

Introduction and Overview of the Pension Plan Funding Reform Monograph

By Steven Siegel and C. Ian Genno

At the time this monograph was created, a series of recent *New York Times* editorials bemoaned the current state of pension funding and the ominous signs for the future. Starting with the airline industry, the editorials noted a growing conviction among analysts that even larger defaults are coming, potentially involving major automakers in the future. Further, the editorials urged Congress to act now to protect American workers' pensions—calling for meaningful reform guided by long-term, sustainable principles rather than shortsighted thinking. Concurrently, this same theme was also taken up by numerous other popular publications including *Time* and *Newsweek*. And the problem is not confined to the U.S.—the private sector pension system in Canada, the U.K. and other countries is similarly at risk. Clearly, this topic is on the public's mind—and is crying out for solutions.

How has the actuarial community responded to these challenges? Over the past year, the SOA Pension Section has been at the forefront of efforts to rethink how employer-sponsored pension plans are funded. This initiative began in the fall of 2004 with a Call for Papers, asking members of the consulting, plan sponsor and academic communities to develop proposals that innovatively address the future of pension plan funding—with the goal of creating a better system. The challenge was to present new thinking on pension plan funding, to develop principles applicable across national borders and to ensure a variety of perspectives would be presented. This monograph is a direct result of that Call for Papers.

The group of SOA volunteers that coordinated this initiative, led by Ian Genno and Tom Lowman, was delighted by the response from practitioners in the U.S., Canada and Japan, with over 20 abstracts submitted for consideration. In order to provide a forum to discuss the resulting papers and debate various proposals for reform, a symposium was organized for pension experts and stakeholders to meet face-to-face. The symposium, officially titled *The Future of Pension Plan Funding and Disclosure*, was held in Washington, D.C. on July 14-15, 2005.

Symposium Summary

For the benefit of those unable to attend, and readers of this monograph, the following is a high-level session-by-session synopsis of the symposium. All sessions were moderated by Ian Genno and Tom Lowman.

Session 1: Funding Reform: Introduction, and a Macro Perspective

This session set the stage for the symposium, addressing issues relating to the fundamental principles and objectives of pension funding. Serge Charbonneau presented the CIA's statement of principles for reporting on pension plan funding, and Michael Archer discussed the problems under the current U.S. funding rules, outlined a rational set of objectives for funding, and presented Towers Perrin's proposal for funding reform. Malcolm Hamilton provided a captivating commentary on the papers, highlighting what actuaries need to do in order to ensure a more rational approach to funding.

Session 2: Funding Lessons From Past Practice in the U.S., Canada and Around the World

Les Lohmann opened this session with his view on funding, asserting that it is a necessary element of the economic exchange between employers and employees, and the natural result of plan sponsors' need to manage liability. He further suggested that North Americans should recognize which elements of retirement plan design are universal versus those dictated by cultural expectations.

Eric Klieber presented his proposal for comprehensive defined benefit pension plan reform that included his thoughts about "model-neutral" funding rules that would allow the integration of financial economics into investments. The session concluded with Keith Ambachtsheer's commentary on the papers, which provided a comparison of the solutions proposed in these two papers with others, including Peter Drucker's and his own.

Session 3: The Role of Governments and Guarantee Organizations

This session focused on the role of governments and guarantee organizations. Although the emphasis was on the PBGC, the concepts debated in this session directly apply to similar guarantee programs currently in place in Ontario and the U.K.

Some of the most provocative debate at the symposium took place in this session. Larry Pollack offered compelling arguments for abolishing the PBGC altogether, a position that clearly was at odds with the views of many of the attendees. The other paper presented, co-authored by Nellie Liang and Julia Coronado, examined the effect of PGBC insurance on pension fund finances, concluding that the current structure of plan termination insurance has a significant influence on the financing choices of corporate DB pension sponsors. Dave Gustafson of the PBGC, who was unable to attend this portion of the symposium, provided a written commentary on the papers justifying the role of the PBGC and describing PBGC research that corroborated the conclusions of Liang and Coronado.

Session 4: Implications of Sponsor Bankruptcy

In this session, Ray Murphy presented a case study of the United Airlines pension plans, using publicly disclosed information, to illustrate how the current U.S. funding rules can obscure the true picture of a pension plan's financial health. To provide some perspective on what happens after a plan sponsor has failed, Nell Hennessey discussed how U.S. bankruptcy courts address a pension plan's funded status, and the challenges that stakeholders will face in trying to reform the bankruptcy rules relating to pension plans.

Session 5: Examining Stakeholder Perspectives

Session 5 provided some of the more colorful moments during the symposium with Michael Clark's presentation of his paper, *Dr. Phil's Guide to Pension Funding Reform*. Although Dr. Phil was unable to attend, Michael provided a proposal for reform that looked at a good parenting vs. bad parenting model for inspiration. As well, Alan Stonewall and Elizabeth Moore's presentation on improving pension funding by considering "WIFMs" — "what's in it for me" — charted an entertaining course through the various pension plan stakeholders' points of view. Don Segal provided thought-provoking commentary on each of the papers.

Session 6: Re-examining Funding Methods: Financial Economics Considerations

This session led off with Mark Ruloff presenting the paper he co-wrote with Howard Winklevoss and Steve Strake, demonstrating the effect of adopting

a stochastic funding method to manage contribution volatility, and that increased volatility is not necessarily the price to be paid to ensure plan solvency. The paper argued that the current state of pension underfunding is due in large part to the use of deterministic actuarial methods which have led to contribution holidays—not to the so-called “perfect storm” of poor equity returns at the start of this decade and low interest rates.

In the second paper presented in this session, Jeremy Gold described his proposal for transitioning into a fully funded and secure pension system through an exchange of bonds issued by the plan sponsor and the PBGC, allowing the capital markets to reflect the risk taken on by the PBGC in securing the plan’s funded status (during the transition period until full funding is achieved). Ed Burrows provided insightful commentary on both papers, including a comparison to principles underlying risk-based capital requirements set by insurance companies.

Session 7: Funding Reform—Future Directions

The closing session of the symposium began with a presentation by Eric Friedman on his proposal for a new set of minimum funding requirements to reduce contribution volatility and increase flexibility for plan sponsors. Ethan Kra and Don Fuerst presented the final paper of the symposium, with their vision for pension funding reform. The paper, which also represents Mercer’s position on pension reform, was guided by four principles: plan solvency, predictable contributions, objective rules and intuitive results. Gerry Mingione tied the discussion together, presenting his views on what works well in the various proposals and what doesn’t.

Luncheon Presentations

Two luncheon sessions were included as part of the symposium. Arnold Shapiro led the luncheon session on the first day, giving a wonderfully entertaining talk on the history of pension funding. The second day’s luncheon session focused on the perspectives of major stakeholders in the pension system. John Turner of AARP, David Blitzstein of the United Food and Commercial Workers, and Kent Mason of the law firm Davis & Harman shared their views on pension funding reform and the papers presented.

Throughout the symposium, attendees contributed significantly to the discussion, debating various viewpoints with the presenters and other attendees.

Feedback on the symposium was extremely positive—among the highest ratings for any SOA-sponsored event in recent years. In particular, attendees offered positive feedback on the immediate relevance of the presentations for plan sponsors, government policy makers and practicing actuaries.

Related Initiatives

Webcast

In October 2005, the Pension Section sponsored a two-hour webcast as a follow-up to the Washington symposium entitled, *The Future of Pension Funding and Disclosure Webcast: Envisioning a Better System*. The webcast, moderated by Emily Kessler of the SOA and led by Ian Genno and Tom Lowman, summarized the ideas presented and issues debated in Washington. The webcast also provided an opportunity for participants to vote on several related questions. The webcast was recorded; copies can be obtained by visiting <http://www.soa.org/ccm/content/research-publications/bookstore/cd-roms/>.

Addressing Reversionary Taxes

One of the themes that emerged at the symposium and in the webcast was the asymmetric funding risk imposed on plan sponsors by reversionary taxes on surplus withdrawals in the U.S., and limitations on the ownership and use of plan surplus in Canada. The Pension Section's Research Team has issued a request for research proposals to explore the impact of reversionary taxes in more depth.

The full request for proposals can be found at the following link: <http://www.soa.org/ccm/content/areas-of-practice/retirement-pension/research/reversion-taxes-quantifying-their-impact-on-pension-plan-funding/>

Conclusion

The symposium presenters, commentators and other authors deserve our thanks for their significant contribution to the success of this SOA initiative. Behind the scenes, thanks also go to the symposium organizing group, which included Michael Archer, David Kass, Emily Kessler, Sue Martz, Sandy

Neuenkirchen, Anne Seeck, Steve Siegel, Martine Sohier and Carol Zimmerman (in addition to Ian Genno as chair, and Tom Lowman as symposium co-moderator).

We encourage you to review the monograph and read papers of particular interest to you. You may not agree with everything you read in the monograph; the organizing group deliberately chose papers that would present different perspectives and spark debate. We invite you to join in the debate, through discussions with your colleagues, in upcoming professional meetings and in letters to the *Pension Section News*.

The Pension Section is committed to playing an integral role in the pension funding reform debate. We welcome your ideas and suggestions for helping us move forward with that goal. Please feel free to contact the symposium organizers, any Pension Section Council member or SOA staff with your thoughts for future initiatives.