

Terminated Vested Lump Sum Offerings

A Discussion With the MidWest Pension Conference

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Topics for Today's Discussion

- Overview
- The “Go, No-Go Decision”
- The Implementation Process
- Questions

Is a lump sum offer right for your company....

THE “GO, NO-GO DECISION”

Lump Sum Feasibility Considerations

1 Financial Implications

- Impact on cash requirements, PPA funding thresholds and remaining funded status
- Risk / Return trade-off of lump sums vs. other alternatives
- Impact on PBGC premiums and future administrative expenses
- Accounting charges, ongoing accounting impact

2 Philosophical View of Lump Sums

- Perspective on allowing participants to take DB annuity as lump sum
- Concern about shifting investment risk away from sponsor to participants
- Viewpoint on managing the cost/risk vs. transferring it

3 Groups to Include and design

- Process to determine groups based on financial metrics (settlement, PPA, etc)
- Inclusion of early retirement subsidies
- Inclusion of union populations
- Window approach vs. ongoing option to plan participants

4 Data Quality and Benefit Calculations

- Status of terminated vested benefits (missing participants, data quality, calculations)
- Non-traditional situations (QDRO, death, previous annuity contracts, etc.)
- Administrative process (QJSA, spousal waiver, etc.)

5 Participant Communications

- Strategy for connecting desired outcome to communication plan
- Key communication issues (relative value, timing, groups)

Business Case for Lump Sum Offering

Advantages of Lump Sum Offer

- Reduce pension plan's size and risk profile
- Some measures of funded status may improve due to paying lump sums (see disadvantages)
- Lock in cost to provide benefits at corporate bonds rates
- Reduction in volatility of pension results is beneficial in pessimistic market conditions
- Reduction in PBGC premiums and on-going administration fees
- Focused effort can result in more efficient processing of TV elections
- Settlement accounting may be viewed as favorable or neutral (specific to each company)

Disadvantages of Lump Sum Offer

- Some measures of funded status may decline due to paying lump sums (see advantages)
- Expected to reduce ongoing pension expense (under current accounting rules)
- May result in slight increase in cost over long-term due to equity risk trade-off
- Reduction in volatility of pension results means upside potential not as significant
- Could result in significant settlement accounting; results will be variable based on market-based discount rates at time of payout
- Will require fairly significant administrative effort to prepare data, calculations, and fulfill elections

Current Marketplace

Issues that influence whether or not organizations are taking action

	Why?	Why NOT?
Plan Financial Position	Plan is well funded, exposing sponsor to more downside risk than upside potential	Plan is poorly funded and not in a position to be able to act
	and/or	and/or
Business Financial Position	Organization has the financial ability to take material action	Organization does not have the ability to take material action
	and/or	and/or
Marketplace Views	Neutral/negative bias on future conditions	Positive bias on future conditions
	and/or	and/or
Operational Readiness	Operationally prepared or actively preparing	Not operationally prepared

Temporary Versus Permanent Feature

1. Should the ability to take a lump sum be provided for a limited period of time (a “window”) or...

2....should terminated vested participants be allowed to elect a lump sum at any time (permanent feature)?

Considerations:

- Providing a window may create a sense of urgency
- A window allows more control over timing of elections
- May lose the opportunity to settle the liability for participants that miss the window
- How do you treat participants who make benefit elections prior to communicating the offering, but after the decision has been made to offer the lump sum window?
- Practice of offering repeated lump sum windows could be viewed as a permanent feature under 411(d)(6) of the Internal Revenue Code

Lump Sum Economics in 2012

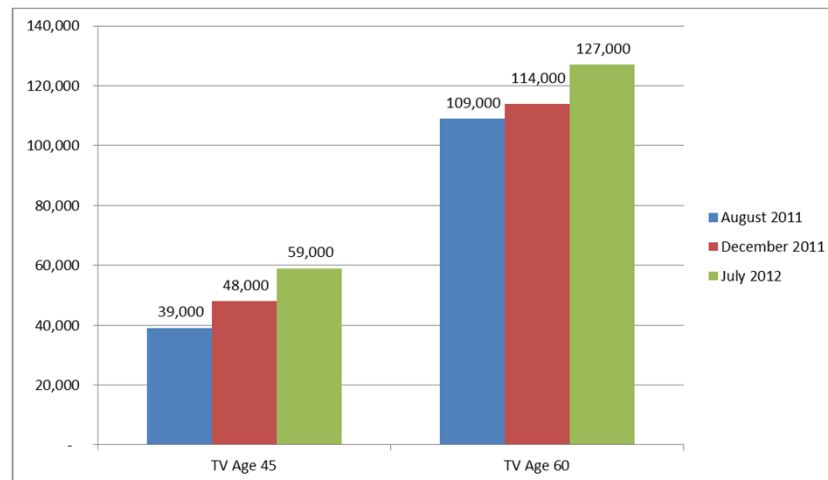
- Many plans reset interest rates on an annual basis, using a permitted “look-back” to a date up to five months prior to the start of the year
- Due to declines in interest rates since August 2011, many companies could offer lump sums in 2012 on a favorable basis (i.e., relative to financial statement liabilities)
 - Financial statement discount rates roughly 4.0% or lower as of August 31, 2012
 - Potential for interest rate arbitrage; TV lump sums could be 5% - 20% lower
- Value of accelerated lump sum windows will vary with market rates; companies that are prepared are in a position to take advantage of opportunities
- Paying lump sums also reduces PBGC premiums and on-going administration costs

Estimated Lump Sum Rates Payable in 2012*

Look-back Month	Terminated Vested Age 45	Terminated Vested Age 60
August 2011	6.02%	5.08%
September 2011	5.80%	4.93%
October 2011	5.50%	4.88%
November 2011	5.26%	4.75%
December 2011	5.24%	4.73%
June 2012 Rates	4.50%	3.97%

* Lump sum determine based on present value of age 65 benefit

Illustrative 2012 Lump Sum Values



Significant Market Activity*

Type	Action	Ford	GM
Plan Design	Plans Closed to New Entrants	Yes	Yes
	Ongoing Benefit Accruals Frozen	No	Yes
Asset Based	Liability Driven Investment (LDI) Strategy	Yes	Yes
Settlement Based	Prospective Lump Sum Option	Yes	Yes
	TV One-Time Lump Sum Offer	Yes (~30,000)	No
	Retiree Lump Sum Offer	Yes (~66,000)	Yes (~42,000)
	Retiree Annuity Purchase	No	Yes (~100,000)
	Estimated Liabilities Settled	\$5B	\$26B
	Settlement Date	End of 2013	End of 2012

* All data provided based on publically available information

After the decision has been made....

THE IMPLEMENTATION PROCESS

Towers Watson's Recent Experience

Client	Eligible Population	Take Rate	Total LS Distribution	Total Calls
A	1,500	60%	\$11M	2,400
B ¹	400/300	86%/43%	\$20M	N/A ⁵
C ²	2,100/800	63%/100%	\$13M	1,500
D	3,800	60%	\$90M	5,000
E ³	2,500/1,900	50%/35%	\$65M	5,500
F ⁴	1,000	95%	\$10M	1,300 ⁵
G	14,000	100%(<5k)	\$39M	2,200
H	5,000	100%(<5k)	\$18M	3,600 ⁵
I	680	42%	\$14M	1,150 ⁶
J	954	45%	\$18M	648
K	18,500	100%(<5k)	N/A	N/A
	53,434	57%(>5k) 100%(<5k)	\$298M+	23,298+

1. Two separate offerings

2. 2,100 for "window", 800 <\$5K

3. 2,500 for "window", 1,900 for "reminder"

4. Divestiture of active employees

5. Taken by client

6. Proactive calls made to participants

- Remaining calendar 2012 engagements, YTD, include over 70 additional plan sponsors and ~450,000 eligible vested terminated participants and retirees

Towers Watson's Insights



Lessons learned

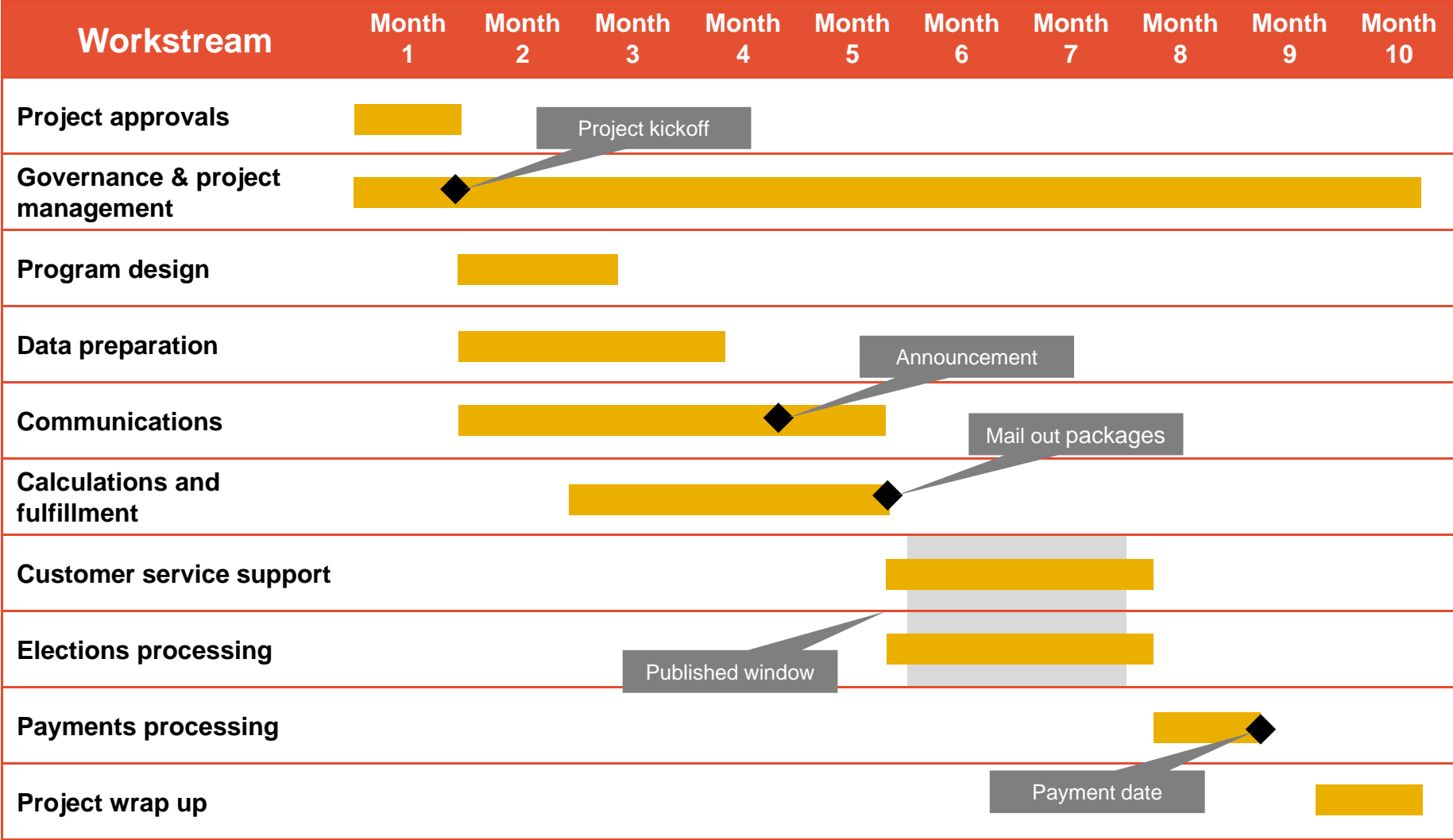
- ✓ You can't pay who you can't find
 - Current address data supports success
- ✓ Communication influences results
 - Early, repeatedly, multi-channel
 - Address all interested parties
- ✓ Make elections as easy as possible
 - Simplify complex election forms
 - Limit proof requirements and other obstacles
- ✓ Manage eligibility for maximum impact
- ✓ Plan like it's an open enrollment
 - Coordinate with other corporate activities
 - Expect high volumes; provision for peaks
 - Activity will skew towards end dates
 - Issue confirmations as quickly as possible
 - Expect high election error rates; processing requires care



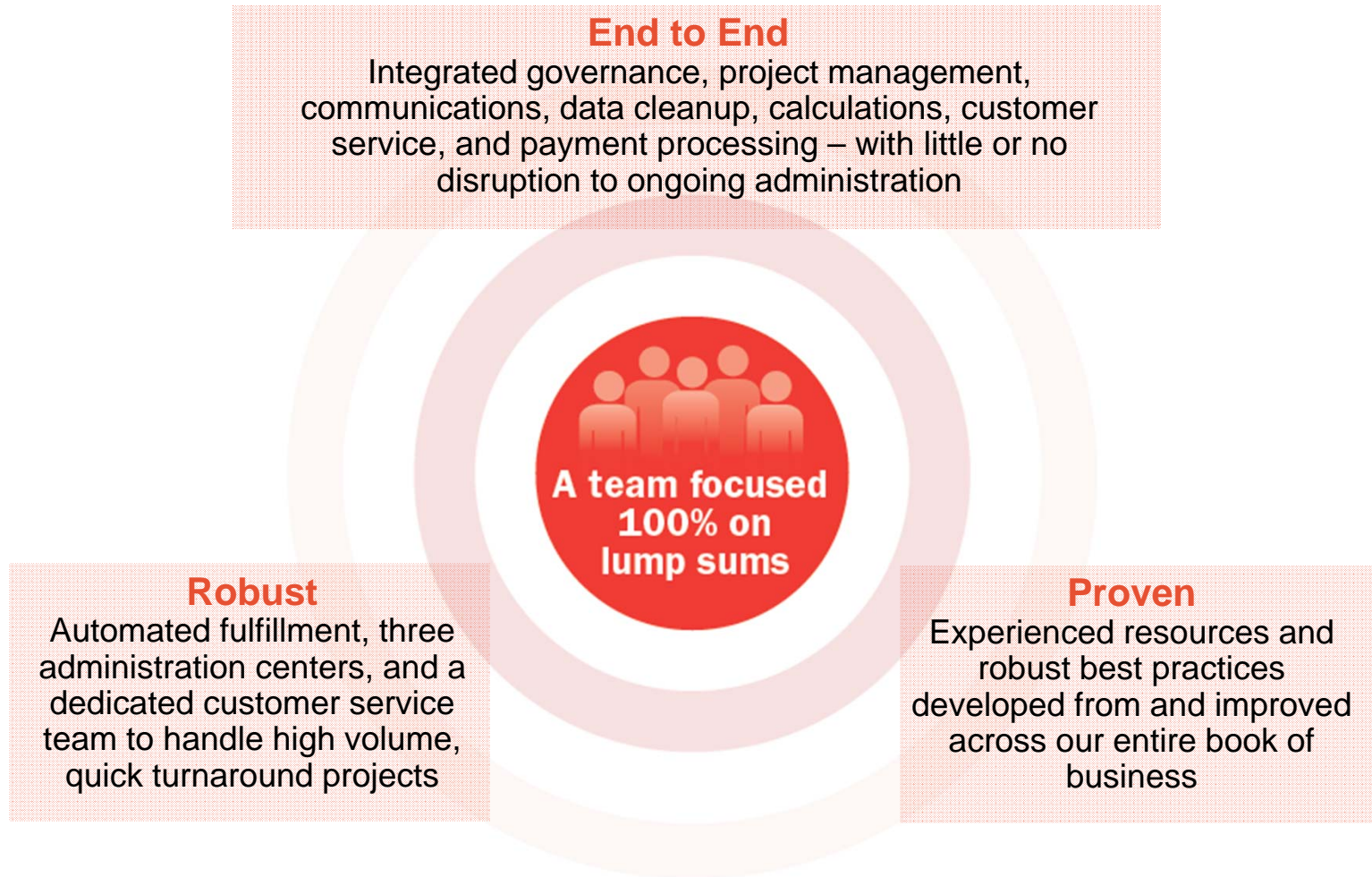
Key considerations

- ? Data readiness
 - Addresses
 - Benefit calculations
- ? Program design
 - Eligibles, special participant types
 - Treatment of subsidies and incentives
- ? Communications
 - Audience(s), objectives and tactics
- ? Division of labor
- ? Project wrap-up
 - Treatment of annuity elections
 - Treatment of late elections
 - Retention of notifications, kits, elections and cases
 - Reporting requirements

Sample Project Timeline

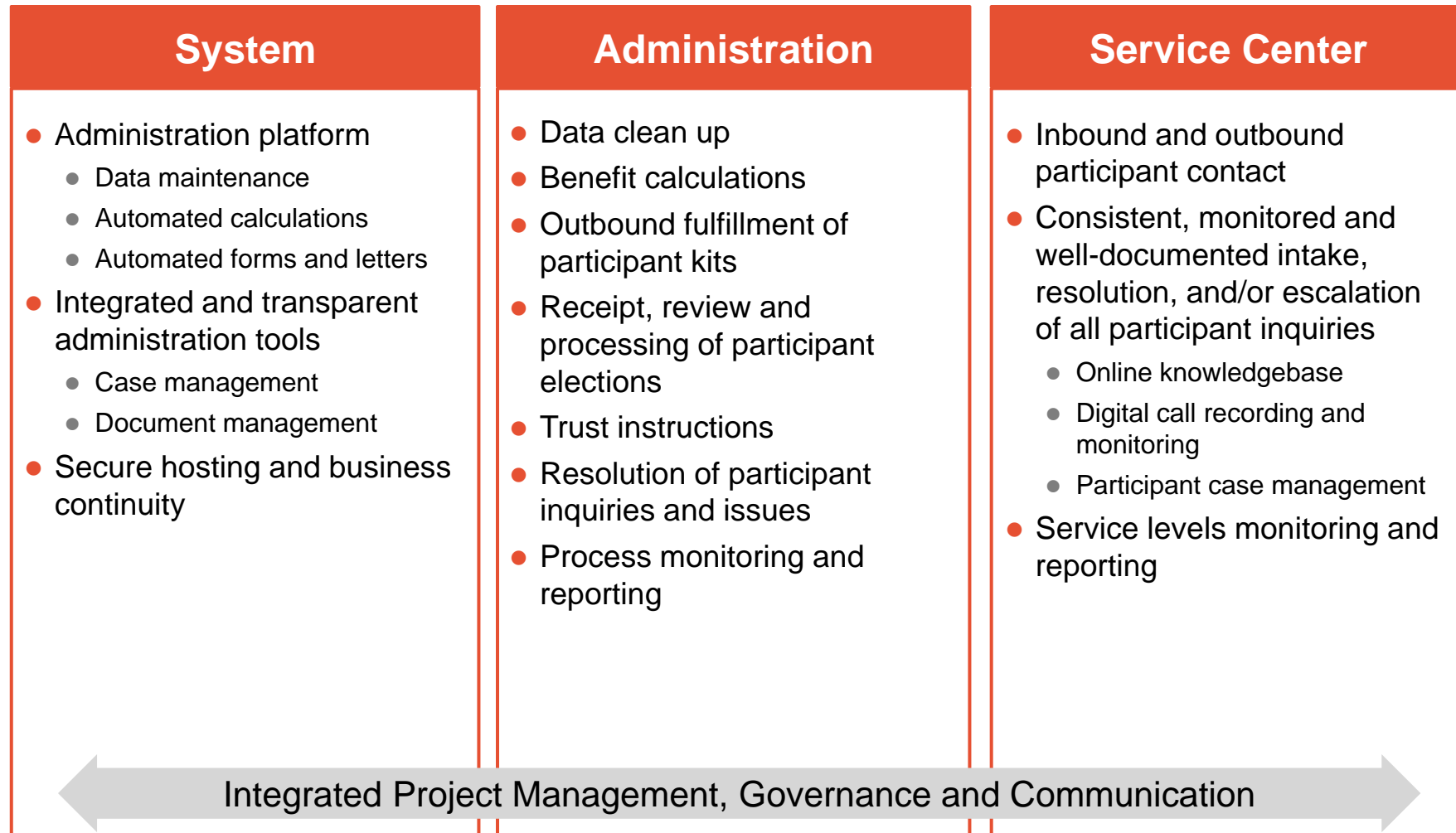


Towers Watson's Approach



Dedicated. Nimble. Effective.

Our Flexible Delivery Model



Questions

