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PBGC FINANCIAL WOES: STRUCTURAL CRISIS OR PASSING PROBLEM?

POLICY FORUM PROCEEDINGS

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P R O C E E D I N G S

[2:09 p.m.]

MR. ELLIOTT: Good afternoon. Thank you all for coming today. I'm Doug Elliott. I'm the president of the Center on Federal Financial Institutions or COFFI, as we call it. We're a nonprofit, nonpartisan, nonideological think tank that focuses on the role of the Federal Government in the lending and insurance areas.

A couple of administrative matters just to start off with. One is that if you hadn't RSVP'd, we'd appreciate it if you would sign in before you leave just so we have your name and email address. And also, you probably saw on the way in that we have a number of reports from COFFI out on the tables or, in some cases, just the front page of the longer report. On the longer reports, you can go to our Website, www.coffi.org, to get the full report.

I'd like to begin by thanking our distinguished panelists for agreeing to participate. They all have important jobs, and one of them even charges by the hour normally, so I'm very pleased to have them here. [To panelist] You did catch the normally part, didn't you?

I'd also like to thank the Subcommittee on Financial Management, the Budget and International Security of the Governmental Affairs Committee of the Senate. They've given us this nice room to use. Tara Baird, the subcommittee clerk, has been particularly helpful. And thanks to my board and to the volunteers who have been so helpful.

I believe the size of the audience today and the camera crew testifies to the depth of the financial problems that the Pension Benefit Guaranty Corporation faces today. In fact, I'm willing to bet that many of you would not have been here six months ago, before United became potentially the first domino in the pension dominos for the airline industry. So this has gained considerable topicality.

Before we jump into the details on PBGC, I would like to remind you that PBGC is just one of many important Federal financial institutions. The Federal Government has $1.4 trillion of lending out to homeowners, students, farmers, businesses, and on the insurance side, there's over $6 trillion of insured risk, including over $1 trillion of pension funds that are covered by Brad and the PBGC.

Federal financial institutions have a number of common characteristics, and some of them, unfortunately, can lead to trouble. In the case of the PBGC, they [the characteristics] have been part of the problem, but they do exist in other agencies as well. So in the interests of time, I'll just highlight three of them.

An underlying problem of some significance is insufficient attention; that is, the Federal Government is the world's largest financial institution. I sometimes describe it as a bank with an army. Yet, policy makers and the public do not pay attention until crises loom, and we know that that pattern is the surest recipe for developing those crises in the first place.

A second problem is the tendency for Congress to micromanage pricing and underwriting standards. In the case of PBGC, Congress sets the premium rates precisely and gives the PBGC no leeway in terms of the requirements they might put out for companies to qualify for the pension insurance.

The third I would point out is screwy accounting, which is true of a lot of the Federal financial agencies. Flawed Federal budget rules mean that PBGC, over its roughly 30-year life, has contributed $12 billion to deficit reduction, at the same time as it has, on a GAAP basis dug itself--I shouldn't say dug itself; it's not your fault; it's the structure, but at the same time as it has encountered a $23 billion cumulative deficit. There is a $35 billion difference between the purportedly positive results and the actual negative results.

Federal lending programs have quite sensible rules on the whole, but Federal insurance programs do not. I believe that serious action to help PBGC might have been taken earlier if the accounting in the Federal budget had reflected the economics more closely.

Moving to the PBGC, today's topic is "PBGC Financial Woes: Structural Crisis or Passing Problem?" The woes are self-evident. PBGC has lost an average of more than $10 billion a year over the last three years. Being in the Dirksen Building, I can't resist paraphrasing the late, great Senator Everett Dirksen: $10 billion here, $10 billion there, soon, you're talking real money.

PBGC's 2004 results, published on Monday, show that it has $23 billion less in assets than it owes in pension and other obligations. At the Center on Federal Financial Institutions, we've developed a fairly sophisticated financial model to model out, to project into the future, what the cash flows are for PBGC and consequently what the level of cash and investments will be at years in the future. We've got information on that model on the table outside and on our Website.

I'll just highlight a couple points: one is that our base case finds that there's a $78 billion hole to be filled assuming no reforms are put into place, and we devoutly hope that reforms will be put into place. Now, that number is in today's dollars. There's flexibility to wait for a number of years before infusing those funds. We don't foresee the PBGC running out of cash for perhaps 15 years.

But the longer we wait to make the reforms, the bigger the number is. Plus, there's simply the time value of money: the longer we wait, the more we have to put in, in dollars of that year, accounting for the lost investment income.

Now, that $78 billion number could balloon to $100 billion in today's dollars if the remaining major airlines terminate and other claims rise modestly. On the other end of the spectrum, even a shutdown, which is an unrealistically conservative option in terms of how bad the number would be, appears to us to cost about $30 billion. That's the $23 billion from the accounting statements at PBGC plus about $7 billion of expenses that, for accounting reasons, they're not able to bring into the present but would exist in the future. We're going to have an optional segment of this forum after the two panels for anyone who would like to stick around and look at more of the technical aspects of that model.

As I say, the woes are evident, and I believe strongly that they are structural, that there's an imbalance between the premiums and the risks that PBGC faces. For future claims, that mismatch could be changed either by changing the risk structure to bring down future claims or by raising premiums or both. I have to caution, however, that for the past problems which are locked in, we don't have the option. Somebody's going to pay for that. It's going to have to be filled with somebody's money.

I've asked the two panels to give their own views, which may contradict mine, and to expand on why we face the situation we do and what we should do about it. I've deliberately left the topic loose, because this is the first policy forum that anybody's done on this topic, at least to my knowledge, and I wanted these experts to be able to focus on what they thought was most important.

And expert is truly the right word here. I won't waste words persuading you that these people are influential and knowledgeable. That is self-evident. I will just introduce them by name and affiliation. You'll find their biographies on the table outside if you're curious as to their backgrounds.

Our first panel consists of Brad Belt, executive director of the PBGC; David Walker, the comptroller general of the United States and a former executive director of PBGC; Douglas Holtz-Eakin, who is director of the Congressional Budget Office; and Mark Iwry. It's in the opposite order, those last two. Mark Iwry is a nonresident senior fellow at Brookings and is the former benefits tax counsel at Treasury.

The second panel represents what I think of as the users of PBGC. Jim Klein is president of the American Benefits Council, who represents employers who sponsor benefit plans. Alan Reuther is the legislative director of the UAW, a union with a great stake in a healthy pension system. And finally, Karen Friedman is the policy director of the Pension Rights Center, which is an advocacy group for pension plan participants.

Again, thank you all for coming, and I'll start off with Brad,

How are things at PBGC?

[Laughter.]

MR. BELT: I think you can tell me that, Doug. You have all the numbers. How do you want to do this?

MR. ELLIOTT: My hope--

MR. BELT: We've got some very good panelists I'd like to hear from. I assume we all have initial remarks and--

MR. ELLIOTT: Exactly. I was hoping each of you would speak for a few minutes, and we'll do Q and A after we've been through the first panel.

MR. BELT: Okay; well, thank you, Doug, for allowing me to participate in this session and for shedding a little sunlight on this topic generally.

You know, if we do go out of business, I'm not sure what it means for COFFI. You've invested so much time and effort on this right now, you'd have to find somebody else to pick on.

MR. ELLIOTT: We'll rename ourselves TEA and do something else.

[Laughter.]

MR. BELT: But kudos to you. You've performed a very valuable public service by helping to educate policy makers, regulators and the markets generally about some of the issues attendant to PBGC.

I don't want to spend a lot of time offering my view of the world, as it were; maybe touch upon a couple of topics, and then, I look forward to a dialogue with my fellow panelists as well as taking some questions from the audience. I guess what I'll do is start briefly in the middle and then go back to the beginning and then to the tail end.

The middle is where are we now? We released our '04 financial results earlier this week. We disclosed that we now have a deficit of just a little over $23 billion. And as Doug noted, that's a substantial increase from prior years. It's about a $30 billion swing from positive to negative over the past three years or so.

In addition to the accumulated deficit, we also disclosed that we have significant exposure to companies that sponsor defined benefit plans who are credit risks, at least perceived as credit risks by the financial markets. They are junk bond-rated companies. And that exposure is about $100 billion. That is, companies that are rated junk bond status have sponsored pension plans which are underfunded to the tune of about $100 billion. In addition to that, we estimate the total underfunding in the defined benefit system is about $450 billion.

So the question that you posed was structural crisis or passing problem? Well, I think I can say unequivocally, it is not a passing problem. It is certainly a problem, but I don't see it passing any time soon. Is it a crisis? Well, I would use that term very guardedly. It's one that's often tossed around in this town.

I think that one thing that's important to emphasize is that, for example, in contrast to the savings and loan situation of 20-some years ago, we are not facing at the PBGC right now a liquidity crisis. The S&L situation was a liquidity crisis. That was a cash crunch. We have about $40 billion in assets that will enable us to pay out benefits for a number of years. Your modeling, your deterministic model, indicates that we would have cash available to pay monies out through the year 2020.

And of course, that's based on a particular set of assumptions. None of us know whether, in fact, any of those assumptions individually are going to be realized, let alone in aggregate. And if you do monte carlo simulations or stochastic modeling, you would show that there's a relatively low probability of running out of money within that kind of time frame.

But I don't want to suggest that the problem isn't a serious one at the same time. There is no question that we've got a deep hole. The hole is getting deeper, and if we don't make any changes in law, it will inevitably get deeper still. So we've got to stop digging, and then, we've got to be able to fill the hole in a measured way.

That's starting in the middle. Going back to the beginning, what got us to this point? And we could literally spend hours if not days talking about the wide variety of factors that have contributed to the challenges facing the defined benefit system as a whole and the more particular challenges facing the pension insurance program. There's a range of economic factors, financial factors, competitive pressures, et cetera.

I think the bottom line is that the pension insurance program is poorly designed. It was poorly designed from the beginning back in 1974, and the changes that have been made in the interim haven't fixed all those flaws; in some respects, they may have exacerbated them. We've got poor liability measures. We've got a lack of transparency. We've got a little bit too much flexibility in the system.

We can go on and on and on with respect to the design flaws within the system, but I think what demonstrates unequivocally that the pension funding rules and the pension insurance system doesn't work is we're here talking about this issue today. We've got a $23 billion deficit and a significant amount of underfunding in the system. The pension funding rules have not worked as they were intended to do.

There's a tremendous lack of transparency in the system. I mean, it's a study in obfuscation. Participants don't have relevant, timely information. Investors don't have relevant, timely information. Quite frankly, regulators don't have relevant, timely information. Our principal source of information, as you may all well know, and I don't want to get too far down in the weeds here, is the Form 5500, which for the '03 plan year started being filed with us just last month, and the data in that Form 5500 spoke to the beginning of the prior year.

So when it was filed, it's about 20 months old; we actually don't have access to that form, which is filed in paper form, for some months yet, so by the time the PBGC begins to look at that data and analyze and assess it, we're making business and policy decisions based upon information that is about two years old, maybe longer than that. It's obviously very difficult for anybody to make a reasonably informed business and policy decision based upon that kind of stale information in these kinds of dynamic markets.

The bigger question, of course, is where do we go from here? Comprehensive reform of the pension insurance program is critically important, and it needs to happen now. Even if we don't want to use the term crisis, and I'm not sure that is appropriate relative to so many other crises around the world, the longer we fiddle while Rome burns, the worse the problem is going to get.

It's incumbent upon us to move forward in a very constructive, balanced, considered fashion but do so fairly quickly when Congress reconvenes next year. The Administration is committed to doing that, and I'm heartened by some of the statements that have been coming out of key members of Congress over the past week once our numbers were released. Chairman Grassley, Chairman Gregg and others have all indicated their intention to move forward fairly aggressively in the next year to address these issues.

As I've outlined in statements that I've made and testimony that I've provided to the Hill, I think there are four key elements to a comprehensive reform package. One is fixing the funding rules. That is first and foremost: let's make sure that money actually gets into the plans. A couple of elements to that: one is to make sure that the funding rules are actually strengthened for companies that pose a risk of loss to the pension insurance program.

There are too many ways, whether it's because of poor liability measures like current liability or funding holidays, credit balances and those types of things that have precluded or effectively allowed companies to avoid putting in appropriate levels of funding into their pension plans.

You know, we've conveyed this data previously; it's out there in the public domain. In the case with Bethlehem Steel, they were sailing along. Most of the world thought for ERISA purposes that they were fully funded, 98, 99 percent funded. When the plan actually came to us, it turned out to be about 50 percent funded, billions of dollars in the hole. We have indicated the same thing publicly in court filings in the United Airlines matter.

For years and years, right up through 2002, 2003, for ERISA purposes, current liability purposes, they were sailing along or flying along at 97, 98, 99 percent funding, yet, if they actually present a claim to us, we estimate that the hole will be about $8.3 billion, and they're only about 50 percent funded. There's a fundamental disconnect; the rules aren't working.

We at the same time need to recognize that this is a voluntary system and that there are a very complex set of rules and regulations. I'm not sure that a one-size-fits-all approach is necessarily going to work. We want to make sure that we incent, encourage the companies that have been acting responsibly, that have been prudently funding their pension plans, to stay in the system.

I've got a parochial interest in that. To the extent that they exit the system, there goes my premium base, my revenue base. But obviously, that's a self interest, and from the broader societal perspective, I think it's critically important that we have this source of retirement income security in the defined benefit system. So we want to provide additional flexibility, simplify the rules and provide additional flexibility for those companies that are acting responsibly.

Secondly, we've got to rationalize the premium structure. It's clear that premiums currently are inadequate to cover expected losses, and they also do not appropriately reflect the risks posed to the pension insurance program. It's unusual to have an insurance system that doesn't compensate or price for risk.

You think about homeowners' insurance, you get a lower rate if you have smoke detectors. If you're talking about health insurance, you pay a higher rate if you're a smoker. You've got a poor driving record, you pay higher rates of auto insurance, et cetera, et cetera.

We don't have that embedded in this insurance system. It's not surprising that the system is rife with the moral hazard it is. It creates perverse incentives. We've got to better reflect the risks of loss that are posted to the pension insurance system.

Three, we've got to increase transparency. We've got to make sure that more-timely, relevant, meaningful information is made available to participants in pension plans, to investors in companies that sponsor pension plans and also to regulators.

Rather than laying on a new set of regulations, there can be some additional discipline, then, imposed by employees and by the markets to encourage companies to prudently fund their pension plans. It's simply not right, it's not fair that participants are left with the view going along that everything is all right with their pension plan as they were in the United Airlines situation, and then, they wake up one day; the company is in Chapter 11, and they find out they stand to lose almost $2 billion in benefits. They're entitled to have the relevant information, timely information about the funded status of the pension plan.

Finally, I think PBGC needs some better tools, and we've talked about, for example, changes in the bankruptcy context to be able to deal with these issues as they arise and when a company actually gets into financial difficulty. As you may know, when a company fails to meet its minimum required contributions under ERISA under Federal law, if they're outside bankruptcy under Section 412 of the Internal Revenue Code, a lien would automatically arise, and we could enforce that lien.

Unfortunately, in the bankruptcy context, the lien does arise, but the automatic stay provisions kick in. And so, as a consequence, there is no consequence to a company's failure to meet its Federally-required contributions to its pension plans, and that was the case in United Airlines and U.S. Airways.

So that's the basic framework for comprehensive reform. What I'd like to do is just close there, Doug, and then, listen to my colleagues and then open it up to a discussion and dialogue.

Thank you.

MR. WALKER: Thanks. Let me take about five minutes to give you an overview. I'm Dave Walker, head of GAO. In the interests of full and fair disclosure, I was at PBGC from October of '83 to August of '85. The numbers have gotten a lot bigger, and they've gotten a lot worse.

The fact of the matter is the PBGC is a microcosm of the Federal--

MR. BELT: Are you trying to point out the fact that in nine months on the job, I've lost $12 billion?

[Laughter.]

MR. WALKER: No, no, I've been gone since 1985, so that's a long time.

But the fact of the matter is the PBGC is a microcosm, arguably, of two things: one, the reversal of fortune for the Federal budget as a whole. It wasn't that long ago that we had significant surpluses. It wasn't that long ago that the PBGC had a $9.7 billion accumulated surplus. Now, it has a $23 billion plus accumulated deficit. That's all happened within a three-year period of time, and frankly, look at the Federal budget: it's gone in the tank in the last three years as well.

Secondly, the PBGC is also, in another way, a microcosm of Social Security. Social Security ran last year a $151 billion cash surplus. We spent every dime of that cash surplus on operating expenses. Last year's budget operating deficit was $568 billion, 4.9 percent of GDP. This is outrageous and unacceptable. So for budget purposes, we've got one thing, and yet, when you look at Social Security, we have a $3.7 trillion to $3.8 trillion unfunded obligation. It's not technically a liability under accounting at the present point in time. So PBGC is, in some ways, a microcosm of the Federal budget and of what's happening with Social Security.

Secondly, I think people have to recognize that this is really not about the PBGC; it's about retirement security. It's about economic security in retirement, because the PBGC is not the only one that's adversely affected when plans terminate; it's also the benefit security of workers and retirees. There are many people, especially in the airline industry, that take significant reductions in their pension benefits when their plans terminate, and it's not just the pilots.

There are a lot of people for example, and the airline industry is illustrative; there are others. There are a lot of people who take early retirement offers, subsidized early retirement benefits in order to rationalize the industry, downsize the industry, restructure because of various events, and they take big hits on their guaranteed benefits. So this is not just about PBGC; it's about retirement security or economic security in retirement.

Part of the problem with the PBGC is a short-term problem, and part of it is a structural problem. Clearly, over the last several years, we haven't had the best market returns until lately, but there was a significant reduction in asset values, and at the same point in time, there was a significant decline in prevailing interest rates, and therefore, there was a double whammy.

The asset values went down as compared to several years ago. The discounted present value amount that was necessary to buy off your liabilities went up. The combined effect was a double whammy on the bottom line. The red got redder and bigger. You know, frankly, there are similar issues in connection with the Federal budget, but that's a different topic.

So the fact of the matter is that yes, there are some short-term factors that may reverse over time; interest rates are only probably going to go one way over time. And the markets are getting a little bit better lately. But the fact of the matter is there are structural problems.

Brief comments on that: administratively, at least a couple of things that I think PBGC has to look at, and keep in mind GAO designated the single employer insurance program of the PBGC high risk I guess a couple years ago, so this is something we've seen on the horizon.

At least a couple of things from an administrative standpoint: clearly, there has to be more transparency associated with plans that clearly represent a risk to the PBGC. Now, the risk is not merely the unfunded obligations based on PBGC's valuation method, because there are some employers that are fairly sound employers, and so, merely because it's underfunded doesn't mean that it's a risk. But we need to have more transparency with regard to those plans that truly are risks.

Secondly, sometimes, the PBGC is just going to have to pull the plug. It's going to have to do an involuntary termination. That's not something that people like; that's not something you want to do if you can avoid it. But if you think you're in a situation where things are only going to get worse with the passage of time, then, sometimes, you have to do it. I did the first involuntary termination in PBGC's history, and I don't know if there have been any ones since then, but I did it and worked with the unions, worked with management, worked with others to get it done, and it worked okay, but it's not really something that you really want to do.

I do, however, believe that legislation is going to be necessary, crossing several different elements: number one, funding. On the one hand, you've got certain industries that are very cyclical in nature. And they need to have additional flexibility to be able to fund up in good times, because they're not going to be able to fund up in bad times, and there's more flexibility that can be provided there than current law does.

Secondly, clearly, there's going to need to be tougher standards for underfunded plans. And thirdly, to the extent that Congress decides to give relief from certain funding requirements, they need to be targeted to make sure that you're not giving relief to ones that represent a risk, because if all you're doing is exacerbating the problem or compounding the problem, that's not positive public policy.

I also think that there has to be a look at how do you define risk for variable rate premiums? Right now, PBGC theoretically has a risk rated premium. It's not a risk rate premium. It's a variable rated premium, but it's not a risk-related premium. If you really look at risk in a pension sense, to me, it's a combination of several things: the funding status of the plan, the financial strength of the sponsor, the plan design, because you can have certain features of the plan that can cause liabilities to arise overnight that could really expose you and the asset allocation of the plan, including whether and to what extent there are significant direct or indirect investments in employer securities, and I'll come back to that.

There clearly needs to be some additional insurance reforms. The phase-in guarantees; there are certain items that ought to be guaranteed, but the way the phase-ins work right now, there can be significant increases in liabilities overnight where there are little or no prefunding of those liabilities; for example, shutdown benefits in the steel industry. Clearly, something has to be done about that. Elimination of allowable offset provisions or Social Security offset provisions is another issue that I don't know if the PBGC has looked at but presents similar risks.

There are other issues such as lump sum benefits. There are a lot of plans that offer lump sums, and there have been rushes on the bank, and I think we have to look at whether and to what extent there ought to be a restriction or elimination of lump sums when plans are funded below a certain level. It ought to start with the executives and highly compensated and then get more restrictive depending on how poorly funded the plan is.

The first ones that ought to be cut off are the executives and the highly compensated, because they're the ones that are in a better position to understand what's going on.

There needs to be a look at further limiting benefit increases in the case of plans that are underfunded to a certain extent. With regard to floor/offset arrangements, I don't know how many are out there and how much exposure they still represent, where there is a relationship of a defined contribution plan to a defined benefit plan and de facto, there can be a circumvention of the 10 percent employer security limit. Enron had one, and guess who was the big firm that lobbied against eliminating floor/offset plans? Enron. We should learn a lesson from that.

There may be a need for bankruptcy reforms, and I think two other issues that I would raise and then turn it over to my colleagues is that we need to deal with the stigma of cash balance plans. I mean, cash balance plans actually provide significant opportunity and hope for the defined benefit system. But there are certain stigmas associated with them.

There are potential abuses when you do conversions of cash balance plans, but I think it's important to try to address the outstanding questions such that that is a viable option for people who want to stay in the defined benefit system. There's been a cloud over these plans for a long time. We've got to lift those clouds.

And the last thing I would say is that I think one has to realize that a disproportionate amount of the risk associated with the pension insurance system is concentrated in certain industries that bear certain characteristics. Number one, they tend to be subject to a lot more global competition, and in some cases, they tend to be deregulated industries.

I think one of the things we have to think about is to what extent are we providing a pension insurance system, or to what extent are we providing assistance for industry restructuring in a time of globalization and deregulation?

And I think one has to think about who should bear the costs and the burdens of that and to what extent should it be the pension insurance program or to what extent should it be a more direct method? Because after all, while the PBGC does have the authority to borrow $100 million from the U.S. Government, the PBGC is technically not backed by the full faith and credit of the United States. Now, on the other hand, we saw what happened with the S&L situation, you know, what happened there, when the Government stepped up.

The Government already has over $40 trillion in debt and unfunded obligations and commitments, $40 trillion. That's $330,000 for every full-time worker, when the average family income is $42,000, and it's getting bigger every second. So the time for action is really now, not just from the standpoint of the PBGC and other reforms that are necessary but, frankly, with regard to the overall Federal budget.

Thank you.

MR. HOLTZ-EAKIN: Thank you, Doug and COFFI for the chance to be here today.

The central policy issue is the desirability of preserving the private defined benefit pension plan as part of the retirement security in America. It fits into the larger array of issues that David Walker mentioned about the role of Social Security, the role of private saving and then the third of the traditional three-legged stool, private employer pensions.

And the central design issue, as a result, is the importance of distinguishing between those checks written as a legacy of the past and those checks which might have to be written for pension systems going forward.

It is the case that the U.S. pension system appears to be substantially underfunded. That is, plans lack sufficient assets to pay promised benefits, and the PBGC does not have sufficient premiums and other income to make up the difference. Thus, the general momentum, as you move down the table, on policies is quite clear. It will be the case that higher insurance premiums and lower risks to the PBGC will require faster and larger contributions by corporate sponsors, less risky investment policies by pension plans, and in making changes to policy, good incentives will in fact require to distinguishing between those high risk plans and sponsors and those which are lower risk plans and sponsors. And, put bluntly, that means that premiums have to be risk adjusted in the way that Brad Belt mentioned at the outset.

However, the preservation of the policy choice, the DB plan really requires that in moving toward any new premium structure, you distinguish between the sunk costs of the past and any pricing of the future. Using estimates that are available from our host today, you can put the sunk costs in the neighborhood of something like $20 billion to $25 billion. That may be a cyclically high number because of relatively low equity prices at the moment and relatively low interest rates that raised the liability, but there is a substantial sunk cost from the past.

And to the extent that the premiums incorporate a sufficient amount the cover that sunk cost, they will have to, again, using the estimates out of the COFFI model, be triple or even quadruple their current levels, and if the premiums were done in that fashion, there is a clear incentive for sponsors to terminate plans and perhaps move to other kinds of plans, such as cash balance or defined contribution plans in general.

So the structure of the design will really have a great influence on the central policy question, which is will there be a neutral playing field, which will allow those employees and employers who desire to have this kind of private defined benefit pension plan the opportunity to do so?

And in other issues, I think it's important to emphasize that acting now as opposed to later will allocate more of the costs to employers, and that's appropriate as these pensions are a form of compensation, albeit deferred, and it will allocate less of that cost to the U.S. taxpayer. So it is desirable to reform the funding rules and the premium structure sooner as opposed to later.

And in doing it, I would echo some of the remarks that have been made before that. It is desirable for the Congress to have very good information about the nature of the scale of the problem and its distribution, and to the extent that present budgetary presentation of these programs is not leading to appropriate tradeoffs, then, we should investigate ways to present the information better, and the Congressional Budget Office has worked on this issue in other areas associated with financial transactions of the U.S. Government, and we are interested in working in this area as well and look forward to working with the Congress in that effort.

But I think the real issue is to step back from the PBGC and remember that it's not really about the Government Pension Benefit Guaranty Corporation. It's about the structure of retirement plans in the United States and the degree to which the policy setting will allow a neutral choice that lets employers and employees pick the kind of pension plan which best suits their needs, and we've got to keep our eye on the ball in doing that.

And I'll turn it over to you.

MR. IWRY: As we all know, we are entering into a national debate of considerable importance focused here on Capitol Hill on what to do about the issues that my colleagues have just discussed in such a thoughtful way.

I would hope that the debate will expand to include several matters that often go unquestioned. We should not allow the debate, I would suggest, to be captured or preempted by assertions that are going unchallenged and that ought to be challenged or looked at more carefully.

For example, we've just put in a temporary stopgap measure to deal with largely the discount rate issue after a lot of discussion about whether to use a yield curve approach to determining the defined benefit pension discount rate or an approach that is not based on a yield curve with a range of maturities.

It was clear that the 30-year Treasury rate, which had been determined as the discount rate in the previous legislation enacted a decade ago was no longer an accurate reflection of a riskless discount rate. Treasury had stopped issuing those securities. The market was thin. The rate was lower, artificially low.

Unfortunately, we went immediately and I would suggest without much serious discussion to a corporate bond rate as the answer. And the discussion then proceeded to soak up most of its energy around the issue of whether that corporate bond rate ought to be determined using a yield curve or not a yield curve. I would suggest that the whole yield curve issue, while meaningful and worth debating, is almost a red herring; that what we really ought to be revisiting is the question what is the appropriate permanent or long-term discount rate, whether a yield curve or a non yield curve approach is used in applying it and that that discussion is a legitimate debate to have and one we ought to have with a full recognition that the 100 or 150 basis points between a riskless long-term rate and a high credit quality, AA, AAA corporate bond rate is one that involves many billions of dollars of funding, and indeed, each basis point involves significant dollars, and Congress ought to approach this from that standpoint.

Similarly, when it comes to the funding of plans in situations where they're not in extremis, where there's a reasonably good financial situation on the part of the company, it's commonly asserted without question that much of the problem with funding is that the rules prevent companies from funding in good times. The rules are too tight. We need to be able to put away more in good times, so we'll have a cushion there in bad times.

As a broad generalization, that's true. But a fairer assessment would take into account the fact that we have just repealed the full funding limit that was the subject of most concern and was the greater constraint during the past two decades.

We've repealed the so-called OBRA '87, the 150 percent of current liability full funding limit. That was the target of the efforts to relax funding and permit more funding in good times for the last 10 or 15 years. It has disappeared almost without mention on Capitol Hill.

Surely, we ought to go back, and while we're reiterating this same concern that the rules are too tight, look at what the effect has been of having repealed the more stringent of the two existing limits on pension funding. The other limit still remains, but it is the ERISA full funding limit that gives actuaries far more discretion to fund as they and their clients think best.

A related clarification of this proposition that we need to be able to fund more in good times; that the rules are too tight, would be a clarification and removal of the confusion about what we mean by good times and bad times. It's not all in sync. There's the state of the overall economy: where are interest rates? Where are stock values? There's the financial state of a particular company, which might or might not reflect the state of the industry that it's in, and there's the financial state of a particular plan. How well funded or poorly funded is it? The rules aren't all operating on those three factors in the same way or at the same time. And those three factors obviously don't coincide necessarily.

Finally, it's worth considering the evidence on how often and to what extent companies were in fact prevented in the nineties and earlier from funding more because they were up against the legal limits, and how often did they simply choose, perhaps entirely legitimately and entirely appropriately, to take a funding contribution holiday because they were able to do so?

And in particular, where companies might have been constrained by a full funding limit from funding more in the past, to what extent was that attributable to the funding limit that we have just repealed, effective January 1, 2004?

It's often noted that an underlying issue here is what needs to be done to the system to minimize the risk of a taxpayer bailout. In thinking about the taxpayer bailout prospect, relatively remote as I think most people assume it to be, I'd suggest that the question is not whether ultimately it will be necessary to put taxpayer money into the defined benefit system but rather whether it will ultimately be necessary to increase the taxpayer money we already have in the defined benefit and defined contribution system, namely, about $150 billion a year in foregone tax revenues or “tax expenditures”, according to the Treasury Department's estimate of the annual tax expenditure.

As a footnote, there's lots of room for debate about what that number really is, and there's a present value estimate that the Treasury has put out and other estimates that the Joint Committee have put out, but bottom line here is that we already have a very large investment of taxpayer equity in this project called the private pension system, and the equity investors have a legitimate right to ask these questions and to consider whether to regulate how plans, for example, are invested and whether to change the funding rules and the way in which the actuarial profession now deals with those rules.

My next suggestion can be summarized in three simple words: creative accounting.

[Laughter.]

MR. WALKER: That IS creative accounting.

[Laughter.]

MR. IWRY: I didn't mean to take up this much time with that point.

[Laughter.]

MR. IWRY: Something that policy makers in Washington tend to neglect and to underestimate is the driving role of financial reporting and accounting results in corporate decision making.

As some of my colleagues have noted, and as more of my colleagues in the next panel are sure to note, it is a voluntary system, and much of the fate of the defined benefit plan and pensions generally depends, and should depend, on employers' willingness to sponsor them as well as employees' demand for them. But what Congress often neglects in its thinking is the impact of the plan's assets and liabilities, the defined benefit plan, on the company's financial statements and quarterly earnings.

We need to look at the practice of using certain earnings assumptions to contribute to P&L. We need to consider more generally that defined benefit plans, if we wish for them to survive, and most of us in this room, I think, do, although that is not a unanimous point of view, that the defined benefit plans, if we wish for them to survive, cannot be used as an instrument of quarterly corporate earnings management.

If the fate of the defined benefit depends on the whims of the market, that will mean that yesterday's darling, the DB plan that contributed to earnings and helped the company smooth out its quarterly results, the plan that looked like a great asset in the eyes of the CFO will, tomorrow, when the market changes, look like an albatross dragging earnings down and suddenly a very questionable value to the company.

I would expect, with respect to the transparency issue that my colleagues addressed, that Congress will soon enact legislation requiring termination liability, the section 4010 of ERISA reporting, the more meaningful picture of the liabilities of a plan when it is at least in trouble or when trouble is in prospect, to be disclosed publicly. Right now, plans with $50 million of underfunding or more have to report this confidentially to the PBGC, and the PBGC is precluded from releasing that information.

I would hope at least in appropriate cases, where there's some reason to be concerned, that that information will be available to employees and the public. But in the meanwhile, I'd like to issue a friendly challenge to the PBGC: to voluntarily adopt a standard of transparency regarding PBGC financial information that opens everything up to public scrutiny, especially for purposes of the debate that Congress and the nation are about to enter into in earnest, except to the extent necessary to protect the confidentiality of company-specific information.

And by company-specific, I'm not referring to the Pension Guaranty Benefit Corporation but to the plan sponsors. The data on plan assets that the PBGC is taking over as well as liabilities and data on PBGC's situation generally, including the modeling that it does, would be helpful to be shared on a fuller basis with Congress and the public.

Final point: Congress should approach this issue recognizing that it is larger, as a number of my colleagues, have noted than the PBGC and its financial condition. PBGC is not simply an insurance company with a Federal charter. It's part of an employer plan system in which defined benefit plans play a central role.

But each step that the administration and Congress take in formulating the reforms that we're looking towards can obviously reflect a fundamental difference in attitude toward defined benefit plans, a fundamental difference in the priority with which people hold the care and feeding and survival of defined benefit plans and their role in the employer system, which reflects a difference in outlook on the role of employer health and retirement plans more generally. More broadly still, this is an issue of industrial policy that obviously has to do with how we deal with old line industries, manufacturing, companies and industries hit by global competition and confronting legacy costs for both health and pensions for the retirees that have assumed a far greater proportion relative to the company's net worth and the company's net income than had ever been anticipated when the promises were entered into.

MR. ELLIOTT: Thank you all. I think that was a really wonderful panel.

We've probably got about 10 minutes for questions for this panel. I'm going to take my prerogative and ask the first question but encourage you all to think of your own questions while I'm doing that. This is a controversial one, so I'm going to let volunteers pick up this one.

People, particularly financial economists, have noted that much of the volatility of pension results has been due to the high level of stock investments in those pension plans. That obviously brings attendant risk for PBGC.

Is that fine? Should the Government be doing something to discourage that level of equity investment? Anyone care to pick up on that one? David?

MR. WALKER: The only comment I would make on that is related to one I made before. If you want to define risk, you need to define risk broadly, and risk, from the standpoint of the PBGC and potentially benefit security is a combination of not just what the current funding status is; it's the asset allocation of the plan; it's the benefit structure of the plan; and a variety of other factors.

So I think it's something that needs to, at a minimum, be considered from the standpoint of defining true risk and what premiums should be charged on that basis.

MR. ELLIOTT: Anyone else?

MR. HOLTZ-EAKIN: I think that's just about on the nose. You've got multiple policy instruments, whether it's the restrictions on the portfolio investments; whether it's the pricing at a premium, and they're going to interact. And so, to the extent that you want to have risk-based premiums, and you've adjusted the other policy instruments, you'll get different answers. And so, you really can't answer that in isolation thinking about the overall structure of the reform and making sure that you've got both the level of funding right and rational incentives.

Given that this is voluntary participation and the plans will be structured in that way, you've got to get the incentives right.

MR. ELLIOTT: Mark?

MR. IWRY: Doug, I think those of us who have spent most of our careers involved in the pension system probably have a tendency to become more insular than we ought to be. And I think that it is actually constructive that the economists, financial economists in particular, have turned their attention to this issue and that instead of rebuffing it reflexively, which would be the impulse of many in the pension community, that we ought to embrace that point of view that there's a legitimate debate to be had here about whether the defined benefit system ought to be more significantly in fixed-income, laddered maturities that immunize the portfolios and less exposed to equities.

I think that this is, in part, a function of the accounting issues that I was talking about a couple of minutes ago, that the more exposed the plan is to equities, the more the fluctuations of the stock market lend themselves to being translated to fluctuations in corporate earnings, and that makes the plan more of a football for the CFO, whether he or she likes it or not.

The question, though, of what we actually ought to do about this has to be taken with the fact that we are a mature system; that is, we have to take into account the fact that we are where we are. The defined benefit system isn't growing; we're not starting a new system from scratch. If we were, this might be much more of a clean slate question.

But now that we are very heavily in equities, and some of the estimates are in the aggregate 75 percent as of a couple of years ago, probably less now with the market being somewhat down, I think we have to look at realistic questions of dislocation and transition.

But we ought to face this one. We ought to have a debate about whether the plans ought to be more protected from equity exposure.

MR. ELLIOTT: Okay; thank you. And I don’t mean to take sides in the debate, either. I'd just agree with you. I think it's one of the elephants in the room we ought to talk about.

Are there questions from the audience?

Susan?

QUESTION: Susan Cornwell with Reuters. I've got a question for Mr. Belt mainly. I was wondering how soon you think the Administration will come forward with its proposal and if you can say how it will be heralded. Can we, perhaps, expect, for example, a reference in the State of the Union?

There's been a lot of talk about doing something with Social Security, but there seems to be more agreement, perhaps, between the parties about trying to do something about pensions. And perhaps the administration would want to move to that first, ahead of getting into the Social Security issue.

So, any comments on that would be welcome.

MR. BELT: Fortunately, I'm not the President's speech writer, and I don't have much say in what goes into the President's State of the Union message. What was in PBGC's press release this week and what was also seconded by the President's spokesman, Scott McClellan, was that the administration would be putting forth a comprehensive reform proposal when Congress reconvenes next year.

QUESTION: I have a question. I'm staying away from all of the politically charged questions. I was just down here writing notes, and my question is for David: when you talked about the overall debt and broke it all down per full-time worker, could you give me that figure again, please?

MR. WALKER: If you consider the total debt outstanding in the United States, it's about $7.4 trillion. If, on top of that, you add the difference between promised benefits and funded benefits under the current structure for Social Security, Medicare, veterans health, and a variety of other issues, the current accumulated unfunded burden in today's dollars is over $40 trillion, which is about 18 times the entire budget, about three and a half times the economy.

We're in a deep hole. First, we have to stop digging, and then, we've got to figure out how we're going to reconcile the growing long-term fiscal gap.

QUESTION: I think she wanted to know per worker.

MR. WALKER: Per worker? Oh, I'm sorry, $330,000 per full-time worker; $140,000 per American, even the newest newborn. And that's non-tax deductible.

[Laughter.]

QUESTION: This is a question for Mr. Walker. I was interested in your remarks as to whether we should [unclear word] pension insurance or [unclear word] insurance since the problems should be greatest on certain industries which are facing global competition issues. You had mentioned the issue of risk premiums, since these problems need to be industry-focused on the airlines right now; would there be merit to having this insurance focused on an industry that might be in trouble, and could you elaborate on the need to restructure this in terms of insurance against global economic issues?

MR. WALKER: Well, when PBGC was created in 1974, it was created to provide for a level of pension insurance for defined benefit pension plans subject to certain limitations, and a lot has happened since 1974, both domestically and globally, as it relates to the economy and restructuring.

I think a legitimate discussion and debate can be held about analyzing the nature of what the risk is with regard to PBGC. To what extent are some of these risks generic, systemic risks that bear no relationship to industry, for example? Or to what extent is there a disproportionate degree of risk associated with certain industries, and what are the factors or potential common factors that relate to those industries?

A conscious discussion and debate could then be held about whether this should be handled like every other pension risk, or should we consider alternative approaches, either within or outside of the pension insurance system as a possible way to deal with those issues.

When the airline industry had a problem post-9/11, there was a reaction by Congress to provide short-term grants and medium-range loan guarantees in certain circumstances. I was on that board, the Airline Transportation Stabilization Board, although I didn't deal with individual loan guarantees for a variety of reasons.

I'm not saying that's an answer. I'm just saying we ought to have a discussion and debate about that, because the fact is there is a concentration in certain industries that do bear certain common attributes.

MR. ELLIOTT: Yes, I did want to give Brad a chance to respond to Mark's friendly challenge before we take any other questions.

Brad?

MR. BELT: I guess the implication was, Mark, that you didn't think we were being particularly transparent and forthcoming, and that's unfortunate if that's your view or the generally held view. Certainly, that's not our intention, and it's not how we've been operating and will operate, at least with respect, for example, to disclosure of our financial numbers. We used to provide only that information on an annual basis; this year, we began doing so on a semiannual basis.

I know there have been some issues in the community of questions or concerns about our model, some about our annuity pricing model for measuring our liabilities, and I will certainly state in this forum, because I've stated in Jim's at ABC's and a host of others that certainly, there is nothing to hide. It's in our interest to make sure that everybody understands each one of those issues, and if there are ways that they can be improved, then, by all means, we want to sit down and talk about that.

You asked specifically, the only specific item you mentioned other than modeling was data on plan assets that we assume. I guess I don't have any problems with providing that information, although it's not particularly relevant, since we transition those assets that come in one form, and we transition them to be consistent with our investment policy, which, as you know by law, all the premium revenues are in Treasury instruments. We do have more discretion over the trust fund assets, but we've implemented--we've adopted a new investment policy this year and are in the process of implementing that which is designed to better match our assets to our liabilities on a go forward basis.

So I'm not sure how much utility there would be in the information about the plan assets that we assume.

MR. IWRY: Brad, thanks, yes, I was not meaning to suggest that PBGC was not being forthcoming now but rather that as we embark on this debate, it would be helpful to really make as much information available as possible and that there are some areas where, while one might debate the full utility of the disclosures, I think as a matter of collaboration and working together with the premium payers, the sponsors of the defined benefit plans and the employees who are ultimately insured, that it would be useful to really open your doors up and give people an opportunity to get together with PBGC at the staff level and ask their questions, technical questions, about the data, including assumptions about assets that are likely to be taken over, that are probable of being taken over, amounts of assets as opposed to the particular investment mix, as well as liabilities, again, to the extent appropriate while protecting confidential individual company information.

MR. BELT: And I certainly welcome your inquiries and that of anybody in the audience. My phone is always open; my email is open. The staff is as well, so we would welcome those inquiries.

The broader issue of transparency, I think, before we break, is a critically important one, because, at the end of the day, rather than, again, as I stated previously, loading up ERISA with new regulations, new disclosure requirements, I think the first order of business is to get better information out in the marketplace. I know Dick Berner, a host of other folks look through the 10-Ks, the 10-Qs; there's been a step forward with respect to the FAS changes.

But we need to go much further than that; still, very limited information there: plans, domestic, international rolled up; it's not broken out specifically by domestic plan. The asset breakdowns are of limited utility. There's much more that can be done, and that way, we can begin to get better discipline provided by the marketplace, and I think that would be the most appropriate way to move forward.

One of the things we're talking to the SEC about is improving disclosure generally. I think the market has not been sufficiently attuned to things like investment risk before, like actuarial risk, like credit risk, the impact of pensions on the income statement and on the balance sheet. And to the extent that we can get more information out there, then, I think that could be very, very constructive on a go forward basis.

Better disclosures on the MD&A, looking more than 12 months ahead, et cetera, the impact of ERISA contributions; those things, I think, are where we should focus.

MR. ELLIOTT: All right; just one more question, I think. Sir?

QUESTION: In my role in a professional committee, this morning, I was given the charge to write a white paper, part of which needs to define transparency. And I think, Bradley Belt, I've heard you use lack of transparency or transparency the most this morning or this afternoon and was wondering not so much what your definition of it is as how do you look at any rule or proposed rule and say this moves us towards transparency?

You know, how do we, you know, measure things as being transparent or not?

MR. BELT: Good question. PBGC, again as part of this kind of proactivity in terms of engaging all the different stakeholder groups and getting a handle on these issues, a week ago, two weeks ago, we sponsored a roundtable at the PBGC that brought together the FASB, the SEC, American Academy of Actuaries: actuaries, financial economists, accountants and others, to begin to get a handle on these issues.

Everybody looks at pensions through different prisms. Everybody speaks a different language. And we need to get past this bridge and begin to speak a common language, reach some understandings about what is the relevant information that's of utility to plan participants? What is the relevant information that's of utility to investors in companies and analysts and to regulators?

And then, what's the best way to get that information out to those users of that information, and how timely should it be? And that's what we're talking about with transparency. I don't think there is a clear definition, and it may be that there is not a single set of information that is directly applicable to those three different groups. But I suspect there can be a lot of convergence.

QUESTION: I was at a meeting with the board, the FASB board recently. As we got up to go to lunch, I threw this out; you know, I'm going to have to write this. They all laughed at me and gave me the good luck pat on the back, like I had the audacity to think that I could actually write something like that. None of them were able to give me a definition.

MR. BELT: Well, I look forward to reading your paper.

[Laughter.]

MR. ELLIOTT: Doug, do you want to step into this?

MR. HOLTZ-EAKIN: Well, I just think that it's useful to remember that there should be some focus in the discussion about the PBGC, that in the end, it is about the design and execution of an insurance program for these DB pensions and that in the presence of an underpriced cheap piece of insurance, even greater disclosure and transparency won't necessarily change incentives.

If shareholders have a cheap put option to give it to the PBGC, that incentive remains no matter how it's disclosed. If you're a fully-insured person covered by the PBGC, and you're going to get your pension no matter what, your incentives aren't changed a bit by greater disclosure. And the incentives are going to matter here.

And on a going forward basis, using the instruments of asset allocation and pricing of insurance will determine a more efficient use of our nation's resources, and that should be distinguished from other policy objectives like reaction to changes in competitive structure from international competition. You really want to separate things and take this policy issue and just this policy issue and focus on it and fix it on a going forward basis.

I think that is the key.

MR. ELLIOTT: And I hate to stop after such an intriguing comment, but we're going to have to get to the second panel. But let's thank this panel, because I think they've done a wonderful job here.

[Applause.]

MR. ELLIOTT: And we'll just swap in the second panel.

Well, again, thank you to the second panel as well. I haven't had a chance to do that individually yet. As I said, it's Jim Klein, Karen Friedman and Alan Reuther. I'll just let Jim start in.

MR. KLEIN: Thank you, Doug, and I just want to compliment you, Doug, for hosting this forum. I think that in the short time that COFFI has been in existence, you've really done a lot to elevate the level of dialogue around a lot of issues, and I think it's really important that we're having this discussion.

Hubert Humphrey once said that everything that needs to be said has already been remarked upon, but not everybody has said it yet.

[Laughter.]

MR. KLEIN: So in that same spirit, you'll probably find a lot of what I have to say echoing some of the comments from the prior panel, but as the representative of the premium payers, it perhaps is relevant that I make some of those same points if for no other reason than to note that on many of these issues, not all but on many of these issues, employers are seeing it much the same way.

I decided to do this little PowerPoint for reasons that will become apparent just momentarily, but I just have about five or six slides. Since Monday, when the PBGC report came out showing that there's a $23 billion deficit, there have been a lot of comments reported upon, some on the Hill, some, quite a lot in the media, not actually, at all, on the prior panel, that have invoked again the specter of a taxpayer bailout, a savings and loan type of crisis.

The word crisis has been used quite a lot. And so, I wanted to think how I could represent what this $23 billion might actually mean. [Moderator and panelist unsuccessfully attempt to make projector work.]

Well, I'll do it without the slides, then. It won't have quite the same effect, but it's pertinent. So I thought of, you know, this $23 billion is not going to be something that the Federal Government would have to expend in one year. This is a liability that of course would be paid out over the course of many decades, during which time the retirees of the terminated plans would be receiving their benefits.

How can we understand this $23 billion? So I tried to think of what's another sort of long-term obligation that the Federal Government might take on for itself? And my daughter, who wants to be an astronaut, made me think of the President's proposal, also over the next couple of decades, that we might send a manned space mission to Mars, which conservatively has been estimated to cost $550 billion.

This next comment is going to be reminiscent of the point that Mark Iwry made on the last panel about creative accounting, but as my daughter has told me, there are three kinds of people in the world: those who are good in math, and those who aren't.

[Laughter.]

MR. KLEIN: So I decided to put together a little math problem to figure out and put this into context, and this is where the PowerPoint would help: the distance between the Earth and Mars is 62 million miles. If you take $550 billion, and you divide that by the 62 million miles that we would have to travel, it comes out to $8,871 per mile.

Well, how far would $23 billion get us to Mars? You do the math: 2,592,717 miles. That's only about one twenty-fifth of the way from Earth to Mars. Applying that same dollar per mile concept, to fly from New York to Los Angeles would cost $2,467,251, which, if the commercial carriers could charge that much for a seat, would go a long way toward their funding their pension plans.

[Laughter.]

MR. KLEIN: Now, right now, the blood is draining out of Doug's face wondering why in the world did I invite this crazy Jim Klein for this panel?

[Laughter.]

MR. KLEIN: Where is he going? I make this tongue in cheek example to actually underscore a very serious point, and that is that this $23 billion that is to be paid out over a great period of time, it's a real problem, but no one should doubt for a moment or suspect for a moment that it is a crisis that our economy could not bear the cost of paying that kind of liability; again, not in one year; consider--many of you are from the Hill here, consider the nature of the debate just this week in terms of reconciling the difference between the House and the Senate on a continuing resolution: expenditures to be made in one year, and now, we're talking about a figure that would be paid out over literally decades, which is not to say that it doesn't need to be addressed, and that's the point that I'm going to make at the very end.

But the fundamental threshold question that Doug posed to us was are these PBGC problems structural or just passing? And I wanted to share with you that I think there are two competing theories about that. The first theory is that over the 30-year history of the PBGC, the agency has served as a guarantor for participants in literally tens and tens and tens and tens of thousands of pension plans, of which a relatively few have actually terminated with insufficient assets and dumped their liabilities into the lap of the PBGC, and of those very few, you could probably count on two if not maybe one hand the number of plans that really accounts for virtually all of that $23 billion deficit.

And that therefore, you could make the case that the funding rules work actually quite well, thank you very much; that the overwhelming majority of plans pose no risk to the PBGC or to their participants, and that, in fact, the PBGC is serving exactly the purpose for which it was envisioned: as a safety net for those instances, perhaps in those industries, that for a variety of very complex reasons find themselves in a situation where they have these large liabilities, and the business conditions are such that they're not able to fulfill them. That's theory number one.

Theory number two is the opposite, that the fact that a handful of companies could present this kind of risk to the tens of thousands of other defined benefit plan sponsors to have to incur potentially greater costs to close the gap, and the fact that ultimately, the taxpayers may have to step in, including taxpayers who have never even in their careers been covered by a defined benefit plan, is fundamentally unfair and proves that the system is really fatally flawed.

I would submit that there's an element of truth in both theories, and what I'm concerned about is that the plan sponsors, who have for years, while some of them subscribing and concerned about this second theory, the fact that gee, this isn't fair; we need our pension obligations; you know, why do we have to pay PBGC premiums, have nonetheless, for the most part, bought into the social compact that's represented by the first theory, the notion that this is the safety net, the final backstop to ensure that people don't lose everything if their pension plan should go belly up.

But I wonder if we have reached or are about to reach the so-called tipping point, which is a term that's entered the vocabulary, where more and more employers are going to subscribe to the second theory? Because in fact, there is a real pension crisis, but it's not the crisis that folks have been talking about. I think the real pension crisis, the one that's gotten a lot less attention, is that the defined benefit system itself is in very, very serious decline.

From 1999 to 2003, there was a 25 percent drop in the number of defined benefit pension plans in this country, and that follows on a pretty steady decline in the several years prior to that. These plans represent the premium base that supports the PBGC, represents the system for which the PBGC sees purposes in being.

And I therefore believe that in addressing the PBGC's problems that we will fortunately begin upon doing next year, we will have to not only address the questions about pension funding and perhaps priority status and bankruptcy and things like that that we talked about previously but also some broader issues around what's ailing the defined benefit pension system, a couple of which were alluded to on the first panel.

For me, the biggest crisis facing the pension system is a crisis of uncertainty. Plan sponsors, for a variety of reasons, are existing in a very uncertain, very volatile situation. First of all, there's uncertainty with regard to the interest rate that they're going to be required to use for purposes of calculating their liabilities, and they can't honestly tell the Wall Street analysts what their pension is going to cost them two years from now, because they don't yet know what interest rate Congress is going to require them to use for purposes of calculating that liability.

Dave Walker mentioned the issue of cash balance and other hybrid plans, and that is a controversial topic that is worthy of a separate policy forum all on its own. But the fact is that from an employer's perspective, I would argue from a participant's perspective, but I don't speak for them, but certainly, from an employer's perspective, we believe that the transition from traditional defined benefit plans to cash balance and other types of hybrid plans is the one good thing that's been going on in the pension system over the last several years, because it's keeping companies in the defined benefit system. To the extent that the future, the legal viability of cash balance plans, remains in question as it has as a result of both litigation and

Congressional consideration of this issue; to the extent that that continues on for a longer time, the more uncertain companies are about whether or not to sponsor plans, and they're not going to revert back to the traditional kind of design; they've already made the decision that that doesn't work for their business model; the decision will be to get out of the defined benefit system altogether.

There's uncertainty about whether certain accounting standards that have been talked about on the International Accounting Standards Board might get adopted over here, and now, the added uncertainty about how Congress will respond to this very real PBGC problem that's been presented to us.

Will Congress respond with dramatically higher premiums that will be one element of the tipping point to cause employers, well-funded employers to say this really isn't worth it anymore; you know, this is beyond the social compact where we're really directly subsidizing the less well-funded plans?

Will there be onerous funding rules which might or might not adversely affect those better-funded plans but might be so severe that they represent the tipping point for the less well funded plans and force them to exit the system altogether and to do exactly what we would hope to avoid, which is to terminate and place their liabilities upon the PBGC?

So I started out by saying it's not a crisis; it's a real problem, but I also wanted to underscore in the clearest terms that the fact that it's merely a problem and not a crisis is not an excuse for delaying, and in that regard, I think I'm echoing each of the prior panelists and I would suspect those who will follow me.

Why? Well, as Doug indicated in his opening remarks, that $23 billion could actually be a number that's much greater, and like any other problem in life, the sooner you deal with it, the more likely you'll keep it from growing. But fundamentally, I think the reason that Congress needs to deal with it next year is not that the number itself is so daunting, but it's this issue of certainty and whether or not employers will remain in the system at all.

And in my 20-plus year career, I've never before witnessed a time when there was such a confluence of different factors that are making employers rethink the wisdom of staying within this system. We can talk about some specific proposals later, I suppose, if there's time and interest, of things that might be done, but I would just conclude by making the point that we really need to decide what is the objective.

If, as a nation, we've decided to give up on the system altogether, we can probably develop some orderly rules by which we can begin to exit out of that system, allow companies that go through a certain cycle to exit that defined benefit system and to permit, in an orderly sort of way, the better-funded plans to leave.

If we're not quite ready to throw in the towel, it may require, much as we regret doing it, accepting the fact that we will have to, as a country, bear some of that expense of that liability in an affordable way, because it will be done over a long period of time, but to develop rules that will not encourage employers to exit that system and moreover to look at the future fiscal integrity of the PBGC as an issue that will be determined not by what we do only with respect to shoring up the funding of plans themselves but by all of the other decisions that we will make relative to the pending pension issues that are before the Congress.

MR. ELLIOTT: Thank you, Jim.

Alan?

MR. REUTHER: I'd like to join in thanking COFFI for sponsoring this forum and beginning the discussion about what to do about the PBGC situation.

The UAW and the Steelworkers Union were deeply involved in the creation of the PBGC. It was the collapse of the UAW negotiated pension plan at the Studebaker auto company that shocked the conscience of the nation and led to a 10-year campaign to pass ERISA and to include termination insurance.

We were also deeply involved, and I see Phyllis Borzi here in the audience, with her and Representative Clay and Representative Roukema, in passing the 1986 legislation that really created the current structure of the single employer termination insurance program. We've had many smaller plants that have terminated plans and been involved with the PBGC, so we have a very strong commitment to making sure that the PBGC continues and is on a strong footing.

Yes, we think that the PBGC is facing a problem. I was pleased to hear Bradley Belt indicate that it's not a problem of the agency running out of money this year or for the next 15 years probably, so it's not the type of crisis where checks are going to be cut off soon. I think there's also no dispute, really, about what the source of the problem is, though.

A number of years ago, the PBGC was running surpluses. Then, you had a wave of bankruptcies in the steel industry, especially Bethlehem and LTV, which were the biggest losses by far that the PBGC ever had to absorb, and that started the PBGC down the road of having deficits, and now, we're facing the looming terminations of plans in the airline industry, whose plans have unfunded liabilities that dwarf those of the steel industry.

So there's really no mystery here. The PBGC is facing a problem because our nation allowed the steel industry and now the airline industry, major segments, to go down the tubes. Now, in terms of how we respond to that, we agree with earlier speakers that there is a need for funding reforms to be enacted to strengthen the funding rules so that other industries don't encounter similar problems and have pension plans with unfunded liabilities similar to those that we've seen in the airline industry and steel industry.

Obviously, those will take time to improve the funded status of the plans, and there are some funding changes we like, some we don't; I'd be happy to answer questions about those later. But there's also a question about okay, what do we do about the immediate deficit that the PBGC has because of the airline and steel liabilities?

The UAW strongly opposes any cutback in the PBGC guarantees. And I was glad to hear speakers on the first panel admit that under the current system, the workers and retirees aren't completely protected. They are going to experience significant losses, not only because of the cap on the guarantees but also because of the five-year phase-in rule on the guarantees.

So workers and retirees are already being hurt; we think it's unfair to shift paying for these airline and steel liabilities, to shift it onto their backs even more through cuts in the guarantees.

The UAW is also very much opposed to increases in the premiums paid by plan sponsors, either the flat premium or the creation of some new type of risk-related premium. First of all, that would be a big hit financially on many companies. I've seen one estimate that premiums would have to be increased sixfold in order to pay for the airline liabilities. That type of financial hit is bad in and of itself for a lot of the plan sponsors.

We think, and I agree with Jim in this respect, that that would lead to an exodus of a lot of a lot of employers from the DB system, and what you'll basically see is a death spiral and a contraction of the DB system, and that will put the PBGC in an even worse position.

I'd also like to point out that those types of premium increases would exacerbate some of the competitive problems we're facing, specifically in the auto industry. We already have a huge competitive problem of the big three auto companies having an awful lot of retirees, two retirees to every active at GM, one-to-one at Ford and Daimler Chrysler. They're competing with Japanese transplants in this country that are so new they have virtually no retirees.

There's already about $1,000 per car differential just on the legacy health care costs. If you start jacking up the PBGC premiums to try and handle the airline and steel liabilities, you're just going to make the big three even less competitive with the Japanese transplants.

There's a lot of talk about transparency. You know, if they're going to pursue these types of premium increases, should they be required to say which auto plants are going to close? Which people are going to lose their jobs because the big three are going to be less competitive?

One word I'd like to say about the notion of creating a new type of risk-related premium that would reflect the risk that the employer or the company poses. It's sort of ironic that we're about to see a Republican administration come out with that proposal. I can't think of anything that would be more big brother government than having the Government starting to say, well, we think Daimler Chrysler is going to go out of business but not GM or, you know, whatever you want to say.

And I think you will find that will be anathema to the business community, and, you know, I'm not even sure how the government would begin to evaluate that type of risk.

The UAW is also very strongly opposed to proposals to increase the PBGC's standing in bankruptcy proceedings, proposals like giving them a lien for unpaid contributions, which Bradley Belt referred to, or changing the distress criteria somehow to give them more leverage. First of all, what we think this will do is drive the lending community away from companies that are in distress and just lead to more liquidations of companies that are in distress, which will be totally counterproductive; will ultimately hurt the PBGC's premium base, will hurt the workers and retirees.

We also think it's very important to recognize that when you have a company in bankruptcy, it's a zero sum game. If you elevate one particular creditor's priority, such as the PBGC, that means other creditors are going to get less. Who is probably the single biggest group of creditors in many of these major bankruptcies? It's the retirees with their retiree health benefits.

So when the PBGC says give us a lien for these missed contributions, they're basically saying their balance sheet should be improved. They should collect more, and the retirees should lose their retiree health benefits. You know, and this is from an agency that is supposed to be protecting the retirees.

In terms of the criteria for going into a distress termination and turning over your plan to the PBGC, I think there's a lot of misunderstanding here. I think people think that all you have to do is file the Chapter 11 petition, and immediately, you can transfer your plan to the PBGC, and it's this abusive process.

It's simply not the case. What current law says is that if you're in Chapter 11 reorganization, the bankruptcy judge has to find that unless the plan is terminated, you're going to go out of business. And what the process allows for is the PBGC and the labor unions and everyone else to come in and say no, they don't have to terminate; there's another possibility; they can freeze the plan, or the executives can take a reduction in their compensation or whatever you want.

But basically, at the end of the day, you have a neutral party, the bankruptcy judge, that's making a determination about the financial condition of the company and what is necessary to prevent the complete liquidation of that company. And again, I'd just underscore: you try and change that; what are we really saying? That we want more companies to completely liquidate and not to come out of bankruptcy reorganization? We think in the end, that's counterproductive not only for the companies but also for the workers and retirees and ultimately for the PBGC.

The PBGC already has enormous leverage in these bankruptcy proceedings, since they are one of the largest creditors; enormous leverage over the ultimate shape of any reorganization. So they're not this poor party that's just sitting there, being abused during the bankruptcy proceeding.

What type of approaches, then, would we support? One proposal that's been made, I know, by the airline pilots has been to freeze the plans in the airline industry; also freeze the guarantees; make the companies fund those liabilities over 30 years. We could support that type of approach. In many cases of companies that are distressed, we've actually proposed that in negotiations.

What I fear, though, is that the horse may already be out of the barn, and by the time Congress gets around to doing anything, some of these plans in the airline industry will already have been terminated, and we know that the companies themselves are opposing any requirement that they freeze the pension plans. So I'm not sure how feasible that approach would be.

A second approach that we could support would be the imposition of some industrywide tax, perhaps a tax on all airline tickets; perhaps an airport concessions tax; if we can fund a baseball stadium in Washington, D.C. with a concessions tax, we don't think it's out of line to think about using that type of mechanism to pay for these airline liabilities.

The key here, though, is if you're going to do any type of tax, it has to be across the board on all the airlines. If you say we're only going to tax those companies that are terminating their plans, all you're going to do is exacerbate the competitive differences in the airline industry; drive more airlines out of business more quickly.

Am I optimistic about this kind of approach? No. I think the industry generally would say we don't want any more taxes; oil prices are already too high, et cetera, so I'm not optimistic about that kind of approach either.

Fundamentally, at the end of the day, what the UAW believes ought to be the proper course is to have an infusion of general revenues to cover the airline and steel liabilities that the PBGC is going to be taking over. The PBGC was never designed to deal with major segments of entire industries going under. The Studebaker case, you didn't have the entire auto industry going under; it was one isolated company. That's the situation in most of the cases.

But it's obviously not what we've had in steel and airlines. We could have a long discussion about why the steel and airline industries have reached the point that they're at. Obviously, there's been a lot of government policies and nonpolicies, whether it's trade or energy or deregulation or the whole 9/11 situation, and I don't want to get into that here.

But the bottom line is we do think this is a question of industrial policy. It's a question of how we're going to respond to the restructuring of these industries and respond to the global competition, especially in the case of the steel industry that created a large part of the problem.

Obviously, the Federal Government responded to the S&L crisis with general revenues. It routinely pays general revenues for natural disasters, hurricanes, drought relief. You know, we don't think it's out of line to say we've had a disaster in steel and airline and the government ought to step up.

Ironically, we've already had a Republican Congress and a Republican president embrace the notion of using general revenues to address the steel situation. As part of the 2002 trade legislation, they enacted provisions, current law, that says if the PBGC takes over a pension plan and is paying the benefits, and the early retirees, 55 to 65, have lost their health care benefits, the Federal Government, out of general revenues, will provide a 65 percent tax credit to those retirees to pay for their health care.

Now, it's a very badly designed health care tax credit; most of these retirees are not able to use it. But some are. And why was this done? Obviously, it was a response to the devastation in the steel communities: Pennsylvania and Ohio and West Virginia, but clearly, Congress said yes, we can use general revenues for that type of a response. We don't believe it's so different to say you can use general revenues to address the pension problem that's been created by the demise of the steel and airline industries.

I understand that there's a kneejerk reaction by a lot of people of oh, we don't have any general revenues to pay for this; I would note that in the discussions about Social Security, already some people are saying oh, that trillion dollars of transition cost, no problem; we'll just do that off-budget, so that doesn't seem to be any problem. I would also note that the administration is going to be proposing major new tax expenditures to vastly increase the amounts that wealthy individuals can contribute to tax deferred individual savings accounts, which probably will

further undermine the defined benefit system. But, you know, if we can spend money on that, why couldn't we take that money instead and use it to pay for the airline and steel liabilities.

Is general revenues a great idea? No, it's not our first choice. It just happens to be better than any of the other alternatives. We believe it's better than cutting the guarantees and directly hurting retirees. We believe it's better than shifting the costs onto other employers and plan sponsors. And we believe it's better than giving the PBGC more leverage in bankruptcy proceedings and having more companies that ultimately liquidate.

With that, I'll conclude. Thank you.

MR. ELLIOTT: Karen?

MS. FRIEDMAN: Do I still have 10 minutes, or are we running out of time here?

MR. ELLIOTT: Take your 10 minutes.

MS. FRIEDMAN: All right; I'm actually a fast talker, so that shouldn't be a problem.

Thank you, Doug, and thank you, COFFI, for putting together this forum. I'm Karen Friedman with the Pension Rights Center. We're a nonprofit organization that works to protect and promote the pension rights of workers and retirees and their families, and of course, we're pleased to be here today to talk about the PBGC from the perspective of employees, but before I begin, I first wanted to say that yesterday, I was talking about flying a rocket to the moon. I'm only kidding. Okay; I just had to do that. I'm sorry.

I know, so everybody's a little bit slow on the uptake on that. Okay; actually, I do want to start by talking about some fundamental concepts underlying this issue that are actually apart from the funding issues. Over the last two weeks, we've heard from pollsters and commentators who have said that millions of people in the last election voted on issues of moral values and security.

I would say that at the heart, the issue before us today, preserving the PBGC, is also about issues of morality and economic security. There are few things more fundamental to employees than knowing that they can count on promises made to them and that they can retire with the pensions that they expect for retirement.

Protecting benefit promises when companies can't meet those obligations is what the PBGC is all about. So whether some experts think the PBGC is facing a crisis, or others say that this is a long-term manageable funding issue, the bottom line is that we as a country have no choice but to ensure that this agency, what we call the crown jewel of the defined benefit system, has to stay strong for generations to come, and this is the right thing to do.

Obviously, and this is where I think all of us are in agreement, tied to the preservation of the PBGC is the health of the defined benefit system. We've all read the doomsday reports about the death of the DB system and how employees don't value these plans, and employers are bailing out of the system in droves. But it's in everybody's interest, everybody here, that we do everything we can to buck this trend and preserve DB plans and especially to keep promises to those now in the system, and I will later address Jim's comments on cash balance plans. I will get to that.

Employees care deeply about defined benefit plans, as evidenced from the protests when companies try to cut back, freeze, convert or terminate their defined benefit plans. As one pilot recently told me, it's defined benefit plans that have built a middle class in this country. If we let companies dump them, it's going to be the end of the middle class.

So now, I'll attempt to answer the questions, is the PBGC in crisis, and does it need structural change? We've heard today that the PBGC's deficit has climbed to $23 billion, but what does this number really mean in plain English? It means that if the PBGC closed its doors tomorrow and had to pay all of its promised benefits at once, then, this would be an immediate problem.

But this isn't going to happen. While we recognize the deficit could be cause for long-term concern, we don't want to induce panic among employees and retirees that the PBGC will go under and not pay its benefits. Americans are living in constant fear now over the plummeting economy: downsizing, wage cuts, terrorism, not the mention the shortage of flu shots and mercury in tuna.

We shouldn't be spreading panic among people about their pensions. We have to keep in mind, to paraphrase Barbara Streisand, that people who have DB plans are the luckiest people in the world.

[Laughter.]

MS. FRIEDMAN: I would sing it for you, but you really don't want that.

[Laughter.]

MS. FRIEDMAN: People need to know that if their company goes under, the PBGC will be there to pay most of their benefits. So we're not looking at this as a Code Red situation but maybe as a Code Blue or Code Yellow, which gives us reason to deliberate on ways to develop solutions to something that could occur in 16 to 20 years.

Let's also keep in mind that the PBGC has been in deficit before. Some commentators, say, as many people here did, that this time, it may be worse, because there are fewer plans paying in; the deficit is huge, and so many companies are struggling economically. But according to actuaries I've spoken with, about $10 billion or about half of the PBGC's deficit could be eliminated if today's low interest rates reverted back to the rates the PBGC was using in mid-2000 and if the stock market went up just a little bit. So we have a long-term problem, but some of it could cure itself.

Other reasons not commonly cited for underfunding were discussed in a recent Wall Street Journal article that said that over the past decade, U.S. companies have siphoned off billions of dollars in assets from their pension plans. They've used the cash to pay for retirees' health coverage, the costs of laying off workers, and even fees to benefit consultants.

So whatever the causes of underfunding, we need to be cognizant of the problems to the agency long-term. In particular, we're extremely concerned about the intention of United and U.S. Airways to terminate their pension plans. We have a lot of questions regarding whether companies in reorganization should be able to use bankruptcy courts to eliminate pension obligations, at least without more critical probing of whether the termination is the only way to preserve the company as a viable operating entity.

The actions of United and U.S. Airways create a dangerous precedent and possibly, as Jim said, a tipping point for other companies to follow suit. This puts unnecessary strain on the PBGC, leads to reductions in employee benefits, and jeopardizes the long-term security of the system. Flight attendants, machinists, and pilots, who have called us over the last couple of weeks, have all used the term criminal to describe the actions of the airlines at first winning concessions from them and then working behind the scenes to terminate the plans.

Many employees have told us that they'll experience significant and unexpected reductions in benefits, as the panelists have all talked about. These employees feel that it's patently unfair to have pension plans wiped out as companies emerge from bankruptcies healthy. Now, certainly, the argument can be made that terminating plans can be a necessary evil to protect companies from going under. But we have concerns that pensions are the first thing on the chopping block and potentially other measures should be considered before these plans are stopped.

Continuation of these plans can mean the difference between whether people have adequate or inadequate incomes when they're too old to work. The PBGC was created to make sure that employees do not lose money when companies are truly in trouble and don't have money to pay benefits. Many employees feel that allowing companies to use bankruptcy courts to dump pension liabilities onto the PBGC in order to appease creditors subverts the intent of Congress in enacting ERISA and creating the PBGC.

Employees question whether there are other places that companies can cut or other measures that could be taken to avoid the draconian solution of terminating pension plans to supposedly save companies. Some commentators have suggested that there should be an examination of midterm measures, such as giving the PBGC the authority to freeze plans when absolutely necessary and then working out a financing plan until weak employers are back on their feet.

Professor Norman Stein suggests that it might be helpful if there was legislation that permitted the PBGC to negotiate with the unions and plan sponsors to allow the plan to continue but then only to freeze the guarantees. These ideas all need further development and examination, but they're a start.

As one flight attendant recently told me, these airlines are promoting long-term solutions to possibly short-term problems. Certainly, we think it's worth examining the kinds of solutions we talked about as well as other possible reforms needed in the bankruptcy process.

Certainly, the Pension Rights Center acknowledges this is a very complex issue, as you've heard today, and there are no easy answers to the questions before us. But we have to have a dialogue that's not heated by crisis rhetoric to develop the right solutions, and I'm going to go through a couple things that--ideas that we're exploring, and we have a written statement out on the front table that talks about these in more depth.

Before, there was a little bit of conversation about the PBGC and what kind of information it provides to employees. Right now, the PBGC is prohibited from giving out specific information on companies that are more than $50 million underfunded and that have to report to the PBGC, and we've heard from employees that tell us, you know, they just don't have the right information to assess is my plan really in trouble?

We think there needs to be a dialogue among all of us to figure out what's the information that employees need. We'd like to reopen the question of whether it's a good idea for companies to use surplus pension assets for non pension purposes; for example, companies now are able to use surplus assets for retiree health benefits and sometimes for merging overfunded and underfunded plans, and we just think there needs to be a dialogue on some of these issues.

And we were with everybody that we need to look at how to prudently strengthen funding rules, but I wanted to reinforce what Alan just said: we strongly oppose solutions that rely on benefit cuts for people in the work force today and who are counting on these benefits for the future. We heard from a few of the panelists and Alan, we're hearing from people across the board who are so upset because there's reductions even when the PBGC takes over those plans, so we really would like to not have to be part of the solution.

If, in fact, solutions involve benefit cuts, it should only be for those benefits earned in the future, and the benefits earned today should never be on the butcher's block.

Finally, we agree with Jim that the best way of addressing the PBGC's shortfall in the future is to try to keep companies in the DB system and encourage new employers to join these plans so more premiums are paid for more people. While some experts are already hammering the nails into the coffin of the DB system, we're less pessimistic.

We believe that there should be a priority for all stakeholders to undertake an all-out educational program similar to that launched by the Labor Department and the American Savings Education Council to educate employers and employees alike about the importance of DB plans to individuals, employers and the economy.

And there may be ways of creating new kinds of DB plans for the future. In my other hat at the Pension Rights Center, I direct something called the Conversation on Coverage, which is a public policy dialogue. We've brought together people on all different sides of the issue, labor unions, business, financial institutions, retiree groups to look at ways of increasing coverage for low and moderate wage earners who are not now covered, and one of our working groups has actually come up with new forms of defined benefit plans and new plans that may not be defined benefit plans but have some of the features, and we welcome you to look at our Website, which is, if you happen to care, www.pensioncoverage.net.

And finally, I think just in my closing words, I want to say that PBGC has been a great success for three decades. And we need to recognize that the current deficit may be the result of a confluence of extreme circumstances. So we have time now to deliberate about what the right kind of solutions are to ensure that they balance the interests of employees, employers and the PBGC.

And I'll be happy to answer any questions.

MR. ELLIOTT: Thank you.

Any questions from the audience?

QUESTION: I have a question for the whole panel, and then, I have a question specifically for Alan. Alan, your question first: you said that you would support freezing plans like the airline industry that is in serious trouble. Would you support such a proposal for industries that have significantly underfunded plans?

MR. REUTHER: No, my reference was just to the airline industry. We would not support that being imposed on other industries. We think the way to address the situation in other industries is through the general funding reforms rather than imposing a freeze.

QUESTION: Okay; those of you who were around for the 1994 Pension Reform Act remember how difficult it was, and the industries that were targeted then, you see them coming back being a problem today. What guarantees do we have that after all of these things that we would go through at a legislative level that we are not going to be right back where we were, but we will have successfully driven healthy companies out of the system?

MR. KLEIN: Could folks hear the question? I'll just repeat it for the benefit of everyone. She said that back in 1994, we went through a similar exercise, and some of the same industries are coming back now, presenting the problem that's landing in our laps, and what guarantees are there that if Congress goes through this effort, that we won't find ourselves in a similar situation later, but in the meantime, we will have presumably inadvertently driven out a lot of healthy plans from the defined benefit systems? Is that a fair paraphrasing?

You know, it's a superb question, and I think it just harkens back to the point that I was making about the extent to which we accept the agency, the corporation, as a safety net, recognize the fact, I mean, we don't have any buggy whip manufacturers anymore, and we have undergone some extraordinary fundamental changes in the steel industry, in the airline industry; obviously, facing pressures from low-cost carriers and so forth.

It may be that, and other commentators from the prior panel made this point, that there may be limited options for dealing with the most troubled plans, and that the best that we can do is develop some rules that will help forestall the next one in another industry, because I don't see this sort of the same conditions at this point being in place with any other industry, so that's sort of the silver lining in the dark cloud.

And with the proper kinds of rules that would require companies to fund up their promises more quickly, to put some restrictions on the ability for there to be lump sums if a company plan falls below a certain threshold level, to fund for new promises that are made, to put some restrictions on new promises when a company is in a certain underfunded situation, then, maybe we can forestall the next steel industry problem.

MR. REUTHER: I'd say a couple things.

We do believe that funding reforms can be effective in at least reducing the number of plans out there that can present a serious problem in the future. And just as one example, if you go back a few years, the General Motors pension plan had a very large amount of underfunding. Since then, GM has contributed an enormous amount, and it's basically 100 percent funded now. So we think situations can change in the plans.

The other side of the coin, though, is there's no guarantees about other industries following in the footsteps of steel and airlines. And that gets back to it's a question of industrial policy for this country, and I would disagree with Jim: it's not a buggy whip question. You look at the auto industry. It's not that the production of autos is becoming obsolete like buggy whips. It is that this nation is allowing the production to be shifted to Mexico and China and Thailand.

And, you know, there's consequences if you allow that type of thing to continue.

MS. FRIEDMAN: And I guess all I would say is I wasn't around back in 1994, but I think it goes back to my point that whatever we do, we should be deliberative and not rush into any solutions right now. I think we need to take into account what the problems are and make sure that we develop rational solutions that aren't developed simply in the heat of the moment.

MR. ELLIOTT: One last question. Yes, sir, in the back?

QUESTION: Can you say something about cash balance plans?

MS. FRIEDMAN: Oh, good, thank you. I was wondering how I was going to get that in.

MR. ELLIOTT: You didn't plant him, did you?

MS. FRIEDMAN: We do agree with Jim and Alan, of course, that the defined benefit system is critical to employees. We were just talking yesterday about what kind of a world would we have in 20 years if we allow all of the DB plans to freeze or terminate; people are going to be left without adequate income.

Jim is taking the view in his statement that cash balance plans are the future of defined benefit plans, and from an employee's perspective, I think a lot of employees feel that cash balance plans for the future may be the right kind of plan for mobile workers. But first, we have to address the fundamental problems of cash balance plans.

They have been deemed unlawful. We consider them age discriminatory, and there's no question that there are problems in the transition from good traditional defined benefit plans to cash balance plans, where workers have lost up to 50 percent of benefits. We would be happy to engage in a dialogue to try to develop solutions for these issues.

MR. ELLIOTT: I think we have to give Jim two minutes, and then, let's cut it there.

MR. KLEIN: I will even take less than that, because we could really have a separate forum all on that. But I would just correct sort of one point: to say that these types of plans have been found unlawful, there's one District Court case that has found that plans, by their design, are inherently unlawful, as are other designs, I mean, because it's a fairly broad ruling.

Every other case that has looked to the specific legal question of whether or not these plans are legitimate plans in terms of not inherently age discriminatory has found the other way, and that one case from the Southern District of Illinois is going up on appeal as well, so I would, without letting this digress into a whole debate about cash balance plans, I would just want to correct that one point.

And to say that it is a question of whether companies will transition to that type of a defined benefit plan, because it is a defined benefit plan, or exit the system altogether, and I think it's a piece of the overall puzzle here.

MS. FRIEDMAN: The legal reasoning of the case is very sound, by the way, and they do violate age discrimination laws.

MR. ELLIOTT: Okay; I think that's a much longer discussion.

Anyway, thank you all, and thanks particularly to this panel.

[Applause.]

MR. ELLIOTT: And for those of you of a more technical bent who would like to stay, in about five minutes, I'll be happy to talk about the model with anybody who is still in the room.

Thank you again.

[Whereupon, at 4:14 p.m., the forum concluded.]