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TOWERS WATSON

Insider

Volume 20 | Number 4 | April 2010

Value at Risk for Pensions Expected to Decline for 2010, but Risks Remain High

After gradually working their way back up to full funding after some rough market conditions during portions of the last decade, pension plan sponsors are again facing an uphill funding challenge. The deteriorating economic conditions that took root in 2007 have increased the funding gap for pensions and caused stock values to plummet, sharpening concerns about the risks posed by these plans.

Over the past year, financial markets regained some lost ground, although stock prices remain significantly below their pre-financial-crisis levels. The improved stock market performance during 2009 boosted both pension funding levels and aggregate firm value. The investment risk to pensions has fallen slightly from last year, but pension risk remains a serious concern.

Towers Watson's Pension Risk Index

More than seven years ago, Towers Watson developed a measure of potential dollar-value decline in a pension plan's funded status relative to the market capitalization of the plan sponsor under a simulation of adverse financial market conditions. We quantify the additional risk imposed by a pension plan on a company's core finances over the next year by a value at risk (VaR) measure called the Pension Risk Index (PRI). The VaR is the dollar reduction in the pension fund's position under adverse financial market conditions given the plan's asset allocation and current funding positions.[1]

The adverse market VaR scenario is defined as having a 5% probability outcome and is calculated using Towers Watson's capital market assumptions and proprietary asset/liability modeling technology. The potential loss to the pension fund is then compared with the plan sponsor's market capitalization. For example, a PRI value of 4% implies that, given the company's current pension funding position and pension asset allocation, there is a 5% likelihood the pension fund will generate an additional deficit of 4% or more of the company's market capitalization over the coming year.

Measured by this metric, the risks posed by pension plans are estimated to have dropped slightly since last year but remain high. This year's marginally lower overall PRI values are mostly attributable to:

- The combined effect of continued large equity positions by pension funds with assumptions of lower volatility and better equity performance in 2010
- Larger increases in company market capitalization than in plan liabilities, although aggregate market capitalization remains well below pre-financial-crisis levels

PRI for the *Fortune* 1000 declines

Towers Watson has been calculating PRI values for *Fortune* 1000 companies for seven years.[2] Median PRI values decreased from 2.5% in 2009 to an estimated 2.1% in 2010. While this is an improvement, these values are still considerably higher than those from 2004 to 2008 (see **Figure 1**, next page).

Before the recent financial crisis, PRI scores remained in a relatively narrow spread, with median values ranging from 0.6% to 1%. From 2008 to 2009, PRI scores jumped significantly, driven primarily by increasing plan liabilities, declining firm values, and higher assumed volatility in equity returns and interest rates. Given the large equity positions still held by many plan sponsors, these conditions created pension funding shortfalls and pushed PRI scores much higher for 2009 (see **Figure 2**, page 3).

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[1] When creating 2010 PRI scores, we used projections for pension funding at year-end 2009 because actual funding data will not be available until later in 2010. For further details on these projections, please refer to "Strong Market Returns Boost Funding Levels of *Fortune* 1000 DB plans for 2009," *Insider*, January/February 2010. The PRI results for 2009 and 2010 are based on the sample of companies from this article so we could isolate the reasons for the decline in VaR scores over the last year.

[2] See *Watson Wyatt Insider,* March 2009, November/December 2008, October 2007 and July 2005.

Insider

Insider is a monthly newsletter developed and produced by the company's Research and Innovation Center.

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Figure 1. Median PRI scores for the *Fortune* 1000

Year	Median PRI value (percentage)
2004	**1.0**
2005	**0.9**
2006	**0.8**
2007	**0.6**
2008	**0.9**
2009	**2.5**
2010 (estimated)	**2.1**

Source: Towers Watson.

The distribution of PRI values has shifted appreciably over the last few years. In 2007, only 8% of companies had PRI values greater than 4%. Almost a third had PRI values greater than 1% and less than 4%, and 63% had values of 1% or less. By 2009, the tail ends of this distribution had shifted — only 28% of plan sponsors had PRI values of 1% or less.

In 2010, our projections are for 33% of plan sponsors to have PRI values of 1% or less and 30% to have values greater than 4%. While this compares very unfavorably with 2007 — when only 8% of companies had PRI values of 4% or higher — it is a step in the right direction from 2009, when values were that high for 33% of sponsors.

During 2009, equities began recovering their value. However, the discount rates used to measure pension liabilities declined, partially offsetting the beneficial impact of higher investment returns on funding. Nevertheless, most firms enjoyed modest increases in pension funding as their asset growth outpaced the growth in plan liabilities.[3]

The PRI scores for 2010 have generally declined slightly from 2009 levels, due to a couple of factors.

Adverse market conditions in 2009 left many companies with disproportionately large pension plans. Pension size is measured by the ratio of plan obligations to the plan sponsor's current market capitalization. Over the last year, market capitalization rose for 82% of companies in this analysis, although it remained well below pre-crisis levels. From year-end 2008 to year-end 2009, for all companies in this study, the median increase in market capitalization was roughly 29%. Higher market capitalization eclipsed the growth in plan obligations caused by lower discount rates, thus decreasing the pension size metric for sponsors.

At year-end 2008, the median pension size ratio for these companies was roughly 22%. Higher market values drove this ratio down to 18% in 2009. So for 2010, decreasing pension size plays a role in lower PRI scores. Even after controlling for asset allocation and current risk (total pension deficits over company market capitalization), a strong association between pension size and PRI scores persists. For every percentage-point increase in the pension size ratio, PRI scores increase by 0.13 percentage points.

The second factor driving the reduction in PRI scores is Towers Watson's capital market assumptions for 2010. Future market assumptions are slightly more optimistic than those for the prior year simulations (although less hopeful than those of two years ago). Returns in 2010, especially for equity markets, are expected to be slightly better, and volatility is anticipated to be lower (reflecting actual experience in the market) than last year's assumptions (see **Figure 3**, next page).

The slight decrease in volatility minimally reduces the range of potential outcomes such that the 5% probability outcome is producing slightly better results (fewer dollars at risk) than last year.

[3] See footnote 1.

Figure 2. Distribution of PRI values for the *Fortune* 1000 (percentages)

PRI value	2010 (estimated)	2009	2008	2007	2006	2005	2004
<=0.5	**18**	**15**	**38**	**44**	**40**	**37**	**33**
<=1.0	**15**	**13**	**16**	**19**	**20**	**20**	**18**
<=1.5	**10**	**8**	**11**	**7**	**8**	**7**	**9**
<=2.0	**6**	**8**	**6**	**7**	**8**	**9**	**8**
<=2.5	**7**	**6**	**5**	**4**	**4**	**5**	**3**
<=3.0	**5**	**5**	**3**	**4**	**5**	**4**	**5**
<=3.5	**5**	**6**	**3**	**2**	**2**	**3**	**4**
<=4.0	**4**	**6**	**4**	**4**	**3**	**3**	**2**
>4.0	**30**	**33**	**14**	**8**	**10**	**13**	**18**

Source: Towers Watson.

Figure 3. 2009 and 2010 Towers Watson's capital market assumptions: Assumed equity statistics, year one

Year	Assumed equity returns	Standard deviation of equity returns
2009	**8.6%**	**26.7%**
2010	**9.2%**	**24.6%**

Source: Towers Watson.

Figure 4. Median PRI values by industry*

*Values are shown for sectors with 10 or more observations.
Source: Towers Watson.

Asset allocations are an important factor in deriving the PRI measurement for 2010. Over the past years, sponsors have been gradually ramping down their equity allocations, but most companies still hold relatively large equity positions (at least in aggregate). The median allocation to equity for companies in this analysis is 60%.[4]

Large equity allocations can help reduce the cost of providing benefits in the long run — at the expense of taking on higher market risk and volatility. To get a sense of how this movement in equities can affect PRI scores, we ran two additional PRI scenarios to compare them with the current median of 2.1%.

In the first scenario, all companies decrease their equity percentage by 5 percentage points, and, concurrently, increase their investments in debt by 5 percentage points. Under this scenario, the median PRI score is 1.9%. In the second scenario, all companies increase their equity allocation by 5 percentage points and reduce their percentage in debt by 5 percentage points, which yields a median PRI value of 2.4%.

PRI values vary by industry classification

Transportation, communication and the automobiles/transportation equipment industries are estimated to have the highest PRI scores for 2010 (see **Figure 4**). In these firms, pensions are disproportionately large relative to firm value. This is not surprising, as many companies in these sectors have been in financial distress for a while now, and their plans have large legacy costs. Some of these firms have already frozen their plans.

[4] Asset allocation data used in this analysis are based on prior-year targets because actual funding data will not be available until later in 2010.

Conclusion

According to our analysis, the risk implied by a pension fund for a company's core finances — the PRI — has declined since 2009. Higher assumed equity returns for 2010 and rising firm market capitalization gave PRI scores a boost over the last year, despite the continuing growth of pension obligations.

While the decrease in VaR is good news, companies still face more investment risk than in previous years. For some companies, these higher levels of risk suggest the possibility of disturbances in their core business if the economy's rebound falters and another financial storm hits.

News in Brief

Supreme Court Declines to Review NRA Based on Service

The U.S. Supreme Court has declined to review a federal appeals court's 2009 decision allowing pension plan sponsors to define normal retirement age (NRA) by a period of service rather than a specific age.

The decision might be helpful for cash balance plans with a service-based NRA that are challenged on distributions occurring before the effective date of the final regulations.

Under IRS regulations that took effect in 2007, a plan's NRA may not be younger than the typical retirement age in the sponsor's industry. Notice 2007-69, issued in connection with these regulations, states that a plan in which a participant's NRA changes to an earlier date after some period of service typically will not satisfy the vesting or accrual rules of IRC section 411(b).

A plan sponsor might want to define NRA as much younger than the typical retirement age for several reasons. For lump-sum distributions from cash balance plans before enactment of the Pension Protection Act (Aug. 17, 2006), having a younger NRA enabled plans to avoid the whipsaw calculation. The whipsaw calculation projected a participant's cash balance account to NRA using the plan's interest crediting rate, and then discounted it back to the participant's current age using a rate specified by law. If the plan's interest crediting rate was more generous than the rate specified by law, the lump sum was bigger than the cash balance account.

In *Fry v. Exelon,* the 7th Circuit case at issue, Exelon's cash balance plan defined NRA as the earlier of (1) five years of service or (2) age 65 or the participant's fifth anniversary of participation, whichever came later. Under that definition, every vested participant had attained NRA, and the Exelon plan did not have to perform the whipsaw calculation to determine lump-sum distributions.

The plaintiffs claimed that this definition violated the Employee Retirement Income Security Act (ERISA) and that a plan must define NRA by age rather than a period of service. But the court determined that, because both ERISA and the tax code define NRA by referencing "the *time* a participant attains normal retirement age under the plan" [emphasis added], plans were allowed to define NRA as a specific age, a period of service or participation, or a combination of age and service/participation.

While neither the *Fry v. Exelon* decision nor the Supreme Court's refusal to hear the case negates the IRS regulations, the decision might be helpful for cash balance plans with a service-based NRA that are challenged on distributions occurring before the effective date of the final regulations.

The Supreme Court's declining to review the case does not necessarily mean it agrees with the lower court's decision. In *Laurent v. PriceWaterhouseCoopers* in 2006, the U.S. federal District Court for the Southern District of New York held that a plan must define NRA by reference to a specified age, not a period of service. *Laurent* is not yet on appeal to the 2nd Circuit, but motions continue to be filed in that case, so the story is not necessarily over.

EEOC Proposes Rule on Age Discrimination Defense

The Equal Employment Opportunity Commission (EEOC) has proposed a rule to provide guidance on the meaning of "reasonable factors other than age" (RFOA) under the Age Discrimination in Employment Act (ADEA). The RFOA defense is one of several ADEA affirmative defenses and is particularly important to employers facing an allegation that a seemingly neutral employment action or policy had a disparate impact on older employees.

The proposed rule lists factors to consider in determining whether an employer's actions were "reasonable" and based on "factors other than age."

Background

The ADEA prohibits employers with 20 or more employees from discriminating on the basis of age against employees aged 40 and older. The law's protections extend to all terms and conditions of employment, including hiring, promotion and employment termination decisions, along with compensation programs and employee benefit plans.

In 2005, the U.S. Supreme Court ruled in *Smith v. City of Jackson* that a seemingly neutral policy or action that disproportionately affected older employees could violate the ADEA — a "disparate impact" violation. However, the court also recognized that such a policy or action is not discriminatory if it is based on RFOA. The test, according to the court, is not whether the employer's actions were a matter of business necessity, i.e., the only way to achieve its goals, but rather whether they were a *reasonable* means of achieving the employer's business goals.

In 2008, the Supreme Court ruled in *Meacham v. Knolls Atomic Power Laboratory* that in a disparate impact lawsuit under the ADEA, the burden of proof with respect to the RFOA defense falls on the employer, which made disparate impact lawsuits more difficult and costly for employers to defend. The EEOC's proposal responds to these court cases and to public comments requesting more information on the meaning of "reasonable factors other than age."

Factors for evaluating RFOA defense

In addition to emphasizing the necessity of a case-by-case approach to evaluating an employment practice, the proposed rule provides nonexhaustive lists of factors relevant to whether an employment practice would be considered reasonable and based on factors other than age.

According to the EEOC, a practice is reasonable if a prudent employer mindful of its ADEA responsibilities would consider it so. An employer must show the employment practice in question was both reasonably designed to further or achieve a legitimate business purpose, and administered so as to reasonably achieve that purpose.

A practice is reasonable if a prudent employer mindful of its ADEA responsibilities would consider it so.

It might be reasonable, for example, to take job performance and skill sets into account when making layoff decisions. It also could be reasonable to consider whether a worker has critical skills or is flexible, such as being able to work on different assignments or acquire new skills. These considerations would be considered reasonable under the ADEA as long as the employer:

- Makes reasonable efforts to administer its employment practice accurately and fairly
- Assesses the age-based impact of the practice
- Takes steps to ameliorate unnecessary and avoidable harm, such as training managers to avoid age-based stereotyping and identifying knowledge or skills that the employer needs to retain

The determination of reasonableness also requires consideration of what the employer knew or should have known about the effect of the challenged practice, according to the EEOC. If the employer had no reason to expect an age-based adverse impact, it cannot be expected to have taken any ameliorating action; however, employers are expected to evaluate their processes with an eye to whether they adversely affect older workers disproportionately.

To assess whether an employment practice satisfies the RFOA defense, the proposed regulation lists the following factors:

- Whether the employment practice and the manner of its implementation are common business practices
- How closely the factor relates to the employer's stated business goal

The EEOC's lists of factors can help employers evaluate the defensibility of their policies and practices.

- Whether the employer took steps to define the factor accurately and to apply the factor fairly and accurately (such as providing training, guidance and instruction to managers)
- The extent to which the employer assessed the adverse impact of its employment practice on older workers
- The severity of the harm to workers aged 40 and older, in terms of both the degree of injury and the number of workers adversely affected, and the extent to which the employer took reasonable preventive or corrective steps to minimize the damage
- Whether other options were available and the reasons the employer selected the option it did

The EEOC says that, while employers are not required to adopt the practice with the least impact on workers aged 40 and older, their knowledge of — but failure to use — equally effective but less discriminatory alternatives is relevant to whether a practice is reasonable.

The importance of various factors would vary according to the employer's facts and circumstances, and the list is not exhaustive; employers could cite other factors relevant to whether a practice is reasonable, according to the EEOC.

Non-age-related factors

In a typical disparate impact case, the practice is based on an objective non-age-related factor, and the only issue is whether the practice is reasonable. In its proposed rule, the EEOC also anticipates situations involving a disparate impact arising from giving supervisors unchecked discretion to engage in subjective decision making. In that case, an impact may be impermissibly based on age because the decision maker acted out of conscious or unconscious age-based stereotypes.

To assess whether an employment practice is based on a non-age-related factor, the proposed regulation would consider the following factors:

- Whether the employer gave supervisors unchecked discretion to assess employees subjectively
- Whether supervisors were asked to evaluate employees based on factors associated with age-based stereotypes
- Whether supervisors received guidance or training on avoiding age discrimination

The EEOC cites "flexibility" as an example of a criterion often subject to age-based stereotyping and advises employers to give supervisors guidance on measuring flexibility objectively. For example, instead of asking supervisors to rate employees' willingness to take on new tasks, employers should instruct supervisors to describe how employees responded when asked to perform new tasks.

An RFOA defense does not require that all the "non-age" factors be present, and the importance of various factors will vary according to the facts and circumstances. The EEOC notes that the list is nonexhaustive, so employers may present other relevant factors.

Implications

The uncertainty facing employers going forward is being able to prove they based their employment decisions, compensation policies and benefit programs on reasonable non-age-related factors. A reasonableness standard is, by definition, subjective, and different courts might evaluate the factors differently.

This emphasizes the importance of the EEOC's proposed rule to the RFOA defense. The Supreme Court has articulated a test for determining whether courts must defer to a federal agency's interpretation of a statute — even one that differs from the court's interpretation. That test requires such deference if the statute is ambiguous on the matter at issue and the agency's interpretation is reasonable. As a result, many courts are likely to defer to the EEOC's regulatory interpretation of the RFOA defense; thus, the EEOC's guidance gives employers an idea of the level of proof they are likely to need to successfully defend an ADEA claim. And the EEOC's lists of factors can help employers evaluate the defensibility of their policies and practices.

Employers should be particularly vigilant in reviewing the age-related implications of their HR polices, including hiring, promotion, termination, compensation and employee benefit plans (particularly age-sensitive programs). When facially neutral policies or decisions have a disparate impact on older employees, the RFOA defense could play a crucial role in helping avoid liability. In this regard, employers should consider evaluating the legal defensibility of their employment policies and benefit plans before implementation, if possible, to minimize their risk of ADEA liability.

TW Pension 100: 2009 Disclosures of Funding, Discount Rates, Asset Allocations And Contributions

During 2009, the aggregate funding ratio[1] for the largest U.S. pension plans increased by 4 percentage points — from 78% to 82%, according to Towers Watson calculations. Our results are based on just-reported pension disclosures from the Securities and Exchange Commission (SEC) 10-K filings of the 100 largest publicly traded U.S. pension sponsors with year-end 2009 fiscal dates.[2] This article examines reported funding results at year-end 2009, the discount rate assumptions used to measure liabilities, target asset allocation policies, and plan contributions made for 2009 as well as those expected for 2010.

Actual year-end funding status

Among these 100 companies, between 2008 and 2009, pension plan assets increased by 12%, plan liabilities grew by 7% and the pension deficit shrank from $209.6 billion to $183.5 billion — a modest funding gain of roughly $26 billion over the year (as shown in **Figure 1**). While the aggregate funding picture has improved somewhat for 2009, funding status has declined by $277 billion since 2007 for companies in this analysis.[3]

Figure 1. Aggregate funding status for top 100 pensions

(n=100; $ billions)

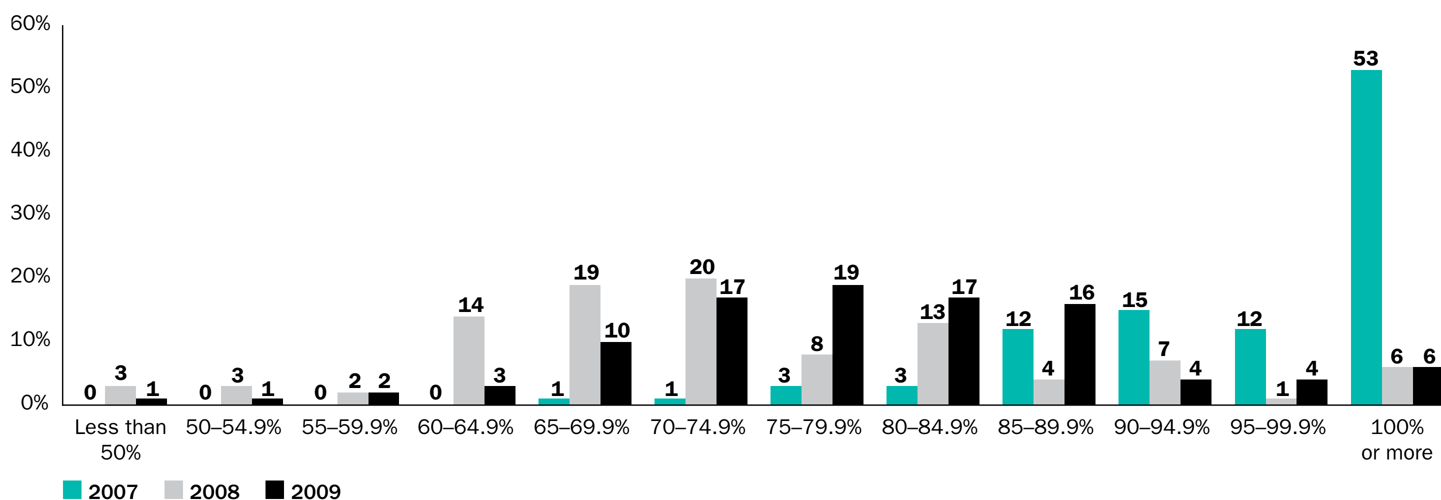
Year ending	PBO	Plan assets	Surplus/ (deficit)
12/31/2007	$946.7	$1,040.1	$93.4
12/31/2008	$977.7	$768.1	($209.6)
12/31/2009	$1,046.5	$863.0	($183.5)

Source: Towers Watson.

At year-end 2009, the average funding ratio (unweighted) for the Towers Watson 100 was 81%, compared with 75% at year-end 2008. **Figure 2** shows the increase in the distribution of funding ratios.

Figure 2. Distribution of funding ratios for top 100 pensions

Funding ratio percentages by percentage of sample (12/31/07–12/31/09)



Source: Towers Watson.

[1] The funding ratio is the sum of plan assets over the sum of projected benefit obligations (PBO).

[2] The Towers Watson 100 consists of the 100 largest U.S. pension sponsors among U.S. publicly traded organizations, ranked by PBO at year-end 2008. For some companies, the allocation of disclosed PBO and assets between U.S. and non-U.S. plans is estimated.

[3] On a global basis, aggregate funding results for these companies are similar to those mentioned above. For all pensions, domestic and foreign, the total PBO increased from $1.18 trillion at year-end 2008 to $1.29 trillion by year-end 2009. Global pension assets for these companies also increased from $916 billion in 2008 to $1.05 trillion by year-end 2009. So on a global basis, the pension deficit dropped from $269 billion to $239 billion, and aggregate funded status rose from 77% to 81% by the end of 2009.

The percentage of companies in this analysis with funding ratios lower than 70% fell significantly, from 41% at year-end 2008 to 17% in 2009. The percentage of these companies with funding ratios between 70% and 90% jumped from 45% at year-end 2008 to 69% for 2009. In both 2008 and 2009, 14% of these companies had funding ratios of 90% or more.

Not all companies in this analysis realized a gain in their pension funding. Funding status declined for 20 of these plan sponsors, although the declines were generally modest: Only five companies lost more than 5 percentage points.

The percentage of companies in this analysis with funding ratios lower than 70% fell significantly, from 41% at year-end 2008 to 17% in 2009.

Discount rate assumptions

Over the last year, the growth of plan obligations mitigated the strong asset gains. Some of this increase arose from using lower interest rate assumptions to measure plan liabilities. While discount rates for year-end accounting purposes rose from 6.29% at year-end 2007 to 6.38% at year-end 2008, they had declined to 5.92% by year-end 2009 (see **Figure 3**).

Target asset allocations

During 2009, plan assets increased by 12% among the 100 largest pensions, mostly due to strong equity market returns and some help from plan contributions (as discussed later). At year-end 2009, aggregate investment returns were 16%, and the average (unweighted) realized rate of returns on plan investments was 18%.[4] In 2008, these same companies had realized an average rate of return on plan investments of –24%. Companies' 2009 target allocations remained heavily geared toward equities.

We analyzed asset allocation strategies in 85 companies that provided target allocation data for both 2009 and 2010 (as shown in **Figure 4**).[5]

Over the last year, average target asset allocation policies for companies continued their incremental shift toward less investment risk, that is, a slight movement away from equities. While most plan sponsors did not change their policy over the last year, a few undertook large shifts in their asset allocation strategies. During 2009, 16 companies reduced their target allocation in equities by more than 7%, and three plan sponsors increased their target exposure to equities by more than 7%.

Figure 3. Discount rate assumptions for top 100 pensions, average discount rate

(n= 100)

Year ending	Average discount rate
12/31/2007	**6.29%**
12/31/2008	**6.38%**
12/31/2009	**5.92%**

Source: Towers Watson.

Employer contributions to pensions

As mentioned above, the value of plan assets increased significantly due to strong market returns. And sponsors' aggregate plan contributions surpassed annual benefit accruals, which also helped reduce overall funding deficits. Aggregate contributions for this group were $30.8 billion in 2009, while service cost (benefits earned over the prior year) was $17.0 billion.[6]

Some plan sponsors made contributions in excess of benefits earned in the last year to improve their funding levels. The average (unweighted) contribution-to-service-cost ratio for companies in this analysis was 3.36 (median 1.73). For the 20 companies whose funding levels declined over the last year, however, the average contribution-to-service-cost ratio was only 0.76 (median 0.61).

For many sponsors, higher minimum required contributions aren't due until 2011 and 2012 (the 2010 and 2011 plan years) because of regulatory and legislative relief granted in the past year.[7] It is difficult to reconcile reported planned contributions with minimum required contributions because of

Figure 4. Average target asset allocation percentages for top 100 pensions

(n=85)

Target allocations	Equity	Debt	Cash	Real estate	Other
2009	**55.1**	**33.4**	**0.2**	**3.5**	**7.8**
2010	**52.8**	**34.9**	**0.6**	**3.4**	**8.3**

Source: Towers Watson.

[4] While investment returns on assets were 16% and cash contributions were much larger than benefits accrued during 2009, plan assets grew by only 12% due to large benefit payouts. Companies in this analysis, in aggregate, paid out $63.2 billion in benefits during 2009.

[5] Target allocation information is usually depicted in ranges in pension disclosures. For purposes of this study, an average of the ranges was taken and results were normalized to equal 100%.

[6] Three firms were missing data on expected contributions for 2010 and so were dropped from the analysis of plan contributions.

[7] See "DB Plans Still Face Sizable Funding Obligations Despite Market Run-Up in 2009," *Insider,* March 2010.

the inclusion of supplemental executive retirement plans, which are exempt from funding requirements, in the disclosures.[8] Moreover, some companies contribute more or less than they planned. Reported planned contributions for 2010 are essentially in line with benefit accrual levels. **Figure 5** shows actual contributions for 2008 and 2009 and expected contributions for 2010.

Figure 5. Actual and expected plan contributions by employers for top 100 pensions

(n=97; billions)

Plan year	Contribution amount
Actual 2008	**$15.6**
Actual 2009	**$30.8**
Expected 2010	**$19.6**

Source: Towers Watson.

Conclusion

While declining interest rates have played a role in increasing pension plan liabilities, strong asset returns and contributions larger than benefit accruals have eased deficits and resulted in modest funding status gains for 2009. Funding on an aggregate basis increased from 78% in 2008 to 82% at year-end 2009.

These companies' pension deficits fell from roughly $210 billion in 2008 to almost $184 billion at year-end 2009. While that is good news, the aggregate pension deficit for companies in this analysis is still quite large. To provide a somewhat longer-term perspective, these same firms had a $93 billion pension surplus in 2007. While plan funding has improved for 2009, a return to full funding health is still likely to take some time.

These companies' pension deficits fell from roughly $210 billion in 2008 to almost $184 billion at year-end 2009. These same firms had a $93 billion pension surplus in 2007.

[8] In the footnotes of the 10-K SEC filings, the PBO includes nonqualified benefit plans, which are typically unfunded. This pushes pension liabilities up while adding nothing to assets, suggesting that our measure of funding is a lower bound for purposes of understanding the funding status of plans subject to legal minimum contribution requirements. Moreover, the PBO includes increases in the value of benefits arising from projected salary increases. Many observers believe the accumulated benefit obligation (ABO), which does not project salary increases, more accurately approximates the liability measure used in calculating minimum funding contributions. ABO funding ratios are generally about 7 percentage points higher than PBO funding ratios. So the funding shortfalls we have shown here, based on financial accounting, are certainly larger than those relevant to legal contribution requirements; timing of contributions, moreover, is subject to a complex interplay of legal and business considerations.

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TW-NA-2010-16151