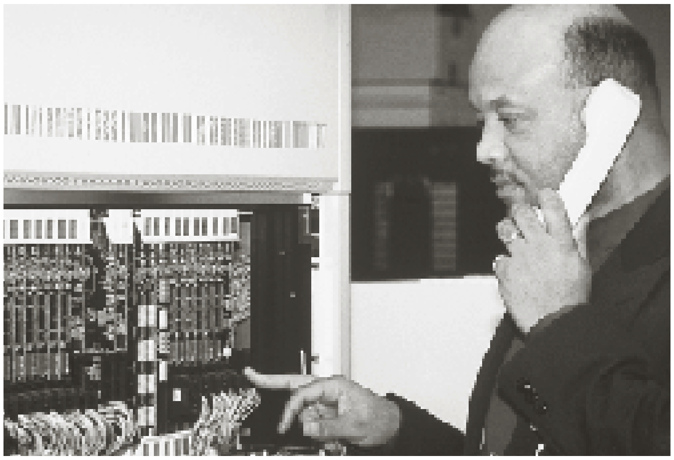
PBGC also moved to improve service at its field benefit offices by installing a special data communications network that links each of the offices with the agency's headquarters location in Washington, DC. The Wide Area Network provides each office with direct high-speed access to the same systems and data available to PBGC headquarters staff. It also allows video teleconferencing and virtually instantaneous exchange of data and images between the field offices and PBGC headquarters.

The quality of the premium accounting system has been recognized through a Technology Excellence Award presented by the Interagency Committee on Information Resources Management to PBGC Chief Financial Officer N. Anthony Calhoun. For the second year in a row, PBGC and the agency's telecommunications manager received awards from the General Services Administration in recognition of improved telecommunications systems.

PBGC took additional steps to develop the systems and applications architecture that will ensure consistency among current and future systems. By the end of the year the agency had completed disaster recovery tests on significant elements of its information systems, furthering its effort to implement a comprehensive continuity-of-operations plan.

## Employee Development

PBGC continued to strengthen its employee training programs. Because many PBGC positions require specific skills for which training by others is not available, the agency has tapped in-house expertise to create customized courses in four training areas: common needs, supervisory and management skills, new employee orientation, and specialized or technical training. The curriculum now has some 130 courses taught in an eight-classroom Training Institute that offers videoconferencing and other electronic capabilities for groups ranging from small seminars to large audiences.



## Financial Management

Sound, consistent financial management is now a hallmark of PBGC. For the fourth year in a row, PBGC's financial statements have received an unqualified opinion from the agency's auditors. The 1996 audit was again performed by Price Waterhouse LLP under the direction and oversight of PBGC's Inspector General.

Record premium income of nearly $1.2 billion, augmented by investment income totaling more than $900 million, enabled PBGC to erase the longstanding deficit in the single-employer program. The automated capabilities of PBGC's new premium accounting system, in combination with the agency's premium compliance program, have significantly enhanced PBGC's ability to promptly collect premiums due the agency. PBGC's escalating program of field examinations of pension plans is proving highly effective in ensuring that premium payments are accurately calculated and paid, having collected about $3 million in additional premium amounts owed at a cost of only $400,000.

"Sound, consistent financial management is now a hallmark of PBGC."

Shortly after the year ended, PBGC also announced a new two-tier premium penalty structure designed to encourage voluntary correction of any errors in premium payments. Under the new penalty policy, employers who pay any unpaid amount before receiving a PBGC notification regarding an actual or possible delinquency will be charged a penalty rate of 1 percent of the unpaid amount per month. Those who pay after PBGC issues a premium notice will still be charged the current penalty rate of 5 percent per month.

## Investment Program

The Corporation has approximately $12.2 billion of total assets available for investment, consisting of premium revenues accounted for in the Revolving Funds and assets from terminated plans and their sponsors accounted for in the Trust Funds.  The Revolving Funds are required to be invested in fixed-income securities; current policy is to invest these funds only in Treasury securities.  PBGC has more discretion in its investment of the Trust Funds, which are primarily invested in high-quality equities, with asset allocation designed for sound long-term performance.

The Revolving Fund monies are invested solely in U.S. Treasury securities, which PBGC uses to earn a competitive return and partially offset changes in its benefit liabilities.  The agency's investment in equities provides overall portfolio diversification and a higher long-term expected return, within prudent levels of risk.  PBGC uses institutional investment management firms to invest its assets subject to PBGC oversight.  PBGC's investment portfolio is structured to improve PBGC's financial condition in a stable manner over the long term.  PBGC continually reviews its investment strategy to ensure that the agency maintains an investment structure that is consistent with its long-term objectives and responsibilities.

**Investment Profile:** As of September 30, 1996, the value of PBGC's total investments, including cash, was approximately $12.2 billion.  The Revolving Fund's value was $7.2 billion and the Trust Fund's value was $5.0 billion.

PBGC's fund allocation further shifted toward equities during 1996 due primarily to strong equity returns.  Cash and fixed-income securities represented 63 percent of the total fund at the end of the year, as compared to 68 percent at the end of 1995, while the equity allocation stood at 36 percent of all investments compared to 32 percent one year earlier.  A very small portion of the invested portfolio remains in real estate and other financial instruments.

### Investment Profile

| | September 30, | |
|---|---|---|
| | **1996** | 1995 |
| **Fixed-Income Assets** | | |
| Average Quality | **AAA** | AAA |
| Average Maturity (years) | **22.6** | 21.4 |
| Duration (years) | **10.1** | 10.3 |
| Yield to Maturity (%) | **7.2** | 6.6 |
| **Equity Assets** | | |
| Average Price/Earnings Ratio | **19.7** | 18.0 |
| Dividend Yield (%) | **2.0** | 2.4 |
| Beta | **1.08** | 1.06 |

**Investment Results:** Fiscal year 1996 was a favorable year for capital market investments and PBGC's investment program. The broad stock market, as measured by the Wilshire 5000 Index that most closely reflects PBGC's equity portfolio, advanced 18.9%, while PBGC's equity program advanced 19.7%. PBGC's fixed-income program returned 2.2% for the year, while the Lehman Brothers Long Treasury Index gained 2.3%. For the year, PBGC reported income of $202 million from fixed-income investments and $695 million from equity investments. Other investments, including real estate and insurance contracts, produced a small gain of $30 million, for total investment income of $927 million.

### Investment Performance
*(Annual Rates of Return)*

| | September 30, 1996 | September 30, 1995 | Five Years Ended September 30, 1996 |
|---|---|---|---|
| Total Invested Funds | **8.5%** | 24.1% | 12.3% |
| Equities | **19.7** | 30.9 | 15.6 |
| Fixed-Income | **2.2** | 22.6 | 10.6 |
| Trust Funds | **18.6** | 26.8 | 14.5 |
| Revolving Funds | **2.3** | 22.5 | 11.2 |
| **Indices** | | | |
| Wilshire 5000 | **18.9** | 29.1 | 15.3 |
| S&P 500 Stock Index | **20.3** | 29.7 | 15.2 |
| Lehman Brothers Long Treasury Index | **2.3** | 23.0 | 9.1 |

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## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### General

The following discussion and analysis provide information that management believes is relevant to an assessment and understanding of the Corporation's financial condition and results of operations. The discussion should be read in conjunction with the financial statements and notes thereto.

PBGC's operating results are subject to significant fluctuation from year to year depending on the frequency and severity of losses from terminating pension plans, general economic conditions, and other factors such as changes in law. Consequently, certain traditional financial ratios and measurements are not meaningful and, therefore, not presented.

### Combined Results

For 1996, PBGC's combined underwriting and financial activities resulted in a net gain of $1.116 billion on gross income of $2.122 billion. The single-employer program earned net income of $1.184 billion and the multiemployer program reported a net loss of $68 million. By law, these two programs are separate.

### Single-Employer Program

Results of Activities and Trends: The net income in 1996 was $1.184 billion compared to net income of $925 million in 1995. The $259 million increase was primarily attributable to the increase in premium income.

Underwriting Activity: The gain of $760 million in 1996 was in contrast to a gain of $620 million in 1995. This $140 million difference was primarily due to the $308 million increase in premium income. This was attributable to a decrease in the funding levels of a large number of single-employer plans caused by historically low interest rates and to the phaseout of the cap on variable-rate premiums, which resulted in higher income from variable-rate premium payments.

Underwriting income increased from $856 million in 1995 to $1.172 billion in 1996. The $316 million increase was primarily due to the increase in variable-rate premium payments.

The Corporation's losses from completed and probable plan terminations decreased from $169 million in 1995 to $118 million in 1996. Although there were no major plan terminations in 1996, losses are unpredictable.

Operating costs increased 7.7 percent in 1996 from $130 million to $140 million.

Actuarial adjustments in 1996 resulted in a charge of $151 million versus a credit of $82 million in 1995. The $233 million increase was primarily due to modifications made to PBGC's expense formula to more closely match the agency's annual claims-related expenses.

Financial Activity: Investment income offset actuarial charges in 1996, resulting in a $424 million gain versus a $305 million gain in 1995. The total return on investments was 8.5% in 1996, compared to 24.1% in 1995. Fixed-income investments experienced a lower return in 1996 than in 1995 due to rising interest rates. PBGC, in accordance with generally accepted accounting principles, marks its assets and liabilities to market.

Actuarial charges primarily resulted from the aging of the present value of future benefits and from changes in interest rates. In 1996, the select interest rate assumption increased from 6.5% at September 30, 1995, to 6.6% at September 30, 1996, while the ultimate rate decreased from 5.0% to 4.75%. In addition, the number of years used for the select rate increased from 20 to 25 years in order to continue to match the survey on insurance prices provided by the American Council of Life Insurance. The passage of time and change in the interest rates resulted in an actuarial charge of $481 million in 1996, compared to an actuarial charge of $1.643 billion in 1995.

Liquidity and Capital Resources: The single-employer fund's net position improved in 1996 to a positive $869 million primarily because of higher premium income and continued strong return on investment earnings. Approximately $11.8 billion (98 percent) of the fund's total assets of $12 billion are in marketable assets.

PBGC's primary sources of cash are from premium receipts and investment activities. If funds generated from these sources are insufficient to meet fixed charges in any period, the Corporation has available a $100 million line of credit from the U.S. Treasury for liquidity purposes. PBGC did not use this borrowing authority in 1995 or 1996 and has no plans to use it in the near future.

There are significant factors that PBGC cannot control (e.g., interest rates, contributions made to the plans by sponsors, etc.) making it difficult to project premium revenue with a high degree of certainty. Benefit payments and administrative expenses should be approximately $1 billion in 1997.

The Corporation is subject to litigation that could have considerable impact on its financial condition. Also, the total underfunding in large plans that are sponsored by companies with below-investment-grade bond ratings ranges from approximately $22 billion to $26 billion. Losses from these plans are not probable at this time but generally accepted accounting principles require the exposure to be disclosed in the footnotes of the financial statements. This exposure is primarily in the steel, airline, transportation equipment, and industrial and commercial machinery industries.

The positive net position of $869 million at yearend will help provide the financial foundation needed to support the Corporation's long-term responsibilities under the Employee Retirement Income Security Act. A properly managed insurance program must have the resources to provide for unforeseen losses from terminating pension plans.

## Multiemployer Program

**Results of Activities and Trends:** The multiemployer program sustained a loss of $68 million in 1996 compared to a loss of $5 million in 1995. This year's loss was primarily due to the accrual of nonrecoverable future financial assistance for a large plan classified as a probable. The accrual of the future nonrecoverable financial assistance resulted in a loss of $102 million in 1996 as compared to a loss of $108 million in 1995. Premium income remained constant at $22 million. Investment income decreased from $83 million in 1995 to $12 million in 1996. Of the fund's assets, 93.8 percent and 95.8 percent were invested in Treasury securities in 1996 and 1995, respectively.

**Liquidity and Capital Resources:** As the multiemployer program has a positive net position and most assets are highly liquid Treasury securities, PBGC has sufficient resources to meet its liquidity requirements now and in the long-term future. Premium receipts will approximate $21 million, while benefit payments and financial assistance will be about $8 million for 1997.

## Federal Managers' Financial Integrity Act Statement

Management controls in effect in 1996 provided reasonable assurance that assets were safeguarded from material loss and that transactions were executed in accordance with management's authority and with significant provisions of selected laws and regulations. Furthermore, PBGC management controls provided reasonable assurance that transactions were properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with generally accepted accounting principles and to maintain accountability for assets among funds.

Although the controls were adequate to provide reasonable assurance, management continued efforts to resolve three weaknesses previously identified. Substantial improvements were made during 1996 as one weakness was corrected and initiatives are underway to overcome the remaining two weaknesses in strategic information management and the integration of PBGC's financial management systems by September 1997.

PBGC's management is responsible for the accompanying Statements of Financial Condition as of September 30, 1996 and 1995, the related Statements of Operations and Changes in Net Position, and the Statements of Cash Flows for the years then ended. PBGC's management is also responsible for establishing and maintaining systems of internal accounting and administrative controls that provide reasonable assurance that the control objectives – preparing reliable financial statements, safeguarding assets, and complying with laws and regulations – are achieved.

The Inspector General engaged Price Waterhouse LLP (Price Waterhouse) to conduct the audit of the Corporation's 1996 and 1995 financial statements. In its opinion on PBGC's financial statements, Price Waterhouse reported that the Statements of Financial Condition as of September 30, 1996 and 1995, Statements of Operations and Changes in Net Position, and Statements of Cash Flows for the fiscal years ended September 30, 1996 and 1995, were fairly stated in all material respects.

In the opinion of management, the financial statements present fairly the financial position of PBGC at September 30, 1996, and September 30, 1995, and the results of operations and cash flows for the years then ended, in conformity with generally accepted accounting principles and actuarial standards applied on a consistent basis.

Estimates of probable terminations, nonrecoverable future financial assistance, amounts due from employers, and the present value of future benefits may have a material effect on the financial results being reported. In addition, pending litigation could have a material impact on the financial condition of the Corporation. PBGC believes, however, that its legal positions have merit and that its positions will be upheld by the courts.

As a result of the aforementioned, these statements are based, in part, upon informed judgments and estimates for those transactions not yet complete or for which the ultimate effects cannot be precisely measured, or for those that are subject to the effects of any pending litigation.

Martin Slate
*Executive Director*

N. Anthony Calhoun
*Deputy Executive Director*
*and Chief Financial Officer*

January 10, 1997

## PENSION BENEFIT GUARANTY CORPORATION
## STATEMENTS OF FINANCIAL CONDITION

| | Single-Employer Program | | Multiemployer Program | | Memorandum Total | |
|---|---|---|---|---|---|---|
| | September 30, | | September 30, | | September 30, | |
| *(Dollars in millions)* | **1996** | 1995 | **1996** | 1995 | **1996** | 1995 |
| **Assets** | | | | | | |
| Cash and cash equivalents | **$ 674** | $ 437 | **$ 24** | $ 12 | **$ 698** | $ 449 |
| Investments, at market (Note 3): | | | | | | |
| Fixed maturity securities | **6,479** | 6,177 | **471** | 457 | **6,950** | 6,634 |
| Equity securities | **4,369** | 3,270 | **3** | 3 | **4,372** | 3,273 |
| Real estate | **53** | 62 | **0** | 0 | **53** | 62 |
| Other | **90** | 80 | **0** | 0 | **90** | 80 |
| Total investments | **10,991** | 9,589 | **474** | 460 | **11,465** | 10,049 |
| Receivables, net: | | | | | | |
| Sponsors of terminated plans | **44** | 76 | **0** | 0 | **44** | 76 |
| Sponsors of restored plans (Note 4) | **51** | 49 | **0** | 0 | **51** | 49 |
| Premiums | **63** | 27 | **1** | 0 | **64** | 27 |
| Sale of securities | **28** | 25 | **0** | 0 | **28** | 25 |
| Notes receivable (Note 5) | **86** | 82 | **0** | 0 | **86** | 82 |
| Investment income | **97** | 69 | **6** | 5 | **103** | 74 |
| Other | **5** | 13 | **0** | 0 | **5** | 13 |
| Total receivables | **374** | 341 | **7** | 5 | **381** | 346 |
| Furniture and fixtures, net | **4** | 4 | **0** | 0 | **4** | 4 |
| Total assets | **$12,043** | $10,371 | **$505** | $477 | **$12,548** | $10,848 |

The accompanying notes are an integral part of these financial statements.

# STATEMENTS OF FINANCIAL CONDITION

| *(Dollars in millions)* | Single-Employer Program | | Multiemployer Program | | Memorandum Total | |
|---|---|---|---|---|---|---|
| | September 30, | | September 30, | | September 30, | |
| | **1996** | 1995 | **1996** | 1995 | **1996** | 1995 |
| **Liabilities** | | | | | | |
| Present value of future benefits, net (Note 6): | | | | | | |
| Trusteed plans | **$ 9,520** | $ 9,016 | **$ 9** | $ 10 | **$ 9,529** | $ 9,026 |
| Terminated plans pending trusteeship | **223** | 193 | **0** | 0 | **223** | 193 |
| Settlements and judgments | **62** | 0 | **0** | 0 | **62** | 0 |
| Claims for probable terminations | **955** | 1,179 | **0** | 0 | **955** | 1,179 |
| Total present value of future benefits, net | **10,760** | 10,388 | **9** | 10 | **10,769** | 10,398 |
| Present value of nonrecoverable future financial assistance (Note 7) | | | **365** | 268 | **365** | 268 |
| Unearned premiums | **296** | 197 | **7** | 7 | **303** | 204 |
| Accounts payable and accrued expenses (Note 8) | **118** | 101 | **0** | 0 | **118** | 101 |
| Commitments and contingencies (Notes 9, 10, and 17) | | | | | | |
| Total liabilities | **11,174** | 10,686 | **381** | 285 | **11,555** | 10,971 |
| **Net position** | **869** | (315) | **124** | 192 | **993** | (123) |
| Total liabilities and net position | **$12,043** | $10,371 | **$505** | $477 | **$12,548** | $10,848 |

The accompanying notes are an integral part of these financial statements.

## PENSION BENEFIT GUARANTY CORPORATION
## STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION

| | Single-Employer Program | | Multiemployer Program | | Memorandum Total | |
|---|---|---|---|---|---|---|
| | For the Years Ended September 30, | | For the Years Ended September 30, | | For the Years Ended September 30, | |
| *(Dollars in millions)* | **1996** | 1995 | **1996** | 1995 | **1996** | 1995 |
| Underwriting: | | | | | | |
| Income: | | | | | | |
| Premium (Note 11) | **$1,146** | $ 838 | **$ 22** | $ 22 | **$1,168** | $ 860 |
| Other (Note 12) | **26** | 18 | **1** | 0 | **27** | 18 |
| Total | **1,172** | 856 | **23** | 22 | **1,195** | 878 |
| Expenses: | | | | | | |
| Administrative | **140** | 130 | **0** | 0 | **140** | 130 |
| Other | **3** | 19 | **0** | 0 | **3** | 19 |
| Total | **143** | 149 | **0** | 0 | **143** | 149 |
| Other underwriting activity: | | | | | | |
| Losses from completed and probable terminations (Note 13) | **118** | 169 | **0** | 0 | **118** | 169 |
| Losses from financial assistance (Note 7) | | | **102** | 108 | **102** | 108 |
| Actuarial adjustments (Note 6) | **151** | (82) | **0** | 0 | **151** | (82) |
| Total | **269** | 87 | **102** | 108 | **371** | 195 |
| Underwriting income (loss) | **760** | 620 | **(79)** | (86) | **681** | 534 |
| Financial: | | | | | | |
| Investment income (loss) (Note 14): | | | | | | |
| Fixed | **191** | 1,187 | **11** | 82 | **202** | 1,269 |
| Equity | **694** | 779 | **1** | 1 | **695** | 780 |
| Other | **30** | (10) | **0** | 0 | **30** | (10) |
| Total | **915** | 1,956 | **12** | 83 | **927** | 2,039 |
| Expenses: | | | | | | |
| Investment | **10** | 8 | **0** | 0 | **10** | 8 |
| Actuarial charges (credits) (Note 6): | | | | | | |
| Due to passage of time | **615** | 642 | **1** | 1 | **616** | 643 |
| Due to change in interest rates | **(134)** | 1,001 | **0** | 1 | **(134)** | 1,002 |
| Total | **491** | 1,651 | **1** | 2 | **492** | 1,653 |
| Financial income | **424** | 305 | **11** | 81 | **435** | 386 |
| Net income (loss) | **1,184** | 925 | **(68)** | (5) | **1,116** | 920 |
| Net position, beginning of year | **(315)** | (1,240) | **192** | 197 | **(123)** | (1,043) |
| Net position, end of year | **$ 869** | $ (315) | **$124** | $192 | **$ 993** | $ (123) |

The accompanying notes are an integral part of these financial statements.

## PENSION BENEFIT GUARANTY CORPORATION
## STATEMENTS OF CASH FLOWS

| *(Dollars in millions)* | Single-Employer Program For the Years Ended September 30, **1996** | 1995 | Multiemployer Program For the Years Ended September 30, **1996** | 1995 | Memorandum Total For the Years Ended September 30, **1996** | 1995 |
|---|---|---|---|---|---|---|
| **Operating Activities:** | | | | | | |
| Premium receipts | **$ 1,191** | $ 836 | **$ 21** | $ 23 | **$ 1,212** | $ 859 |
| Interest and dividends received, net | **509** | 465 | **32** | 28 | **541** | 493 |
| Cash received from plans upon trusteeship | **47** | 42 | **0** | 0 | **47** | 42 |
| Receipts from sponsors | **47** | 189 | **0** | 0 | **47** | 189 |
| Other receipts | **17** | 19 | **0** | 0 | **17** | 19 |
| Receipts of notes receivable | **8** | 6 | **0** | 0 | **8** | 6 |
| Benefit payments – trusteed plans | **(778)** | (737) | **(2)** | (2) | **(780)** | (739) |
| Payment of Pan Am annuities settlement | **0** | (25) | **0** | 0 | **0** | (25) |
| Financial assistance payments | | | **(5)** | (4) | **(5)** | (4) |
| Settlements and judgments | **(35)** | 0 | **0** | 0 | **(35)** | 0 |
| Payments for administrative and other expenses | **(158)** | (141) | **0** | 0 | **(158)** | (141) |
| Net cash provided by operating activities (Note 16) | **848** | 654 | **46** | 45 | **894** | 699 |
| **Investing Activities:** | | | | | | |
| Proceeds from sales of investments | **5,093** | 2,646 | **176** | 86 | **5,269** | 2,732 |
| Payments for purchases of investments | **(5,704)** | (3,490) | **(210)** | (141) | **(5,914)** | (3,631) |
| Net cash used in investing activities | **(611)** | (844) | **(34)** | (55) | **(645)** | (899) |
| Net increase (decrease) in cash and cash equivalents | **237** | (190) | **12** | (10) | **249** | (200) |
| Cash and cash equivalents, beginning of year | **437** | 627 | **12** | 22 | **449** | 649 |
| Cash and cash equivalents, end of year | **$ 674** | $ 437 | **$ 24** | $ 12 | **$ 698** | $ 449 |

The accompanying notes are an integral part of these financial statements.

## Note 1 – Organization and Purpose

The Pension Benefit Guaranty Corporation (PBGC or Corporation) is a federal corporation created by Title IV of the Employee Retirement Income Security Act of 1974 (ERISA) and subject to the provisions of the Government Corporation Control Act. Its activities are defined in ERISAas amended by the Multiemployer Pension Plan Amendments Act of 1980, the Single-Employer Pension Plan Amendments Act of 1986, the Pension Protection Act of 1987, and the Retirement Protection Act of 1994. The Corporation insures pensions, within statutory limits, of participants in covered single-employer and multi-employer defined benefit pension plans that meet the criteria specified in Section 4021 of ERISA.

ERISArequires that PBGC programs be self-financing. The Corporation finances its operations through premiums collected from covered plans, assets assumed from terminated plans, collection of employer liability payments due under ERISAas amended, and investment income. In addition, PBGC may borrow up to $100 million from the U.S. Treasury to finance its operations. The Corporation did not use this borrowing authority during the years ended September 30, 1996, or September 30, 1995, nor is use of this authority currently planned. ERISAprovides that the U.S. Government is not liable for any obligation or liability incurred by PBGC.

Under the single-employer program, PBGC is liable for the payment of guaranteed benefits with respect only to underfunded terminated plans. An underfunded plan may terminate only if PBGC or a bankruptcy court finds that one of the four conditions for a distress termination, as defined in ERISA, is met or if PBGC involuntarily terminates a plan under one of five specified statutory tests. The net liability assumed by PBGC is generally equal to the present value of the future benefits (including amounts owed under Section 4022(c) of ERISA) less (1) the amounts that are provided by the plan's assets and (2) the amounts that are recoverable by PBGC from the plan sponsor and members of the plan sponsor's controlled group, as defined by ERISA.

Under the multiemployer program, if a plan becomes insolvent, it receives financial assistance from PBGC to allow the plan to continue to pay participants their guaranteed benefits. Such assistance is recognized as a loss to the extent that the plan is expected to be unable to repay these amounts from future plan contributions, employer withdrawal liability, or investment earnings.

## Note 2 – Significant Accounting Policies

**Revolving and Trust Funds:** PBGC accounts for its single-employer and multiemployer programs'revolving and trust funds on an accrual basis. Each fund is charged a pro rata portion of the benefits paid each year. The revolving and trust funds have been combined for presentation purposes in the financial statements. The single-employer and multiemployer programs are separate programs by law and, therefore, are reported separately.

ERISAprovides for the establishment of revolving funds to be used by PBGC in carrying out its duties. The revolving funds support the operational and administrative functions of PBGC and fund any deficits incurred by PBGC in trusteeing plans or providing financial assistance. Premiums collected from ongoing plans are accounted for through the revolving funds. The Pension Protection Act of 1987 created a single-employer revolving fund that is credited with all premiums in excess of $8.50 per participant, including all penalties and interest charged on these amounts, as well as investment income. This fund may not be used to pay PBGC's administrative costs or the benefits of any plan terminated prior to October 1, 1988, unless no other amounts are available.

The trust funds reflect accounting activity associated with: (1) trusteed plans – plans for which PBGC has legal responsibility, (2) plans pending trusteeship – terminated plans for which PBGC has not become legal trustee by fiscal yearend, and (3)probable terminations – plans that PBGC determines are likely to terminate and be trusteed by PBGC. PBGC cannot exercise legal control over a plan's assets until PBGC becomes trustee, which may be several years after the date of plan termination.

**Allocation of Revolving and Trust Funds:** Revolving and trust fund assets, liabilities, income, and expenses are allocated to each program's revolving and trust funds to the extent that such amounts are not directly attributable to a specific fund. Revolving fund income is allocated on the basis of each program's average cash available for investment during the year while the expenses are allocated on the basis of each program's present value of future benefits. Revolving fund assets and liabilities are allocated on the basis of the yearend equity of each program's revolving funds. The plan assets acquired by PBGC and commingled at PBGC's custodian bank are credited directly to the appropriate fund while the earnings and expenses on the commingled assets are allocated to each program's trust funds on the basis of each trust fund's value, relative to the total value of the commingled fund.

**Valuation Method:** Consistent with generally accepted accounting principles outlined in Statements of Financial Accounting Standards Nos. 35, 60, and 87, PBGC reports its assets and liabilities at fair value. A primary objective of PBGC's financial statements is to provide financial information that is useful in assessing PBGC's present and future ability to ensure that defined benefit beneficiaries receive benefits when due. PBGC believes that measuring its assets and liabilities at fair value provides the most relevant information to the reader.

**Cash and Cash Equivalents:** Cash includes cash on hand and demand deposits. Cash equivalents are securities with a maturity of one business day.

**Investment Valuation and Income:** Fair values are based on the last sale of a listed security, on the mean of the "bid-and-asked" for nonlisted securities, or on a valuation model in the case of fixed-income securities that are not actively traded. These valuations are determined as of the end of each fiscal year. Purchases and sales of securities are recorded on the trade date. Investment income is accrued as earned. Dividend income is recorded on the ex-dividend date. Realized gains and losses on sales of investments are calculated using an average cost basis. Any increase or decrease in the market value of a plan's assets occurring after the date on which the plan is terminated must, by law, be credited to or suffered by PBGC (see Notes 3, 6, and 14).

**Sponsors of Terminated Plans, Receivables:** The amounts due from sponsors of terminated plans or members of their controlled group represent the settled claims for employer liability (underfunding as of date of plan termination) and for contributions due their plan less an allowance for uncollectible amounts. Any amounts expected to be received beyond one year are discounted for time and risk factors. Some agreements between PBGC and plan sponsors provide for contingent payments based on future profits of the sponsors. Any such future amounts realized will be reported in the period in which they accrue or are received.

**Premiums:** Premiums receivable represent the earned but unpaid portion of the premiums for plans that have a plan year commencing before the end of PBGC's fiscal year and past due premiums deemed collectible, including collectible penalties and interest. Unearned premiums represent an estimate of payments received during the fiscal year that cover the portion of a plan's year after the Corporation's fiscal yearend. Premium income represents revenue generated from self-assessments received from defined benefit pension plans as required by Title IV of ERISA.

**Present Value of Future Benefits (PVFB):** The PVFB is the estimated liability for future pension benefits that PBGC is or will be obligated to pay with respect to trusteed plans and terminated plans pending trusteeship. This liability is stated as the actuarial present value of estimated future benefits less the present value of estimated recoveries from sponsors and members of their controlled group and the assets of terminated plans pending trusteeship. The estimated liabilities attributable to probable future plan terminations are also included in the PVFB as a separate line item (net of estimated recoveries and assets). To measure the actuarial present value, PBGC used assumptions to adjust the value of those future payments to reflect the time value of money (by discounting) and the probability of payment (by means of decrements, such as for death or retirement). PBGC also included anticipated expenses to settle the benefit obligation in the determination of the PVFB.

(1) Trusteed Plans – represents the present value of future payments of benefits less the present value of expected recoveries, for which an agreement has not been reached, from sponsors, and members of their controlled group, of plans that have terminated and been trusteed by PBGC prior to fiscal yearend.

(2) Terminated Plans Pending Trusteeship – represents the present value of future payments of benefits less the plans' net assets at fair value anticipated to be received and the present value of expected recoveries, for which a settlement agreement has not been reached, from sponsors, and members of their controlled group, of plans that have terminated but have not been trusteed by PBGC prior to fiscal yearend.

(3) Net Claims for Probable Terminations – includes reasonable estimates of the losses, net of plan assets and the present value of expected recoveries from sponsors and members of their controlled group, for plans that are likely to terminate in a future year. These estimated losses are based on conditions that existed as of PBGC's fiscal yearend. It is likely that one or more events subsequent to PBGC's fiscal yearend will occur, confirming the fact of the loss.

Benefit payments to participants of pension plans trusteed by PBGC, or that are terminated and pending trusteeship, represent a reduction to the PVFB (see Note 6).

**Present Value of Nonrecoverable Future Financial Assistance:** In accordance with Title IV of ERISA, PBGC provides financial assistance to multiemployer plans, in the form of loans, to enable the plans to pay guaranteed benefits to participants and reasonable administrative expenses. These loans, in exchange for interest-bearing promissory notes, constitute an obligation of each plan.

The present value of nonrecoverable future financial assistance represents the estimated nonrecoverable payments to be provided by PBGC in the future to multiemployer plans that will not be able to meet their future benefit obligations. The present value of nonrecoverable future financial assistance is based on the difference between the present value of future guaranteed benefits and expenses and the market value of plan assets, including the present value of future amounts expected to be paid by employers, for those plans that are expected to require future assistance. The amount reflects the rates at which, in the opinion of management, these liabilities (net of expenses) could be settled in the market for single-premium nonparticipating group annuities issued by private insurers (see Note 7).

**Other Expenses:** These expenses represent a current period estimate of the net amount of receivables deemed to be uncollectible. The estimate is based on the most recent status of the debtor (e.g., sponsor), the age of the receivables, and other factors that indicate the element of uncollectibility in the receivables outstanding.

**Losses from Completed and Probable Terminations:** Amounts reported as losses from completed and probable terminations in the Statements of Operations and Changes in Net Position represent the difference as of the date of plan termination between the present value of future benefits (including amounts owed under Section 4022(c) of ERISA) assumed, or expected to be assumed, by PBGC, less related plan assets and the present value of expected recoveries from sponsors and members of their controlled group (see Note 13). In addition, the plans'net income from date of plan termination to the beginning of the fiscal year is included as a component of losses from completed and probable terminations for plans with termination dates prior to the year in which they were added to PBGC's inventory of terminated plans.

**Actuarial Adjustments and Charges:** Actuarial adjustments related to changes in method and the effect of experience are classified as underwriting activity. Actuarial charges related to changes in interest rates and passage of time are classified as financial activity. These adjustments and charges represent the change in the PVFB that results from applying actuarial assumptions in the calculation of future benefit liabilities (see Note 6).

**Depreciation:** Depreciation of PBGC's furniture and equipment is calculated on a straight-line basis over the estimated useful lives of the assets. The useful lives range from 5 to 10 years. Routine maintenance and leasehold improvements (the amounts of which are not material) are charged to operations as incurred.

## Note 3 – Investments

Premium receipts are invested in securities issued by the U.S. Government.

The trust funds include assets PBGC acquires or expects to acquire with respect to terminated plans and investment income thereon. These assets generally are held by custodian banks.

The basis and market value of the investments by type are detailed below. The basis indicated is cost of the asset if acquired after the date of plan termination or the market value at date of plan termination if the asset was acquired as a result of a plan's termination. Realized and unrealized gains and losses, in addition to interest and dividends earned on these investments, are disclosed in Note 14.

INVESTMENTS OF SINGLE-EMPLOYER REVOLVING FUNDS AND SINGLE-EMPLOYER TRUSTEED PLANS

*(Dollars in millions)*

| | **September30, 1996** | | September 30, 1995 | |
|---|---|---|---|---|
| | **Basis** | **Market Value** | Basis | Market Value |
| Fixed maturity securities: | | | | |
| U.S. Government securities | **$6,440** | **$ 6,462** | $5,555 | $6,143 |
| Commercial paper | **1** | **1** | 0 | 0 |
| Corporate bonds | **15** | **16** | 28 | 34 |
| Subtotal | **6,456** | **6,479** | 5,583 | 6,177 |
| Equity securities | **3,096** | **4,369** | 2,395 | 3,270 |
| Real estate | **57** | **53** | 64 | 62 |
| Other: | | | | |
| Insurance contracts | **37** | **36** | 70 | 41 |
| Mortgages | **1** | **1** | 1 | 1 |
| Foreign securities | **58** | **53** | 31 | 38 |
| Total | **$9,705** | **$10,991** | $8,144 | $9,589 |

INVESTMENTS OF MULTIEMPLOYER REVOLVING FUNDS AND MULTIEMPLOYER TRUSTEED PLANS

*(Dollars in millions)*

| | **September30, 1996** | | September 30, 1995 | |
|---|---|---|---|---|
| | **Basis** | **Market Value** | Basis | Market Value |
| Fixed maturity securities: | | | | |
| U.S. Government securities | **$469** | **$471** | $412 | $457 |
| Corporate bonds | **0** | **0** | 0 | 0 |
| Subtotal | **469** | **471** | 412 | 457 |
| Equity securities | **2** | **3** | 2 | 3 |
| Total | **$471** | **$474** | $414 | $460 |

## Note 4 – Receivables,Net: Sponsors of Restored Plans

In fiscal year 1995 the LTVCorporation re-purchased its own zero coupon bonds from PBGC. In exchange for the $724 million face value ($75 million book value) bonds, PBGC received $39 million in cash and a $48 million, 8½% interest-bearing note that matures on December 31, 2020. The current receivable from LTVincludes $2 million of interest owed that was added to the principal balance and accrued interest of approximately $1 million.

## Note 5 – Receivables,Net: Notes Receivable

During fiscal year 1993, PBGC received a series of 14 secured notes from Continental Airlines as part of the settlement for underfunding in certain terminated plans. These 3- to 15-year 12% secured notes total $202 million in principal (face value) and mature between 1996 and 2007. The net present values of the notes as of September 30, 1996 and 1995, were $86 million and $82 million, respectively.

## Note 6 – Present Value of Future Benefits

The following table summarizes the actuarial adjustments, charges, and credits that explain how the Corporation's single-employer program liability for the present value of future benefits changed for the years ended September 30, 1996 and 1995.

PBGC used a 25-year select interest rate of 6.6% followed by an ultimate rate of 4.75% for 1996 and a 20-year select interest rate of 6.5% followed by an ultimate rate of 5% for 1995. These rates were determined to be those needed to continue to match the survey of annuity prices provided by the American Council of Life Insurance. PBGC's regulations state that both the interest rate and the length of the select period may vary to produce the best fit with these prices. The prices reflect rates at which, in the opinion of management, the liabilities (net of expenses) could be settled in the market at September 30, for single-premium nonparticipating group annuities issued by private insurers. These rates are impacted by many factors including Federal Reserve policy.

In both years, PBGC used the 83GAM mortality table with margins, projected to 1993 by Scale H. PBGC has found that this table is generally consistent with its experience.

For 1996 the administrative expense assumption (for expenses associated with terminating plans) consisted of (1) an initial case processing cost of $26,000 per plan plus $650 per participant, both of which are phased out over four years following the date of trusteeship; and (2) a flat 3.25 percent of total benefit liability. For 1995 this assumption consisted of (1) an initial case processing cost of $10,800 per plan plus $270 per participant, both of which were phased out over four years following the date of trusteeship; and (2) a flat 1.35 percent of total benefit liability. The expense formula used to calculate the PVFB was modified for 1996 to more accurately reflect PBGC's claims-related expenses.

PBGC reached a settlement in a class-action suit during 1996 under which PBGC will pay an estimated $96 million in benefits and expenses. To date PBGC has paid $34 million, leaving an estimated balance of $62 million to be disbursed over the next three years.

The present values of future benefits for trusteed multi-employer plans for 1996 and 1995 reflect changes due to benefit payments, change in interest assumption, passage of time, and effect of experience.

The resulting liability represents PBGC's best estimate of the measure of anticipated experience under these programs.

## RECONCILIATION OF THE PRESENT VALUE OF FUTURE BENEFITS FOR THE YEARS ENDED SEPTEMBER 30, 1996 AND 1995

*(Dollars in millions)*

| | September 30, 1996 | | September 30, 1995 | |
|---|---|---|---|---|
| Present value of future benefits, at beginning of year – Single-Employer, net | | $10,388 | | $ 9,215 |
| Estimated recoveries | | 58 | | 74 |
| Assets of terminated plans pending trusteeship, net | | 212 | | 108 |
| Present value of future benefits at beginning of year, gross | | 10,658 | | 9,397 |
| Net claims for probable terminations, prior year | | (1,179) | | (1,166) |
| Actuarial adjustments – underwriting: | | | | |
| Changes in method and assumptions | $ (44) | | $ (54) | |
| Effect of experience | 195 | | (28) | |
| Total actuarial adjustments – underwriting | 151 | | (82) | |
| Actuarial charges (credits) – financial: | | | | |
| Passage of time | 615 | | 642 | |
| Change in interest rates | (134) | | 1,001 | |
| Total actuarial charges – financial | 481 | | 1,643 | |
| Total actuarial charges | | 632 | | 1,561 |
| Terminations: | | | | |
| Current year | 675 | | 463 | |
| Changes in prior year | (98) | | (15) | |
| Total terminations | | 577 | | 448 |
| Benefit payments* | | (790) | | (761) |
| Estimated recoveries | | (36) | | (58) |
| Assets of terminated plans pending trusteeship, net | | (119) | | (212) |
| Settlements and judgments | | 62 | | 0 |
| Net claims for probable terminations: | | | | |
| Future benefits** | 2,680 | | 2,800 | |
| Estimated plan assets and recoveries from sponsors | (1,725) | | (1,621) | |
| Total net claims, current year | | 955 | | 1,179 |
| Present value of future benefits, at end of year – Single-Employer, net | | 10,760 | | 10,388 |
| Present value of future benefits, at end of year – Multiemployer | | 9 | | 10 |
| Total present value of future benefits, at end of year, net | | $10,769 | | $10,398 |

* The benefit payments of $790 million and $761 million include $12 million in 1996 and $24 million in 1995 for benefits paid from plan assets by plans prior to trusteeship.

** The future benefits for probable terminations of $2,680 million and $2,800 million for fiscal years 1996 and 1995, respectively, include $118 million and $111 million, respectively, in net claims (future benefits less estimated plan assets and recoveries) for probable terminations not specifically identified.

## ASSETS OF SINGLE-EMPLOYER TERMINATED PLANS PENDING TRUSTEESHIP, NET

*(Dollars in millions)*

| | September30, 1996 | | September 30, 1995 | |
|---|---|---|---|---|
| | Basis | Market Value | Basis | Market Value |
| U.S. Government securities | $ 29 | $ 28 | $ 56 | $ 59 |
| Corporate bonds | 26 | 27 | 40 | 43 |
| Equity securities | 27 | 29 | 55 | 70 |
| Insurance contracts | 25 | 16 | 14 | 10 |
| Other | 0 | 0 | 14 | 15 |
| Cash and cash equivalents | 19 | 19 | 15 | 15 |
| Total, net | $126 | $119 | $194 | $212 |

**Net Claims for Probable Terminations:** Factors that are presently not fully determinable may be responsible for these claim estimates differing from actual experience.

Included in net claims for probable terminations is a provision for future benefit liabilities for plans not specifically identified.

The values recorded in the following reconciliation table have been adjusted to the expected dates of termination.

RECONCILIATION OF NET CLAIMS FOR PROBABLE TERMINATIONS

*(Dollars in millions)*

| | September 30, 1996 | | September 30, 1995 | |
|---|---|---|---|---|
| Net claims for probable terminations, at beginning of year | | **$1,179** | | $1,166 |
| New claims | **$ 144** | | $ 121 | |
| Actual terminations | **(113)** | | (116) | |
| Eliminated probables | **(73)** | | (11) | |
| Change in benefit liabilities | **(30)** | | 90 | |
| Change in plan assets | **(102)** | | (140) | |
| Change in expected recoveries | **(50)** | | 69 | |
| Loss on probables | | **(224)*** | | 13* |
| Net claims for probable terminations, at end of year | | **$ 955** | | $1,179 |

* See Note 13

## Note 7 – Multiemployer Financial Assistance

Financial assistance is granted to multiemployer defined benefit pension plans in the form of loans. An allowance is set up to the extent that repayment of these loans is not expected.

NOTES RECEIVABLE
MULTIEMPLOYER FINANCIAL ASSISTANCE

*(Dollars in millions)*

| | September 30, 1996 | September 30, 1995 |
|---|---|---|
| Gross balance at beginning of year | **$ 26** | $ 22 |
| Financial assistance payments – current year | **5** | 4 |
| Subtotal | **31** | 26 |
| Allowance for uncollectible amounts | **(31)** | (26) |
| Net balance at end of year | **$ 0** | $ 0 |

The losses from financial assistance reflected in the Statements of Operations and Changes in Net Position include annual changes in the estimated present value of nonrecoverable future financial assistance and assistance granted that was not previously accrued.

PRESENT VALUE OF NONRECOVERABLE FUTURE FINANCIAL ASSISTANCE AND LOSSES FROM FINANCIAL ASSISTANCE

*(Dollars in millions)*

| | September 30, 1996 | September 30, 1995 |
|---|---|---|
| Balance at beginning of year | **$268** | $164 |
| Changes in allowance: | | |
| Losses from financial assistance | **102** | 108 |
| Financial assistance granted (previously accrued) | **(5)** | (4) |
| Balance at end of year | **$365** | $268 |

## Note 8 – Accounts Payable and Accrued Expenses

The following table itemizes accounts payable and accrued expenses reported in the Statements of Financial Condition:

ACCOUNTS PAYABLE AND ACCRUED EXPENSES

*(Dollars in millions)*

| | September 30, 1996 | September 30, 1995 |
|---|---|---|
| Due for purchase of securities | **$ 91** | $ 37 |
| Annual leave | **3** | 3 |
| Other payables and accrued expenses | **24** | 61 |
| Accounts payable and accrued expenses | **$118** | $101 |

## Note 9 – Contingencies

There are a number of large single-employer plans that may terminate. In addition, there are some multiemployer plans that may require future financial assistance. The amounts disclosed below represent the Corporation's best estimates given the inherent uncertainties about these plans.

PBGC estimates that total unfunded vested benefits on termination of single-employer plans that represent reasonably possible exposure as of September 30, 1996, range from $22 billion to $26 billion. This exposure is primarily in the steel, airline, transportation equipment, and industrial and commercial machinery industries. The estimate has been calculated as in previous years by using data obtained from filings with the government and corporate annual reports for fiscal years ending in calendar 1995. The value reported for liabilities in the $22 billion estimate has been adjusted to the December 31, 1995, PBGC select interest rate of 5.3%. When available, data has been adjusted to a consistent set of mortality assumptions. Plans not insured by PBGC have been eliminated from the data. Since these figures are generally based on the reporting requirements in the Financial Accounting Standards Board's Statement of Financial Accounting Standard No. 87 ("Employers' Accounting for Pensions"), no provision has been made for the possible failure of the plan sponsor to make subsequent contributions or for plan liabilities that would be incurred after that date. The total underfunding in single-employer plans is estimated at $64 billion as of December 31, 1995.

PBGC has included amounts in the liability for the present value of nonrecoverable future financial assistance (see Note 7) for multiemployer plans that PBGC estimates may require future financial assistance. In addition, PBGC currently estimates that it is reasonably possible that other multiemployer plans may require future financial assistance in the amount of $243 million.

The future financial assistance liability for each multiemployer plan identified as probable or reasonably possible was calculated as the present value of guaranteed future benefit and expense payments as of the later of September 30, 1996, or the projected (or actual, if known) date of plan insolvency, discounted back to September 30, 1996, using interest only. The Corporation's identification of plans that are likely to require such assistance and estimation of related amounts require consideration of many complex factors. These factors are affected by future events, including actions by plans and their sponsors, most of which are beyond the Corporation's control.

A select and ultimate interest rate assumption of 6.6% for the first 25 years and 4.75% thereafter was used. The 83GAM mortality table with margins, projected to 1993 using Scale H, also was used.

## Note 10 – Commitments

PBGC leases its office facility under a commitment that began on December 11, 1993, and expires December 10, 2008. The lease provides for periodic rate increases based on increases in operating costs and real estate taxes over a base amount. In addition, PBGC is leasing space for field benefit administrators. These leases began in 1996 and expire in 2005. The minimum future lease payments for office facilities having noncancellable terms in excess of one year as of September 30, 1996, are as follows:

COMMITMENTS: FUTURE LEASE PAYMENTS

*(Dollars in millions)*

| Years Ending September 30, | Operating Leases |
|---|---|
| 1997 | $ 11.3 |
| 1998 | 11.6 |
| 1999 | 11.5 |
| 2000 | 11.8 |
| 2001 | 12.1 |
| Thereafter | 92.4 |
| Minimum lease payments | $150.7 |

Lease expenditures were $10.7 million in 1996 and $9.6 million in 1995.

## Note 11 – Premiums

For both the single-employer and multiemployer programs, ERISAprovides that PBGC shall continue to guarantee basic benefits despite the failure of a plan administrator to pay premiums when due. PBGC assesses interest and penalties up to 100 percent of the unpaid amount for late payment or underpayment (see Note 12). Annual premiums for the single-employer program are $19 per participant for a fully funded plan. Underfunded single-employer plans pay an additional variable-rate charge, previously capped at $53 per participant, based on funding levels. The Retirement Protection Act, signed into law on December 8, 1994, phases out the cap on the variable-rate charge for most plans over three plan years, effective for plan years commencing on or after July 1, 1994. The multiemployer premium is $2.60 per participant.

## Note 12 – Underwriting: Other Income

UNDERWRITING: OTHER INCOME

*(Dollars in millions)*

| | For the Years Ended September 30, 1996 | 1995 |
|---|---|---|
| Interest income-premiums | **$ 1** | $ 2 |
| Penalty income-premiums | **15** | 3 |
| Interest income-employer liability | **4** | 5 |
| Interest income-due and unpaid contributions | **2** | 3 |
| Other | **5** | 5 |
| Total | **$27** | $18 |

## Note 13 – Losses from Completed and Probable Terminations

Amounts reported as losses are the present value of future benefits (including amounts owed under Section 4022(c)) less related plan assets and the present value of expected recoveries from sponsors. The following table details the components that make up the losses:

LOSSES FROM COMPLETED AND PROBABLE TERMINATIONS – SINGLE-EMPLOYER PROGRAM

*(Dollars in millions)*

| | For the Years Ended September 30, **1996** | | | 1995 | | |
|---|---|---|---|---|---|---|
| | **New Terminations** | **Changes in Prior Year Terminations** | **Total** | New Terminations | Changes in Prior Year Terminations | Total |
| Present value of future benefits | **$675** | **$ (98)** | **$ 577** | $463 | $(15) | $448 |
| Less plan assets | **340** | **13** | **353** | 275 | 36 | 311 |
| Plan asset insufficiency | **335** | **(111)** | **224** | 188 | (51) | 137 |
| Less estimated recoveries | **3** | **(25)** | **(22)** | 7 | (26) | (19) |
| Subtotal | **$332** | **$ (86)** | **246** | $181 | $(25) | 156 |
| Settlements and judgments | | | **96** | | | 0 |
| Probables | | | **(224)*** | | | 13* |
| Total | | | **$ 118** | | | $169 |

* See Note 6

## Note 14 – Financial Income

FINANCIAL INCOME
*(Dollars in millions)*

| | For the Years Ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | **1996** | | | 1995 | | |
| | **Terminated Plans Pending Trusteeship** | **Revolving Funds and Trusteed Plans** | **Total** | Terminated Plans Pending Trusteeship | Revolving Funds and Trusteed Plans | Total |
| Fixed-income securities: | | | | | | |
| Interest earned | **$ 3** | **$ 513** | **$ 516** | $ 7 | $ 460 | $ 467 |
| Realized gain (loss) | **0** | **306** | **306** | 0 | (13) | (13) |
| Unrealized gain (loss) | **0** | **(620)** | **(620)** | 7 | 808 | 815 |
| Total fixed-income securities | **3** | **199** | **202** | 14 | 1,255 | 1,269 |
| Equity securities: | | | | | | |
| Dividends earned | **0** | **57** | **57** | 1 | 52 | 53 |
| Realized gain | **0** | **261** | **261** | 2 | 134 | 136 |
| Unrealized gain | **0** | **377** | **377** | 14 | 577 | 591 |
| Total equity securities | **0** | **695** | **695** | 17 | 763 | 780 |
| Other income (loss) | **(5)** | **35** | **30** | (3) | (7) | (10) |
| Total financial income (loss) | **$(2)** | **$ 929** | **$ 927** | $28 | $2,011 | $2,039 |

## Note 15 – Employee Benefit Plans

All permanent full-time and part-time PBGC employees are covered by the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Full-time and part-time employees with less than five years service under CSRS and hired after December 31, 1983, are automatically covered by both Social Security and FERS. Employees hired before January 1, 1984, participate in CSRS unless they elected to transfer to FERS by June 30, 1988.

The Corporation's contribution to the CSRS plan equals the 7 percent of base pay contributed by employees covered by that system. For those employees covered by FERS, the Corporation's contribution was 12.2 percent of base pay for both 1996 and 1995. In addition, for FERS-covered employees, PBGC automatically contributes 1 percent of base pay to the employee's Thrift Savings account, matches the first 3 percent contributed by the employee, and matches one-half of the next 2 percent contributed by the employee. Total retirement plan expenses amounted to $6 million in 1996 and $5 million in 1995.

These financial statements do not reflect CSRS or FERS assets, accumulated plan benefits, or any unfunded plan liabilities applicable to PBGC employees. These amounts are reported by the U.S. Office of Personnel Management (OPM) and are not allocated to the individual employers. OPM accounts for federal health and life insurance programs for those retired PBGC eligible employees who had selected federal government-sponsored plans. PBGC does not offer other supplemental health and life insurance benefits to its employees.

## Note 16 – Cash Flows

The following is a reconciliation between the net income (loss) as reported in the Statements of Operations and Changes in Net Position and net cash provided by operating activities as reported in the Statements of Cash Flows.

### RECONCILIATION OF NET INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES

*(Dollars in millions)*

| | Single-Employer Program | | Multiemployer Program | | Memorandum Total | |
|---|---|---|---|---|---|---|
| | September 30, | | September 30, | | September 30, | |
| | **1996** | 1995 | **1996** | 1995 | **1996** | 1995 |
| Net income (loss) | **$1,184** | $ 925 | **$(68)** | $ (5) | **$1,116** | $ 920 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | | | | | |
| Net (appreciation) decline in fair value of investments | **(379)** | (1,395) | **21** | (53) | **(358)** | (1,448) |
| Net (income) loss of terminated plans pending trusteeship | **3** | (30) | **0** | 0 | **3** | (30) |
| Loss on completed and probable terminations | **118** | 169 | **0** | 0 | **118** | 169 |
| Actuarial charges | **632** | 1,561 | **1** | 2 | **633** | 1,563 |
| Benefit payments-trusteed plans | **(778)** | (737) | **(2)** | (2) | **(780)** | (739) |
| Cash received from plans upon trusteeship | **47** | 42 | **0** | 0 | **47** | 42 |
| Changes in assets and liabilities, net of effects of trusteed and pending plans: | | | | | | |
| (Increase) decrease in receivables | **(41)** | 142 | **(3)** | (1) | **(44)** | 141 |
| Increase in present value of nonrecoverable future financial assistance | | | **97** | 104 | **97** | 104 |
| Increase (decrease) in unearned premiums | **99** | (32) | **0** | 0 | **99** | (32) |
| Increase (decrease) in accounts payable | **(37)** | 9 | **0** | 0 | **(37)** | 9 |
| Net cash provided by operating activities | **$ 848** | $ 654 | **$ 46** | $ 45 | **$ 894** | $ 699 |

## Note 17 – Litigation

PBGC records as a liability on its financial statements an estimated cost for unresolved litigation to the extent that losses in such cases are probable and estimable in amount. PBGC estimates that the resolution of other litigation matters will not have a material adverse effect on PBGC's financial position.

# Actuarial Valuation

PBGC calculated and validated the present value of future PBGC-payable benefits (PVFB) for both the single-employer and multiemployer programs and of nonrecoverable future financial assistance under the multiemployer program. Methods and procedures for both single-employer and multiemployer plans are generally the same as those used in 1995. The 1996 valuation included the newly implemented Missing Participants Program and improvements in the method for determining the portion of PBGC's recoveries that is shared with plan participants.

PRESENT VALUE OF FUTURE BENEFITS AND NONRECOVERABLE FUTURE FINANCIAL ASSISTANCE – 1996

*(Dollars in millions)*

| | Number of Plans | Number of Participants (000) | Liability |
|---|---|---|---|
| I. Single-Employer Program | | | |
| A. Terminated plans | | | |
| 1. Seriatim at fiscal yearend (FYE) | 1,469 | 133 | $ 3,378 |
| 2. Seriatim at DOPT, adjusted to FYE | 117 | 32 | 1,055 |
| 3. Hybrid plans | 4 | | |
| a. Benefits valued seriatim | | 5 | 329 |
| b. Benefits valued nonseriatim | | 15 | 529 |
| 4. Nonseriatim[1] | 748 | 201 | 4,665 |
| 5. Rettig settlement[2] (nonseriatim) | – | 1 | 2 |
| 6. Missing Participants Program[3] | – | 1 | 2 |
| Subtotal | 2,338 | 388 | 9,960 |
| B. Probable terminations (nonseriatim)[4] | 27 | 105 | 2,680 |
| Total [5] | 2,365 | 493 | $12,640 |
| II. Multiemployer Program | | | |
| A. Pre-MPPAAterminations (seriatim) | 10 | 1 | $ 9 |
| B. Post-MPPAAliability (net of plan assets) | 41 | 52 | 365 |
| Total | 51 | 53 | $ 374 |

Notes:

1) The liability for terminated plans has been increased by $31 million for terminated plans not yet reported and by $62 million for the Collins settlement.

2) The Rettig settlement refers to the extra benefit liability that PBGC incurred due to a settlement of a class action lawsuit that increased benefits for some participants and provided new benefits to others.

3) The Missing Participants Program refers to a liability that PBGC has assumed for unlocatable participants in standard plan terminations.

4) The net claims for probable plans reported in the financial statements include $118 million for not-yet-identified probable terminations. The assets for the probable plans, including the expected value of recoveries on employer liability and due-and-unpaid employer contributions claims, are $1,725 million. Thus, the net claims for probables as reported in the financial statements are $2,680 million less $1,725 million, or $955 million.

5) The PVFB in the financial statements ($10,760 million) is net of estimated plan assets and recoveries on probables ($1,725 million), estimated recoveries on terminated plans ($36 million), and estimated assets for plans pending trusteeship ($119 million), or, $12,640 million less $1,725 million less $36 million less $119 million = $10,760 million.

## Single-Employer Program

PBGC calculated the single-employer program's liability for benefits in the terminated plans and probable terminations, as defined in Note 2 to the financial statements, using a combination of three methods: seriatim, nonseriatim, and hybrid. For 1,469 plans, representing about 63 percent of the total number of single-employer terminated plans (34 percent of the total participants in single-employer terminated plans), PBGC had sufficiently accurate data to calculate the liability separately for each participant's benefit – the seriatim method. This is an increase of 47 plans over the 1,422 plans valued seriatim last year. For 117 plans whose data were not yet fully automated, PBGC calculated the benefits and liability seriatim as of the date of plan termination (DOPT) and brought the total amounts forward to the end of fiscal year 1996.

For 748 other plans, PBGC did not have sufficiently accurate or complete data to value individual benefits. Instead, the Corporation used a "nonseriatim" method that brings the liabilities from the plan's most recent actuarial valuation forward to the end of fiscal year 1996 using certain assumptions and adjustment factors.

For four specific plans, PBGC had sufficient data to calculate the liability for certain retirees using the seriatim method and the liability for the remaining participants using the nonseriatim method – a hybrid of the two methods that enhanced the overall accuracy of the valuation. The plan valuations for four other plans valued as hybrids in fiscal year 1995 were completed this year. These plans were therefore included in either the seriatim or the seriatim-at-DOPT category for the fiscal year 1996 valuation.

For the actuarial valuation, PBGC used a select and ultimate interest rate assumption of 6.6% for the first 25 years after the valuation date and 4.75% thereafter. The mortality assumptions used for the valuation are the same as for the 1995 valuation: (1) for healthy lives – the 1983 Group Annuity Table (83GAM) with margins projected to 1993 using Scale H, with a 6-year age setback for females; (2) for disabled lives not receiving Social Security benefits – the healthy lives tables set forward 3 years; and (3) for disabled lives receiving Social Security benefits – the Social Security disability table as described in subpart B of the PBGC regulation on Allocation of Assets in Single-Employer Plans for persons up to age 65, adjusted to parallel healthy mortality for ages above 65. PBGC assumed an explicit loading for expenses, in all terminated plans and single-employer probable terminations, equal to:

(a) $26,000 per plan, plus
(b) $650 per participant, plus
(c) 3.25% of benefit liability.

The expense elements (a) and (b) are phased out over the first four years from the plan's date of PBGC trusteeship. This expense formula represented a change from the prior year to reflect more accurately PBGC's actual level of claims-related expenses.

For non-pay-status participants, PBGC used expected retirement ages, as explained in subpart B of the Allocation of Assets in Single-Employer Plans regulation. PBGC assumed that participants who had attained their expected retirement age were in pay status. In seriatim plans, for participants who were older than their plan's normal retirement age, were not in pay status, and were unlocatable at September 30, 1996, PBGC reduced the value of their future benefits to zero over the three years succeeding normal retirement age to reflect the lower likelihood of payment.

## Multiemployer Program

PBGC calculated the liability for the 10 pre-MPPA terminations using the same assumptions and methods applied to the single-employer program.

PBGC based its valuation of the post-MPPA liability for nonrecoverable future financial assistance on the most recent available actuarial reports, Form 5500 Schedule B's, and information provided by representatives of the affected plans. The Corporation expected 41 plans to need financial assistance because severe industrial declines have left them with inadequate contribution bases and they have either run out of assets or are expected to run out of assets in the foreseeable future.

## Statement of Actuarial Opinion

This valuation has been prepared in accordance with generally accepted actuarial principles and practices and, to the best of my knowledge, fairly reflects the actuarial present value of the Corporation's liabilities for the single-employer and multiemployer plan insurance programs as of September 30, 1996.

In preparing this valuation, I have relied upon information provided to me regarding plan provisions, plan participants, plan assets, and other matters, some of which are detailed in a complete Actuarial Report available from PBGC.

In my opinion, (1) the techniques and methodology used for valuing these liabilities are generally acceptable within the actuarial profession; (2) the assumptions used are appropriate for the purposes of this statement and are individually my best estimate of expected future experience discounted using current settlement rates from insurance companies; and (3) the resulting total liability represents my best estimate of anticipated experience under these programs.

Joan M. Weiss

Joan M. Weiss, FSA, EA
*Chief Valuation Actuary, PBGC*
*Member, American Academy of Actuaries*

A complete actuarial valuation report, including additional actuarial data tables, is available from PBGC upon request.

Pension Benefit Guaranty Corporation
PBGC U.S. GOVERNMENT AGENCY
1200 K Street, N.W., Washington, D.C. 20005-4026

Office of Inspector General

To the Board of Directors
Pension Benefit Guaranty Corporation

Under the direction of the Office of Inspector General, Price Waterhouse LLP(Price Waterhouse) conducted an audit and expressed an unqualified opinion on the Fiscal Years 1996 and 1995 financial statements of the Pension Benefit Guaranty Corporation (PBGC).

The Chief Financial Officers (CFO) Act of 1990 (P.L. 101-576) requires PBGC's Office of Inspector General or an independent external auditor, as determined by the Inspector General, to audit the Agency's financial statements in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States.

Our responsibility under the CFO Act was fulfilled by evaluating the quality of the audit work performed in accordance with *Government Auditing Standards*. Specifically, we:

- reviewed Price Waterhouse's approach and planning of the audit;
- evaluated the qualifications and independence of its auditors;
- monitored the progress of the audit at key points;
- examined its working papers and reports to evaluate compliance with *Government Auditing Standards*; and
- performed other procedures we deemed necessary.

Based on our quality review, we determined that Price Waterhouse planned, executed, and reported the results of its audit of PBGC's Fiscal Years 1996 and 1995 financial statements in accordance with *Government Auditing Standards.* Therefore, in our opinion, Price Waterhouse's audit work provided a reasonable and reliable basis on which to render its January 10, 1997 opinion, and we concur with its report.

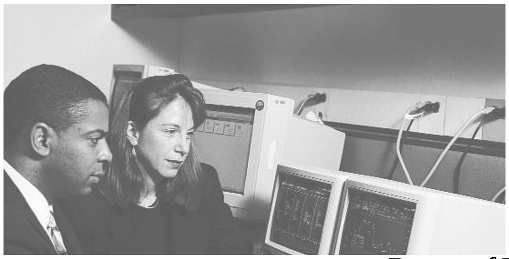
On the same date, Price Waterhouse also issued two reports — an unqualified opinion on PBGC management's assertion about the effectiveness of its internal control structure and a report on PBGC's compliance with laws and regulations. A complete set of Price Waterhouse's reports (97-4/23110-2) are available upon request from the PBGC's Office of Inspector General.

Sincerely,

Wayne Robert Poll

Wayne Robert Poll
Inspector General

February 18, 1997



**Report of Independent Accountants**

To the Inspector General
Pension Benefit Guaranty Corporation

We have audited the accompanying statements of financial condition as of September 30, 1996 and 1995, of the Single-Employer and Multiemployer Funds administered by the Pension Benefit Guaranty Corporation (PBGC or the Corporation) and the related statements of operations and changes in net position and statements of cash flows for the years then ended. These financial statements are the responsibility of PBGC's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Single-Employer and Multiemployer Funds administered by PBGC at September 30, 1996 and 1995, and the results of their operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

By law, PBGC's Single-Employer Fund (the Fund) must be self-sustaining and as such, its premiums must be sufficient to cover both its short and long-term obligations. The Fund is able to meet its short-term benefit obligations, and internal analyses indicate that the combined effect of future premium revenue and reduced underfunding of single-employer plans may allow the Fund to meet its future obligations as well. While the Fund’s Statement of Financial Condition reports a net position (assets in excess of liabilities) of $869 million at September 30, 1996, losses that are “reasonably possible” as a result of unfunded vested benefits are estimated to be in the range of $22 to $26 billion, as discussed in Note 9. To the extent contingent losses currently classified as “reasonably possible” become more likely, such as from deteriorating economic conditions or from insolvency of a large plan sponsor, the Fund’s net position could be depleted.

The overview of PBGC, the Actuarial Valuation, and other supplemental information contain a wide range of data, some of which are not directly related to the principal financial statements. We do not express an overall opinion on this information. However, we compared this information for consistency with the principal financial statements and discussed the methods of measurement and presentation with PBGC officials. Based on this limited work, we found no material inconsistencies with the principal financial statements.

In addition, in accordance with *Government Auditing Standards*, we have issued reports dated January 10, 1997 on PBGC management’s assertion about the effectiveness of its internal control structure and on its compliance with laws and regulations.

Price Waterhouse LLP

January 10, 1997
Washington, D.C.

97-3/23110-1

# Organization

## BOARD OF DIRECTORS

Cynthia A. Metzler, Chairman *
*Acting Secretary of Labor*

Robert E. Rubin
*Secretary of Treasury*

William M. Daley *
*Secretary of Commerce*

## EXECUTIVE MANAGEMENT

Martin Slate **
*Executive Director*

N. Anthony Calhoun
*Deputy Executive Director and Chief Financial Officer*

Joseph Grant
*Deputy Executive Director and Chief Operating Officer*

Ellen A. Hennessy
*Deputy Executive Director and Chief Negotiator*

John Seal **
*Deputy Executive Director and Chief Management Officer*

Judy Schub
*Assistant Executive Director for Legislative Affairs*

James J. Keightley
*General Counsel*

Judith Welles, *Director*
Communications and Public Affairs Department

*Robert Reich and Michael Kantor resigned as Secretaries of Labor and Commerce, respectively, after yearend.

**John Seal was named Acting Executive Director following the death of Martin Slate.

## CORPORATE DEPARTMENTS

Cristin M. Birch, *Director*
Information Resources Management Department

Sharon Barbee-Fletcher, *Director*
Human Resources Department

Bennie Hagans, *Director*
Insurance Operations Department

Robert Herting, *Director*
Procurement Department

Edward L. Knapp, *Director*
Financial Operations Department

Andrea E. Schneider, *Director*
Corporate Finance and Negotiations Department

Stuart A. Sirkin, *Director*
Corporate Policy and Research Department

Janet Smith, *Director*
Facilities and Services Department

Henry R. Thompson, *Director*
Budget Department

Harriet D. Verburg, *Director*
Participant and Employer Appeals Department

Dale Williams, *Director*
Contracts and Controls Review Department

Richard A. Ippolito
*Chief Economist*

Wayne Robert Poll *
*Inspector General*

* The Inspector General reports directly to the Chairman of the Board.

## THE PBGC ADVISORY COMMITTEE

*Appointed by the President of the United States*

### Representing the Interests of the General Public

Milton M. Irvin, *Chairman*
Managing Director
Salomon Brothers, Inc.
New York, New York

Joseph A. Perkins
Vice President
American Association of Retired Persons
Danvers, Massachusetts

Beverly Fisher White
Senior Governmental Analyst
Florida Office of Tourism, Trade, and Economic Development
Tallahassee, Florida

### Representing the Interests of Employers

M. Sharon Cassidy
General Counsel
United States Steel and Carnegie Pension Fund
Millwood, New York

One vacancy to be filled.

### Representing the Interests of Employee Organizations

Judith A. Scott
General Counsel
International Brotherhood of Teamsters
Washington, DC

Teresa Ghilarducci
AFL-CIO
South Bend, Indiana

# Financial Summary

*(Dollars in millions)*

| Single-Employer Fund | **1996** | 1995 | 1994 | 1993 | 1992 | 1991 | 1990 | 1989 | 1988 | 1987 |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Year Ended September 30, | | | | | |
| **Summary of Operations:** | | | | | | | | | | |
| Premium income | **$ 1,146** | 838 | 955 | 890 | 875 | 741 | 659 | 603 | 465 | 268 |
| Other income | **$ 26** | 18 | 42 | 38 | 118 | 45 | 5 | – | – | – |
| Investment income (losses) | **$ 915** | 1,956 | (380) | 1,538 | 614 | 860 | (109) | 387 | 5 | 261 |
| Actuarial charges (credits) | **$ 632** | 1,561 | (926) | 1,680 | 848 | 905 | 181 | 362 | 359 | 87 |
| Losses from completed and probable terminations | **$ 118** | 169 | (249) | 743 | 896 | 1,049 | 938 | 163 | 58 | (1,872) |
| Loss on contingent value rights | **$ 0** | 0 | 0 | 96 | | | | | | |
| Administrative and investment expenses | **$ 150** | 138 | 135 | 107 | 97 | 71 | 63 | 45 | 48 | 36 |
| Other expenses | **$ 3** | 19 | 0 | 0 | 0 | 212 | 162 | 0 | 0 | 0 |
| Net income (loss) | **$ 1,184** | 925 | 1,657 | (160) | (234) | (591) | (789) | 420 | 5 | 2,278 |
| **Summary of Financial Position:** | | | | | | | | | | |
| Cash and investments | **$11,665** | 10,026 | 7,857 | 7,866 | 5,897 | 4,562 | 2,408 | 2,356 | 1,817 | 1,728 |
| Total assets | **$12,043** | 10,371 | 8,281 | 8,267 | 6,381 | 5,422 | 2,797 | 3,059 | 2,422 | 2,163 |
| Present value of future benefits | **$10,760** | 10,388 | 9,215 | 10,693 | 8,790 | 7,594 | 4,476 | 3,984 | 3,806 | 3,629 |
| Net position | **$ 869** | (315) | (1,240) | (2,897) | (2,737) | (2,503) | (1,913) | (1,124) | (1,543) | (1,549) |
| **Insurance Activity:** | | | | | | | | | | |
| Benefits paid | **$ 790** | 761 | 719 | 720 | 634 | 514 | 369 | 353 | 357 | 300 |
| Participants receiving monthly benefits at end of year | **198,600** | 181,000 | 172,800 | 156,800 | 150,200 | 140,100 | 110,380 | 106,770 | 110,300 | 109,700 |
| Plans trusteed and pending trusteeship by PBGC | **2,338** | 2,084 | 1,961 | 1,848 | 1,760 | 1,644 | 1,558 | 1,501 | 1,455 | 1,376 |

*(Dollars in millions)*

| Multiemployer Fund | **1996** | 1995 | 1994 | 1993 | 1992 | 1991 | 1990 | 1989 | 1988 | 1987 |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Year Ended September 30, | | | | | |
| **Summary of Operations:** | | | | | | | | | | |
| Premium income | **$ 22** | 22 | 23 | 23 | 23 | 23 | 21 | 20 | 17 | 17 |
| Other income (losses) | **$ 1** | 0 | 0 | (1) | 1 | 1 | 1 | – | – | – |
| Investment income (losses) | **$ 12** | 83 | (46) | 107 | 27 | 38 | 13 | 16 | 7 | 3 |
| Actuarial charges (credits) | **$ 1** | 2 | (1) | 2 | (1) | 3 | 1 | 1 | 3 | 2 |
| Losses (gains) from financial assistance | **$102** | 108 | 57 | 20 | 46 | 21 | 23 | 1 | (6) | (9) |
| Administrative and investment expenses | **$ 0** | 0 | 0 | 0 | 0 | 0 | 2 | 3 | 3 | 3 |
| Net income (loss) | **$ (68)** | (5) | (79) | 107 | 6 | 38 | 9 | 31 | 24 | 24 |
| **Summary of Financial Position:** | | | | | | | | | | |
| Cash and investments | **$498** | 472 | 374 | 405 | 279 | 236 | 183 | 154 | 122 | 106 |
| Total assets | **$505** | 477 | 378 | 407 | 283 | 238 | 190 | 161 | 129 | 114 |
| Present value of future benefits | **$ 9** | 10 | 10 | 13 | 13 | 16 | 15 | 17 | 19 | 19 |
| Nonrecoverable future financial assistance, present value | **$365** | 268 | 164 | 110 | 94 | 52 | 33 | 11 | 11 | 19 |
| Net position | **$124** | 192 | 197 | 276 | 169 | 163 | 132 | 123 | 92 | 68 |
| **Insurance Activity:** | | | | | | | | | | |
| Benefits paid | **$ 2** | 2 | 2 | 2 | 2 | 2 | 2 | 3 | 3 | 3 |
| Participants receiving monthly benefits from PBGC at end of year | **1,100** | 1,300 | 1,400 | 1,590 | 1,760 | 1,990 | 2,170 | 2,310 | 2,500 | 2,800 |
| Plans receiving financial assistance from PBGC | **12** | 9 | 8 | 6 | 6 | 5 | 3 | 3 | 3 | 6 |

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