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PROPOSAL TO INCREASE PBGC PREMIUMS: MYTHS AND FACTS

The Administration has proposed to raise premiums payable to the Pension Benefit Guaranty Corporation (“PBGC”) by $16 billion over 10 years. This would be achieved partially by increasing the flat-rate premium and partially by giving the PBGC the right to set its own variable rate premiums and to base such premiums on factors that include the financial condition of the employer. Adoption of this proposal in whole or in part would substantially accelerate the decline of the defined benefit plan system and adversely affect job retention. Several myths about PBGC that have been raised during the policy debate are highlighted here.

MYTH: PBGC is in danger of a taxpayer bailout.

FACT: PBGC stated in a recent annual report: “[s]ince our obligations are paid out over decades, we have more than sufficient funds to pay benefits for the foreseeable future.” In fact, in a November 2011 report, PBGC concluded, based on 5,000 simulations, that the chances of its single employer program running out of money by 2020 were zero. Moreover, in a majority of the 5,000 simulations, PBGC’s financial position improved over the next 10 years.

MYTH: PBGC has a deficit of $26 billion.

FACT: There is no economic evidence to support PBGC’s reported $26 billion deficit. On the contrary, a study by a leading actuary concluded that 80% of PBGC’s deficit is attributable to the Fed’s actions in decreasing interest rates since 2008. The other 20% is attributable to the fact that PBGC uses an interest rate to value its liabilities that is even lower than today’s artificially low interest rates. In short, using a historically representative interest rate, PBGC has no deficit. In this context, there is no reason to impose new premium burdens on plans and plan sponsors.

MYTH: The proposed premium increases are modest and would not have a material effect on businesses.
FACT: In order to raise $16 billion, it is clear that a very large number of companies will have their PBGC premiums increased by 300% (the maximum increase under the Administration’s proposal). So for many very large plans, the annual additional cost would be tens of millions of dollars. That amount of money would have a clear effect on jobs.

MYTH: The proposed premium increases would not have any other adverse effects.

FACT: Aside from the significant effect on jobs described above, the premiums increase would have a severe unintended effect. Plans across the country are being advised that, if anything close to the Administration’s proposal is adopted, they should explore offering lump sums to their deferred vested participants and possibly even their retirees in order to save potentially tens of millions of dollars annually in PBGC premiums. Based on historical data, we would expect the overwhelming majority of individuals with new lump sum options to elect lump sums. The retirement security implications of this development should be considered. In addition, PBGC’s premium base would shrink dramatically. This could mean quadrupling premiums for far more companies in order to hit the $16 billion revenue target since there would be fewer participants in the base.

MYTH: The proposal would impose a premium, not a tax.

FACT: The proposal would clearly impose a tax. If we ignore the economic realities discussed above and assume that the PBGC’s has a $26 billion deficit, it is generally attributable to employers that no longer sponsor a pension plan. When one taxpayer is asked to pay expenses attributable to another taxpayer, that is a tax, not a premium. It is fair to ask defined benefit plan sponsors to pay the cost of the insurance protection they receive from the PBGC. But there has not been a hearing or other examination of the cost of the protection. Without such an examination, a $16 billion increase in PBGC premiums is a new tax on pension plan sponsors.

MYTH: The government would not be involved in evaluating companies under the Administration’s proposal.

FACT: By definition, the government would have to evaluate the financial condition of all companies, including public companies (since credit ratings are not used under the Administration’s proposal), private companies, and tax-exempt organizations.

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It is inappropriate to impose taxes on defined benefit plan sponsors plans that provide retirement security for millions of Americans without the facts about PBGC’s actual financial condition and a full examination of many important public policy issues.