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A Plan to Recalculate Pensions

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Corporations would find billions of dollars of pension shortfalls eliminated overnight under a proposal being prepared to address a longstanding issue in pension accounting.

The proposed legislation, being drafted by a Democrat and a Republican who sponsored changes in retirement laws in 2001, would create a permanent replacement for the 30-year bond in certain pension calculations. An interim measure, allowing companies to use a more favorable rate, is set to expire at the end of the year.

The proposal, embraced by the nation's biggest corporations, would use a rate that is tied to high-rated corporate bonds and that is higher than both the interim measure and the rate that companies have traditionally used to measure their pension obligations. The higher rate, known as the discount rate, makes obligations to retirees look smaller, at least on paper.

Because companies are required to keep their pensions funded at certain levels, smaller obligations will shrink their mandatory contributions, even though nothing else has changed.

America's companies, large and small, had a total pension shortfall of about \$300 billion at the end of 2002, according to the government agency that insures pensions. That was by far the largest total deficit in the history of that agency, the Pension Benefit [Guaranty Corporation](#), and it has aroused concerns about the health of the pension system. The worst deficits are found among a relatively small number of companies, in sectors like the auto and airline industries and deregulated public utilities.

Many big companies, most notably [General Motors](#), have said they must make billions of dollars of contributions to their plans in the next few years to comply with funding requirements. Company pension plans have weakened in the last three years as stocks and interest rates have plummeted.

Companies received some temporary accounting relief at the beginning of 2002, but will show an immediate weakening if that measure expires at the end of this year with no new rate.

Large companies have lobbied hard for relief. Actuaries say that for every percentage point rise in the rate, pension liabilities appear 10 to 15 percent smaller. The new proposal would raise the rate by about eight-tenths of a percentage point, based on the market environment at the end of last year. Under the old calculation pegged to the 30-year bond, companies would have used a rate of 5.84 percent, versus 6.67 percent under the interim measure. If the new proposal had been in place at the end of the year, the rate would have been 7.42 percent.

For General Motors, to use one very large example, the proposed rate would have reduced liabilities by about \$7 billion. G.M.'s level of pension funding would have been 91 percent instead of 75 percent. The funding level of a pension plan determines whether a company must make contributions. Other companies have smaller pension funds than G.M., but their liabilities would also look smaller.

Congressional aides said they expected the proposal to be included in a broader retirement savings package to be introduced today by Representative Rob Portman, Republican of Ohio, and Representative Benjamin L. Cardin, Democrat of Maryland. The two sponsored legislation two years ago that allowed workers to make larger contributions to their retirement savings plans and eliminated some pension rules.

Though companies have made forceful arguments for the proposed change in pension accounting, the change would not necessarily help all companies, or help employees, over the long run. For companies with severe pension deficits and weak finances over all, the change could cover up the weakness longer.

That may not matter if market conditions improve and pension funds recover by themselves. But if unfavorable conditions persist, the accounting change would conceal fatal illnesses at some pension funds, which would ultimately fail.

Pension plans are insured by the government, but only up to specific limits, as the pilots of US Airways recently discovered when their benefits were reduced.

In addition, when a pension fund is taken over by the government, the cost is borne by other companies that sponsor pension plans and pay insurance premiums. As the pension agency's deficit grows, so does the likelihood that it will raise its premiums, causing companies that have kept their pension funds robust to subsidize those that have failed to do so.

The pension agency has questioned the approach Congress is contemplating, saying it blurs together issues that should be kept separate: the nuts and bolts of pension accounting and the question of whether companies are setting aside enough. The suspension of the 30-year bond in 2001 caused a reassessment of pension accounting and has prompted some academics to call for a more thorough review of how pension values are measured.

"We must first find an accurate measure of pension liabilities," Steven A. Kandarian, the agency's executive director, told the Senate Finance Committee this month. "Once pension liabilities are accurately measured, appropriate funding rules can be addressed."