
TIAA-CREF Investment Management

New Views of Defined Benefit Plans: Risks and Rewards for Plan Sponsors



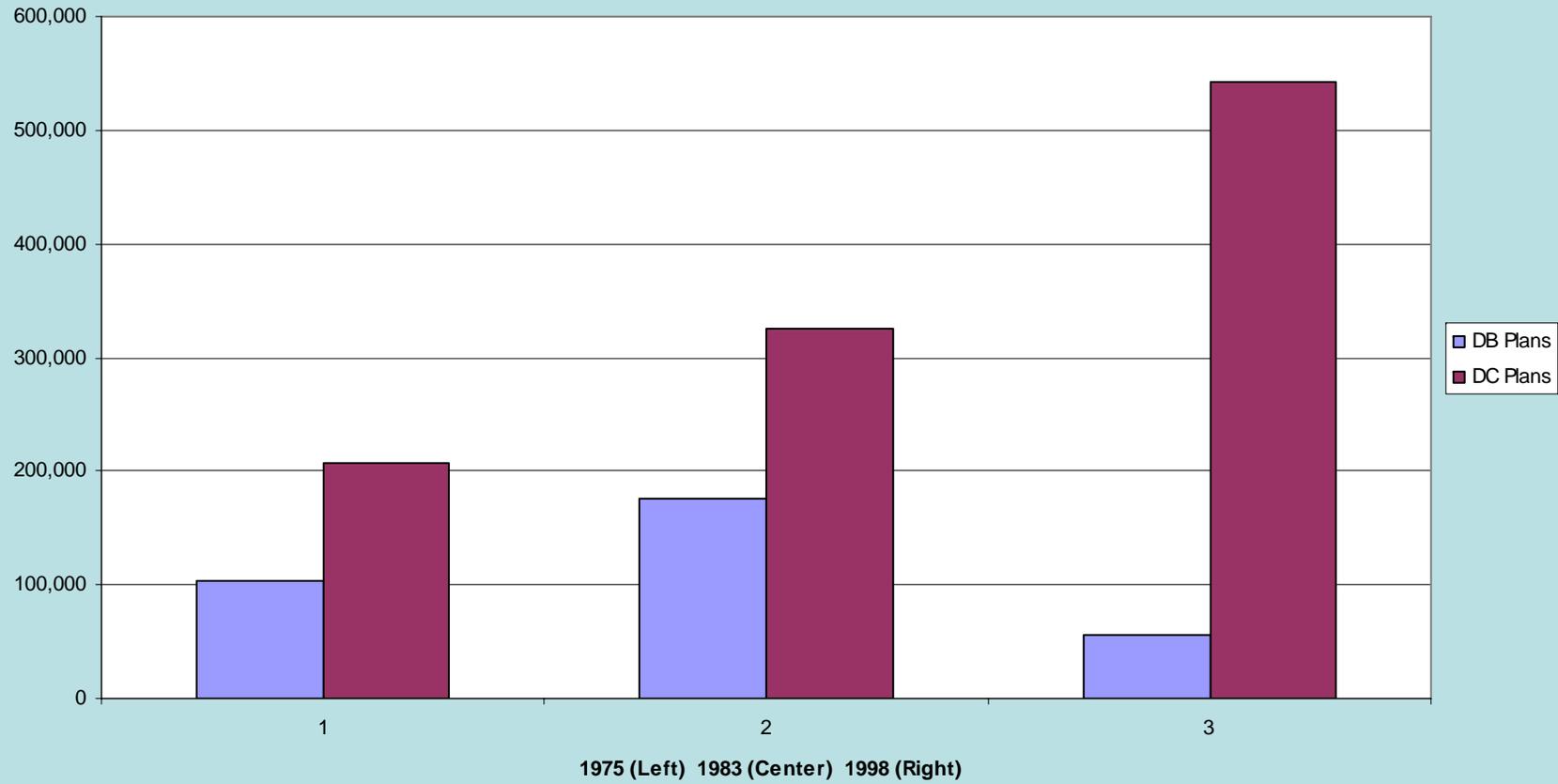
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Presentation Overview

- Private sector DB plan trends since the passage of ERISA.
- An overall look at problems of and prospects for DB plans.
- Major sources of systemic risk for DB plans.
- Proposed fixes from “easy” to “difficult.”
- A new paradigm for DB plans.



Figure 1: Numbers of Private DB and DC Plans



The Basic Assertions

- The DB plan is dying a slow, but perhaps accelerating death.
- The economics and politics of the DB plan may be working against it.
- The DB plan does have application for some modern workers.
- Aligning the accounting and regulation with the economics would help.
- A new DB paradigm could help more.



The View From 30,000 Feet

- DB plans have not evolved with the changes in the labor market and economy.
- DB plans in sectors deregulated and/or subject to globalization.
- Compliance costs keep increasing and plans become harder to price.
- Pension Put/Call problem.
- PBGC insurance not properly priced.



The Biggest Problems

- The “Perfect Storm” of falling equity prices and low interest rates.
- Truly awful accounting. FAS 132 is an improvement but FAS 87 has got to go.
- The multi-billion dollar deficit at the PBGC.
- PBGC’s problems also include: insurance pricing; credits; backward looking process.
- Economics of pension finance not applied.



Why Try to Fix the DB Pension?

- Collective interest in assuring lifetime individual financial security.
- Some people not interested in saving/managing investments.
- Forced saving, professional investment management, income option, and risk pooling all make economic sense.
- Especially if Social Security is moving toward a DC model.



Some Proposed Fixes

- Get the economics right, and the accounting will follow.
- Transition toward a marked-to-market framework for valuing assets and liabilities.
- Apply principles of insurance to the PBGC.
- Transition toward convergence with international standards.
- But these might not be enough...



A New Paradigm

- Approach based on the idea of portability.
- New DB plans to share common actuarial standards.
- New DB plans to share common benefit accrual rates.
- Individuals could purchase service credits in other plans and take credits with them.
- Payout formulas need not be standard.

