

Proposed IEEE-USA Position Statement
PENSION UNDERFUNDING and PBGC SOLVENCY PROBLEMS
March 2005

To: IEEE-USA Operating Committee

From: Ron Hira
Vice President, Career Activities

Subject: ENDORSEMENT OF A PROPOSED IEEE-USA POSITION
STATEMENT ON **Pension Under-funding and PBGC
Solvency Problems**

Originating Committee(s): Career & Workforce Policy Committee

Reviews/Endorsements: Most recent CWFPC Review, 08 Oct. 2004
IEEE-USA Editorial Review, 19 Oct. 2004

Intended Use: For use as appropriate with Congress and
the Administration.

Proposed Distribution: All as appropriate, including Congress and the
Administration.

Action Requested: Moved that the IEEE-USA OpCOM endorse for
Board approval the proposed IEEE-USA
position statement on "Pension Under-
funding and PBGC Solvency Problems."

Rationale: This position statement is needed to provide a
basis in policy for IEEE-USA communications on
funding problems that threaten the ability of the
nation's defined benefit pension system to pay
promised benefits, including recommended
actions that should be taken to reduce risks
confronting plan sponsors, plan participants, the
Pension Benefit Guaranty Corporation (PBGC),
and U.S. taxpayers.

Proposed IEEE-USA Position Statement

PENSION UNDERFUNDING AND PBGC SOLVENCY PROBLEMS

Many defined benefit (DB) pension plans that were fully funded five years ago are now seriously under-funded, due to a combination of lower investment returns and additional entitlements earned by vested plan participants. As a result, the Pension Benefit Guaranty Corporation (PBGC) faces increased exposure to depleted financial resources, should the agency have to assume the benefit obligations of under-funded plans.

Continuing increases in pension under-funding have serious implications for the PBGC, plan sponsors, plan participants and taxpayers:

- The PBGC faces a potentially staggering increase in its exposure to the risk of terminating under-funded defined benefit plans.
- Sponsors of financially sound plans face the prospect of having to pay higher premiums to the PBGC to cover the agency's losses.
- Plan participants are likely to lose some or all of their promised benefits, if their under-funded plans have to be terminated.
- Congress may have to call upon taxpayers to pay for a bailout, should the PBGC exhaust the financial resources the agency needs to meet its obligations to participants.

IEEE-USA recommends that the following actions be taken to alleviate pension under-funding and related PBGC solvency problems:

1. Establish graduated PBGC insurance premium requirements, so that fees paid by plan sponsors correspond with the level of risk posed by the funded status of their plans
2. Improve the PBGC's standing among corporate creditors in bankruptcy proceedings involving under-funded pension plans, by permitting the agency to effect liens in favor of such plans

3. Prohibit employers with under-funded pension plans from promising additional benefits that could ultimately become a PBGC obligation
4. Limit lump sum distributions from under-funded pension plans by withholding an amount equal to the percentage of plan under-funding, and granting recipients a claim for unpaid balances
5. Use market rates of return on plan investments to determine net present values for future un-funded plan liabilities
6. Raise the limit on allowable over-funding for privately sponsored defined benefit plans and ease the requirement for "topping off" the funds such plans need to meet their benefit obligations
7. Increase the penalty for withdrawing plan surpluses and using those funds for other corporate purposes
8. ~~Require~~ **Allow** vested plan participants to transfer earned benefits to **IRA's or other** defined contribution plans if they change or lose their jobs at any time prior to the earliest date for normal retirement. ~~This requirement will result in the removal of~~ **By removing** such benefits from the pension insurance pool backed by the PBGC, **this option will help** ~~and~~ reduce the risk of shortfalls in pension guaranty funding.
9. Assess the risks that "frozen" defined benefit plans pose to the retirement security of participants, and the viability of the retirement income protection program administered by the PBGC
10. Require plans to disclose the full extent of their funded status to plan participants, as well as to the PBGC.

This statement was developed by IEEE-USA's Career and Workforce Policy Committee and represents the considered judgment of a group of U.S. IEEE members with expertise in the subject field. IEEE-USA is an organizational unit of the IEEE, created in 1973 to advance the public good while promoting the careers and public policy interests of the more than 225,000 electrical, electronics, computer and software engineers who are U.S. members of IEEE. The IEEE is the world's largest technical

and professional society. For more information, go to:
<http://www.ieeeusa.org>.

Background

The Pension Benefit Guaranty Corporation (PBGC) was established in 1974 to protect plan participants when private defined benefit pension plans terminate with insufficient assets to meet their obligations. There is a statutory limit on the amount of a plan's benefit that the PBGC can guarantee. This limit is adjusted annually based on changes in the Social Security contribution and benefit base, and is permanently established for each pension plan on the date the plan terminates. For plans with a 2004 termination date, the maximum guaranteed benefit amount is \$44,386.32 yearly (\$3,698.86 monthly) for a single-life annuity at age 65.

<http://www.pbgc.gov/about/BENEFITS.htm>

In its most recent financial report, the PBGC reported a deficit of \$278.6 billion in pension funding for companies with more than \$50 million in un-funded liabilities -- up from \$18.4 billion in 1999. Although lump-sum payments may be more expensive for a plan than the comparable annuity, this minimum funding deficit does not take lump-sum payouts into account. The average funded ratio is less than 70 percent of total liabilities.

http://www.pbgc.gov/news/press_releases/2004/pr04_53.htm

In addition, the PBGC uses a "one size fits all" interest rate of 4.5% to make default liability calculations at a time when pension plans typically use an 8% to 9% interest rate. Current law also limits the ability of plan sponsors to contribute more to their plans when times are good by limiting contributions to 125% of current liabilities. This so-called "full funding limit" should be raised or removed entirely, provided there are safeguards to prevent pension funds from being used for purposes other than to pay plan benefits. Substantial penalties for withdrawal of plan surpluses should prevent such abuses.

Twenty percent of private sector workers are currently covered by a defined benefit plan. The PBGC guarantees benefits for 34 million workers and retirees in more than 31,000 private sector plans. Although the majority of defined benefit pension plans insured by the PBGC are adequately funded, a significant minority -- primarily in the airline and

steel industries -- are under-funded, and the level of under-funding in these plans is growing.

Even though the PBGC has sufficient assets to pay benefits well into the future, the agency's deficit has reached historically high levels and is still growing. In addition, current pension funding rules can have the perverse effect of delaying needed pension funding. As a result, employers may be called upon to make substantial "catch-up" funding contributions to their plans at times when they can least afford to do so.

The defined benefit system's insured participant base is also shifting from active workers to retirees. The percentage of active participants has fallen from 78 percent in 1980 to 53 percent in 2000. To make matters worse, half of all insured participants are in plans sponsored by companies in older, smokestack industries – the industries that are most adversely affected by global competition and by the shift from a manufacturing to a knowledge-based economy.

http://www.pbgc.gov/news/speeches/testimony_101403.pdf

And while data is published annually on defined benefit plan terminations, very little is currently known about the incidence of defined benefit plan freezes and the kinds of threats they may pose for PBGC solvency and the retirement security of plan participants .

<http://www.gao.gov/new.items/d04200r.pdf>

Because of these and other problems, the General Accountability Office (GAO) recently concluded that the long-term financial viability of the PBGC's defined benefit pension insurance program is in serious doubt and warrants immediate Congressional attention. The GAO's decision to add the PBGC to its high risk list of Federal agencies should spur the kinds of reforms needed to help protect the retirement benefits of the 34 million Americans who participate in the 30,000 defined benefit plans that make up America's voluntary private pension system.

<http://www.gao.gov/new.items/d031050sp.pdf>

###