United States General Accounting Office

GAO

Report to the Congress

May 1994

FINANCIAL AUDIT

Pension Benefit Guaranty Corporation's 1993 and 1992 Financial Statements

GAO/AIMD-94-109

GAO

United States
General Accounting Office
Washington, D.C. 20548

151691

Comptroller General
of the United States

B-164292

May 4, 1994

To the President of the Senate and the
Speaker of the House of Representatives

This report presents our opinion on the financial statements of the Single-Employer Fund and the Multiemployer Fund for the fiscal years ended September 30, 1993 and 1992. These financial statements are the responsibility of the Pension Benefit Guaranty Corporation, the administrator of the funds. Because of the Corporation's continuing progress in improving internal controls, we were able, for the first time, to opine on each of the Corporation's financial statements for fiscal year 1993. Although material internal control weaknesses continue to affect both funds, the Corporation is working to resolve them. This report also includes our recommendations to improve the Corporation's internal control structure and discusses our continuing concerns about the long-term viability of the Single-Employer Fund and weaknesses in employee benefit plan audits and reports.

We conducted our audit pursuant to the provisions of 31 U.S.C. 9105, as amended, and in accordance with generally accepted government auditing standards.

We are sending copies of this report to the Chairmen and Ranking Minority Members of the Senate Committee on Governmental Affairs; the House Committee on Government Operations; and the Subcommittee on Oversight, House Committee on Ways and Means. We are also sending copies to the Secretaries of Labor, the Treasury, and Commerce in their capacities as Chairman and members of the Board of Directors of the Pension Benefit Guaranty Corporation; the Corporation's Executive Director; the Director of the Office of Management and Budget; and other interested parties.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

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Abbreviations

ERISA	Employee Retirement Income Security Act
GAO	General Accounting Office
PC	personal computer
PLUS	Pension and Lump Sum

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To the Board of Directors
Pension Benefit Guaranty Corporation

We have audited the accompanying statements of financial condition as of September 30, 1993 and 1992, of the Single-Employer and Multiemployer Funds administered by the Pension Benefit Guaranty Corporation, and the related statements of operations and changes in equity and statements of cash flows for the fiscal year ended September 30, 1993. We did not audit the Corporation's statements of operations and changes in equity and statements of cash flows for the fiscal year ended September 30, 1992, and, accordingly, we do not express an opinion on them. We found the following:

- The statements of financial condition as of September 30, 1993 and 1992, and the statements of operations and changes in equity and statements of cash flows for the fiscal year ended September 30, 1993, were reliable in all material respects.
- Internal controls as of September 30, 1993, were not effective in assuring that transactions were properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with generally accepted accounting principles and to maintain accountability for assets among funds. However, through additional audit procedures, we were able to satisfy ourselves that these weaknesses did not have a material effect on the Corporation's financial statements. In contrast, internal controls in effect on September 30, 1993, did provide reasonable assurance that assets were safeguarded from material loss and that transactions were executed in accordance with management authority and significant provisions of selected laws and regulations.
- There was no material noncompliance with laws and regulations we tested.

Because of the Corporation's continuing progress in improving internal controls, we were able, for the first time, to opine on each of the Corporation's financial statements for fiscal year 1993. During our fiscal year 1992 audit, we identified material weaknesses affecting both funds. Along with the Corporation's Inspector General, we made recommendations for addressing those weaknesses in reports issued in September 1993.[1] These recommendations called for strengthening internal controls over systems development/modification and integration, financial reporting, multiemployer financial assistance, and participant

[1]Financial Audit: Pension Benefit Guaranty Corporation's 1992 and 1991 Financial Statements (GAO/AIMD-93-21, September 29, 1993) and Pension Benefit Guaranty Corporation Inspector General Report No. 93-6/23069-1, September 29, 1993.

data. The Corporation has stated its commitment to fully addressing the weaknesses disclosed in these reports but had not fully done so as of September 30, 1993.

The following section discusses significant matters considered in performing our audit and forming our opinions. This report also discusses our audit conclusions, additional recommendations for improving the Corporation's internal control structure, and the Corporation's comments on our report. Appendix I discusses the scope of our audit, including one area for which we reviewed and relied on the work of an independent public accountant under contract to the Corporation's Inspector General. Appendix II presents the financial statements of the funds, and appendix III contains the Corporation's written comments on a draft of this report.

Significant Matters

The following information discusses our continuing concerns about

- the long-term viability of the Single-Employer Fund and
- weaknesses in employee benefit plan audits and reporting.

In addition, significant matters involving material weaknesses in internal controls are discussed in a separate section below.

Concerns About the Long-term Viability of the Single-Employer Fund

The Single-Employer Fund is able to meet its near-term benefit obligations because premium receipts presently exceed benefit payments and the Fund held investments having a market value of $7.6 billion and cash of over $300 million at September 30, 1993. However, the Fund's unfunded $2.9 billion deficit, which represents a shortfall in assets needed to satisfy the Corporation's benefit liabilities for terminated plans and for those plans considered likely to terminate, constitutes a threat to the Fund's long-term viability. In addition to the losses recorded in the financial statements and reflected in the unfunded deficit as of September 30, 1993, the Corporation disclosed $13 billion to $18 billion in estimated unfunded liabilities in single-employer plans that represent reasonably possible future losses.

The Single-Employer Fund's long-term viability will also be affected by (1) existing pension funding standards that do not ensure that sponsors contribute enough assets to fund guaranteed benefits should the plan terminate and (2) a premium structure that is only partially risk-related. These conditions severely limit the Corporation's ability to control or manage its exposure from underfunded plans should plan sponsors be unable to meet their unfunded pension obligations.

The Employee Retirement Income Security Act of 1974 (ERISA), which created the pension insurance program, established funding standards for insured plans but allows benefits to become guaranteed before being funded by plan sponsors. The resulting timing difference has contributed, in large measure, to the Corporation's exposure should a financially troubled plan sponsor be unable to meet its pension obligation. While the Congress acted in 1987 to improve plan funding by requiring underfunded plans to begin making a "deficit reduction contribution," our analysis found that plan sponsors are able, under existing law, to eliminate or substantially reduce the effect of this additional funding requirement.[2]

Moreover, the premium structure of the Single-Employer Fund limits the Corporation's ability to manage the exposure posed by underfunded plans because premiums paid by those plans do not fully cover the risks. In 1987, the Congress modified the Single-Employer Fund's basic flat-rate premium structure by adding a supplemental variable rate premium which, for the first time, established a link between premiums and plan underfunding. The variable rate premium is based on the unfunded vested liability as calculated by the plan, after adjusting for a common interest rate, rather than the specific unfunded liability the Fund assumes should a plan actually terminate. As previously reported,[3] however, the Single-Employer Fund often assumes a substantially larger liability upon termination than the last one calculated and reported by a plan.

Also, the variable rate premium is subject to a maximum dollar amount that, when reached, effectively limits the risk-based linkage between premiums and plan underfunding. In addition, the Single-Employer Fund's premium structure does not take into account the added risk of termination posed by underfunded plans sponsored by financially troubled companies.

On September 30, 1993, the administration announced its proposals to address concerns about the Single-Employer Fund's long-term viability. The Corporation believes that enacting the Retirement Protection Act of 1993 (H.R. 3396 and S. 1780) would strengthen pension plan funding

[2]Underfunded Pension Plans: Federal Government's Growing Exposure Indicates Need for Stronger Funding Rules (GAO/T-HEHS-94-149, April 19, 1994).

[3]Pension Plans: Hidden Liabilities Increase Claims Against Government Insurance Program (GAO/HRD-93-7, December 30, 1992).

requirements, especially for underfunded single-employer plans. It would increase premiums for severely underfunded plans by phasing out the cap on the variable rate premiums. The proposed legislation contains other provisions which the Corporation believes would help it to ensure compliance with funding rules and broaden disclosure of information to participants in underfunded plans. Our analysis of the proposed legislation's funding provisions indicates that they would accelerate funding for many, but not all, underfunded plans. Our work to date suggests that the evidence of funding problems in some plans is sufficiently compelling to support stronger funding requirements for underfunded plans.

Weaknesses in Employee Benefit Plan Audits and Reporting

Weaknesses in the scope and quality of audits of employee benefit plans and the lack of plan reporting on internal controls reduce their effectiveness in safeguarding the interests of plan participants and the government. Under ERISA, the Department of Labor is responsible for establishing reporting and disclosure requirements and monitoring ongoing employee benefit plans, which include defined benefit pension plans insured by the Corporation.

Our reviews of independent public accountants' audits of employee benefit plans found severe weaknesses in both the quality and scope of plan audits that made their reliability and usefulness questionable.[4] ERISA allows plan administrators to limit the scope of plan audits by excluding plan assets held by certain regulated institutions from the scope of the auditor's work. Thus, in cases where the scope is limited, the auditor provides little or no assurance about the existence, ownership, or value of assets that may be material to the financial condition of those plans. In addition, plan auditors are not required to check the accuracy and completeness of pension insurance premium filings applicable to insured plans or related premium payments made to the Corporation. Finally, while plan administrators are responsible for establishing sound internal controls and for complying with applicable laws and regulations, ERISA does not require that either plan administrators or plan auditors report to regulators and participants on the effectiveness of internal controls.

In our April 1992 report (GAO/AFMD-92-14), we recommended that the Congress eliminate ERISA's limited scope audit provision and require plan

[4]These reviews are discussed in Employee Benefits: Improved Plan Reporting and CPA Audits Can Increase Protection Under ERISA (GAO/AFMD-92-14, April 9, 1992) and Changes Are Needed in the ERISA Audit Process To Increase Protection for Employee Benefit Plan Participants, U.S. Department of Labor, Office of Inspector General, 09-90-001-12-001 (Washington, D.C.: November 9, 1989).

administrators and auditors to report on internal controls. As of March 31, 1994, the Congress had not acted on these recommendations.

Material Internal Control Weaknesses

Our work disclosed that the Corporation has continued to make progress in improving internal controls affecting its financial reporting. However, as of September 30, 1993, material weaknesses[5] continued to exist in the Corporation's internal control structure in the three areas reported in our previous audit. We found

- weaknesses in financial systems and related internal controls,
- inadequate controls over the assessment of the Multiemployer Fund's liability for future financial assistance, and
- inadequate controls over nonfinancial participant data.

Through substantive audit procedures,[6] we were able to satisfy ourselves that these weaknesses did not have a material effect on the September 30, 1993 and 1992, statements of financial condition of the Single-Employer and Multiemployer Funds, and the related statements of operations and changes in equity and statements of cash flows for the fiscal year ended September 30, 1993. However, these weaknesses could result in misstatements in future financial statements and other financial information if not corrected by management. These weaknesses, described below, could also have an adverse impact on management decisions based, in whole or in part, on information whose accuracy is affected by the deficiencies. Unaudited financial information, including budget information, reported by the Corporation or used as a basis for management's operational decisions also may contain inaccuracies resulting from these weaknesses.

Weaknesses in Financial Systems and Related Internal Controls

We reported for fiscal year 1992 that weaknesses in financial systems and related internal controls presented an unacceptable risk to the Corporation that material misstatements might occur in the Corporation's financial information and not be detected promptly by the Corporation.

[5]A material weakness is a reportable condition in which the design or operation of the internal controls does not reduce to a relatively low level the risk that losses, noncompliance, or misstatements in amounts that would be material in relation to the financial statements may occur and not be detected within a timely period by employees in the normal course of their assigned duties.

[6]Substantive audit procedures are detailed tests and analytical procedures performed to detect material misstatements in the classification of transactions, account balances, and disclosure components of financial statements.

During fiscal year 1993, the Corporation took steps to strengthen internal controls and to identify and begin addressing weaknesses in specific financial and management information systems. Specifically, the Corporation implemented procedures for the electronic transfer of certain data and for supervisory review and approval of complex interfund allocations to compensate for deficiencies associated with redundant data entry and incorrect asset and income allocations between the Single-Employer and Multiemployer Funds. These deficiencies had caused material misstatements resulting in adjustments to the financial statements in previous years.

During the fiscal year, the Corporation also began using its security software more effectively to limit and detect unauthorized access to its mainframe computerized application systems. In addition, the Corporation completed the implementation of numerous policies and procedures to strengthen its annual financial reporting process. Furthermore, the Corporation awarded a contract for the design, development, and implementation of a new premium accounting system.

However, as of September 30, 1993, the Corporation had not effectively implemented sufficient financial reporting controls to compensate fully for its lack of financial system integration. Deficiencies in automated management and financial information systems continued to severely inhibit management's ability to promptly and accurately accumulate and summarize the information needed for internal and external reports. Overall, the Corporation's cumbersome and nonintegrated processes for preparing the financial and other management information needed to support operations and financial/budgetary reporting were time-consuming and labor-intensive. Thus, system and control weaknesses exposed the Corporation to a significant risk that the information could be materially misstated.

- The Corporation's primary and subsidiary financial and management information systems generally were not integrated and thus could not share data. This lack of system integration resulted in an overreliance on personal computers (PC) and departmental computer networks which frequently resulted in duplicate data being maintained to accomplish and support complex operational and financial reporting requirements. Because the Corporation's manual and PC-based processes for accumulating, summarizing, and supporting financial information continued to occur outside traditional automated computer controls and, in some cases, without adequate supervisory review or compensating controls, the risk of material misstatements in the Corporation's financial and management information was significantly increased.

- The Corporation had no established internal methodologies or organizational standards to govern the consistent development or modification of computer application systems and related controls.
- Certain reporting procedures and accounting policies the Corporation used to develop the statements of cash flows were not effectively implemented and initially resulted in incorrect cash flow amounts for fiscal year 1993. In auditing the Corporation's statements of cash flows for the first time, we found deficiencies in controls over their preparation and in the underlying accounting policies which governed their preparation. Because the Corporation's primary financial information systems did not adequately summarize significant cash flow data, many of the amounts used in preparing the statements of cash flows were derived, in whole or in part, from data maintained on PC-based spreadsheets. We found that supervisory review of documentation supporting the statements of cash flows was not effective in identifying certain noncash transactions. In addition, underlying accounting policies which governed the Corporation's preparation of the statements of cash flows were not finalized by fiscal year-end and provided for the inclusion of certain cash transactions that should have been excluded. As a result of our audit work, the Corporation adjusted the statements of cash flows to correct the effects of these transactions, some of which related to prior years.
- Faced with premium accounting system deficiencies, the Corporation continued to rely on a temporary, labor-intensive process to generate bills and collect amounts owed for certain past-due premiums, interest, and penalties. The process used during fiscal year 1993 was inefficient and susceptible to error and required intense managerial oversight.

In combination, the weaknesses in the Corporation's financial systems and internal controls significantly increased the risk that errors and misstatements might occur in management and financial information and not be promptly detected by the Corporation. This condition was due, in part, to shortcomings in systems development and operations, including the absence of a proven systems development methodology. Other contributing factors were the inability of the primary financial systems to meet the Corporation's needs for financial and budgetary information and the absence during fiscal year 1993 of an interim financial reporting process to provide added system discipline and improve year-end reporting accuracy.

Inadequate Controls Over the Assessment of the Multiemployer Fund's Liability for Future Financial Assistance

In our fiscal year 1992 audit of the Multiemployer Fund's financial statements, we found that the Corporation, in preparing its financial statements, had not adequately considered or recognized the Fund's liability for financial assistance for plans which may require financial assistance in the future. We also found limited evidence of supervisory review of the Corporation's fiscal year 1992 liability assessment process and its results.

During fiscal year 1993, the Corporation initiated a more comprehensive assessment process. After fiscal year-end, the Corporation continued to implement the process and obtained financial information on certain insured plans that previously had not been available to the Corporation. However, as of September 30, 1993, the Corporation's internal controls over the Multiemployer Fund's liability assessment process were ineffective because certain procedures performed were either incomplete or implemented ineffectively. Our audit of the Corporation's assessment for fiscal year 1993 found deficiencies in its documentation and methodology, related computer controls, and review and supervision.

The Corporation had incomplete documentation supporting its liability assessment. In several areas, the documentation was insufficient to support conclusions the Corporation had reached until certain steps had been repeated or additional evidence had been obtained. We also identified plans for which the Corporation had not fully evaluated its financial exposure. Its methodology and procedures did not address the accuracy of certain data utilized and did not fully and consistently consider risks associated with reportable events, declining plan financial trends, excessive concentrations of plan assets, and the use of outdated data. Furthermore, key steps in the process involved computer applications performed outside the Corporation's general computer controls, thus negating the effectiveness of key security controls designed to limit file access to authorized personnel.

The Corporation was unable to provide evidence which documented its review and supervision of certain key aspects of its liability assessment process. The lack of documentation involved certain aspects of determining the multiemployer plan universe, screening to identify financially troubled plans, and evaluating the likelihood that those plans might require future financial assistance.

To compensate for the potential effects of internal control deficiencies, we performed additional audit procedures designed to identify and assess the

Fund's exposure from underfunded multiemployer plans that the Corporation's assessment had not adequately evaluated. In performing these procedures, we identified several plans not included in the Corporation's plan universe. Our audit procedures resulted in adjustments to the liability and related losses the Corporation developed in its fiscal year 1993 assessment process.

Inadequate Controls Over Nonfinancial Participant Data

For fiscal year 1992, we reported that data input controls did not ensure the accuracy of nonfinancial participant data entered into actuarial worksheets and the Pension and Lump Sum (PLUS) system. In processing a terminated pension plan, the Corporation obtains nonfinancial participant data (such as social security numbers and dates of birth and employment) and uses the data, in conjunction with other information, to initially determine participants' guaranteed benefits. After the nonfinancial data are obtained and initial benefits are determined, the data are entered into the PLUS automated data base, which is used to respond to participant inquiries and administer other benefit services. The Corporation uses these data annually to value its benefit liability for participants whose data have been entered in PLUS. Inaccurate nonfinancial data can reduce the precision of the Corporation's fiscal year-end liability valuation and delay the final calculation of participant benefits.

During fiscal year 1993, the Corporation initiated efforts designed to improve the accuracy of certain aspects of nonfinancial participant data entered into the PLUS system. However, control weaknesses involving these data continued to exist for fiscal year 1993 because the Corporation had not made significant progress in improving procedures for obtaining and documenting participant data in a timely manner. Also, weaknesses existed in the Corporation's verifying and editing of the nonfinancial participant data entered and maintained in the Corporation's records and its PLUS data base.

Weaknesses in controls over nonfinancial participant data and related recommendations are discussed further in the Pension Benefit Guaranty Corporation Inspector General Report No. 94-6/23079-1. We concur with the report's recommendations, which are designed primarily to strengthen the verification of participant data and the input and edit controls over participant data maintained in PLUS.

Opinion on Fiscal Years 1993 Financial Statements and 1992 Statements of Financial Condition

The accompanying statements of financial condition present fairly, in all material respects, the financial position of the Single-Employer and Multiemployer Funds as of September 30, 1993 and 1992, and their results of operations and cash flows for the fiscal year ended September 30, 1993, in accordance with generally accepted accounting principles. However, misstatements may nevertheless occur in other financial information reported by the Corporation as a result of the internal control weaknesses previously described.

In our fiscal year 1991 and earlier audits, we were unable to express an opinion on the Corporation's financial statements.[7] Because the amounts in the September 30, 1991, statements of financial condition materially affected the results of operations for fiscal year 1992, we were unable to express an opinion on the Corporation's statements of operations and changes in equity for the fiscal year ended September 30, 1992. Accordingly, our audit for fiscal year 1992 was limited to the Corporation's statements of financial condition, and we did not audit the Corporation's statements of cash flows for fiscal year 1992.

In our September 29, 1993, report, we issued a qualified opinion on the statement of financial condition of the Multiemployer Fund as of September 30, 1992, because information on certain financially troubled pension plans was not available to determine whether they might require assistance from the Corporation. However, after we issued our report, the Corporation obtained sufficient information on those plans and restated the Multiemployer Fund's liability for future financial assistance to record additional liabilities of $34 million, and we were then able to test those amounts. Accordingly, our opinion on the Multiemployer Fund's statement of financial condition as of September 30, 1992, as presented herein, is now unqualified and different from our opinion expressed in our previous report.

Furthermore, the Corporation's assessment of the Multiemployer Fund's exposure to liabilities for future financial assistance is subject to material uncertainties, whose eventual effects cannot be reasonably determined at present. Many complex factors must be considered to identify multiemployer plans which are likely to require future assistance and estimate the amount of such assistance. These factors, which include the financial condition of the plans and their multiple sponsors, will be

[7]Financial Audit: System and Control Problems Further Weaken the Pension Benefit Guaranty Fund (GAO/AFMD-92-1, November 13, 1991) and Financial Audit: Pension Benefit Guaranty Corporation's 1991 and 1990 Financial Statements (GAO/AFMD-92-35, March 2, 1992).

affected by future events, most of which are beyond the Corporation's control.

Opinion on Internal Controls

We evaluated whether the Corporation's internal controls in effect on September 30, 1993, provided reasonable assurance that losses, noncompliance, or misstatements material in relation to the financial statements would be prevented or detected. Specifically, the controls we evaluated were those designed to

- safeguard assets against loss from unauthorized use or disposition;
- assure the execution of transactions in accordance with management authority and with laws and regulations; and
- properly record, process, and summarize transactions to permit the preparation of financial statements in accordance with generally accepted accounting principles and to maintain accountability for assets.

Because of the previously described material weaknesses, internal controls did not provide reasonable assurance that the Corporation properly recorded, processed, and summarized transactions to permit the preparation of financial statements in accordance with generally accepted accounting principles. However, controls in effect on September 30, 1993, provided reasonable assurance that assets were safeguarded against loss from unauthorized use or disposition and that transactions were executed in accordance with management's authority and significant provisions of selected laws and regulations.

Reportable Conditions

While the Corporation made progress in addressing the reportable conditions identified and discussed with the Corporation during our fiscal year 1992 audit, our audit for fiscal year 1993 found that some of these reportable conditions continued to exist. Although these reportable conditions are not considered to be material weaknesses, they continue to represent significant deficiencies in the design or operation of the Corporation's internal controls and should be corrected.

- The Corporation had not implemented controls to test the financial information submitted by multiemployer plans requesting financial assistance to ensure that the requests were valid and adequately supported prior to providing the assistance.
- The Corporation's controls over documentation supporting participant data maintained on PLUS were inadequate. In many cases, the Corporation

was unable to provide documentation supporting the nonfinancial participant data entered on PLUS. In addition, the Corporation was not always able to demonstrate that procedures designed to support the accuracy of PLUS data were performed. Without proper supporting documentation, the Corporation may be unable to demonstrate the accuracy of PLUS data used to value the Corporation's liability for terminated plans. This reportable condition and related recommendations, with which we concur, are discussed further in the Pension Benefit Guaranty Corporation Inspector General Report No. 94-6/23079-1.

During fiscal year 1993, the Corporation initiated action to address two of the reportable conditions identified during our fiscal year 1992 audit. As of September 30, 1993, the Corporation initiated audits to ensure that Multiemployer Fund financial assistance previously provided had actually been used to pay guaranteed benefits and related expenses. In addition, the Corporation strengthened its internal controls over the activities of field benefit administrators. Field benefit administrators provide support services under contract to the Corporation; these services include maintaining financial data, creating participant files, and corresponding with participants.

In addition to the material weaknesses and reportable conditions described in this report, we noted other less significant matters involving the Corporation's internal control structure and its operations which we will be reporting separately to the Corporation's management. Similarly, in addition to the material weakness and reportable condition described in Pension Benefit Guaranty Corporation Inspector General Report No. 94-6/23079-1, other less significant matters related to the Corporation's internal control structure over its liability for future benefits on terminated plans will be reported separately to management by the Corporation's Inspector General.

Compliance With Laws and Regulations

Our tests of compliance with significant provisions of selected laws and regulations disclosed no material instances of noncompliance. Also, nothing came to our attention in the course of our other work to indicate that material noncompliance with such provisions occurred.

Recommendations

To strengthen internal controls over the Corporation's assessment of the Multiemployer Fund's liability for future financial assistance, we recommend that the Corporation's Executive Director direct the Chief Financial Officer to

- monitor and test the Corporation's liability assessment process to ensure that it fully complies with its recently established policies and procedures for supporting and documenting all key decisions and for reviewing and supervising the process and its results and
- enhance the liability assessment policies and procedures by requiring that (1) computer controls be established to appropriately control the use of automated information and data, (2) automated data used in the process be tested for accuracy and completeness, and (3) the assessment process fully and consistently consider reportable events, plan financial trends, extent of asset concentrations, and the age of the plan data used in the assessment.

To strengthen internal controls over the Corporation's liability for future benefits on terminated plans, we recommend that the Corporation's Executive Director direct the Chief Operating Officer to implement the Inspector General's recommendations on strengthening internal controls over participant data as reported in Pension Benefit Guaranty Corporation Inspector General Report No. 94-6/23079-1.

Agency Comments and Our Evaluation

Commenting on a draft of this report, the Corporation's Executive Director agreed with our findings and recommendations. The Executive Director's written comments, provided in appendix III, discuss various efforts, many of which are ongoing, intended to address the reported material weaknesses and reportable conditions and respond to our recommendations. We plan to evaluate the adequacy and effectiveness of these efforts as part of our follow-up audits of the Corporation's financial statements.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

April 20, 1994

Objectives, Scope, and Methodology

The Corporation's management is responsible for

- preparing the annual financial statements of the two funds in conformity with generally accepted accounting principles,
- establishing and maintaining internal controls and systems to provide reasonable assurance that the internal control objectives discussed earlier are met, and
- complying with applicable laws and regulations.

We are responsible for obtaining reasonable assurance about whether (1) the Corporation's financial statements we audited are reliable (free of material misstatement and presented fairly in conformity with generally accepted accounting principles) and (2) relevant internal controls are in place and operating effectively. We are also responsible for testing compliance with significant provisions of selected laws and regulations.

In fulfilling these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the aforementioned financial statements of each of the two funds;
- assessed the accounting principles used and significant estimates made by the Corporation's management;
- evaluated the overall presentation of the aforementioned financial statements of each of the two funds;
- evaluated and tested relevant internal controls over the following areas:
  - present value of future benefits and related losses and expenses;
  - benefit determinations;
  - present value of nonrecoverable future financial assistance, and related losses;
  - financial reporting;
  - investments and treasury, and related income;
  - premium income and receivables;
  - other assets;
  - other liabilities and expenses;
  - budget accounting; and
  - cash flows.
- evaluated and tested compliance with significant provisions of the Employee Retirement Income Security Act of 1974, as amended, and the Chief Financial Officers Act of 1990. The provisions selected for testing included, but were not limited to, those relating to
  - benefit guarantees and financial assistance;

- the availability of, accounting for, and use of funds;
- the preparation and issuance of financial statements and management reports; and
- premiums and the assessment of related interest and penalties.

We also conducted tests of compliance with the Anti-Deficiency Act that were limited to comparing the Corporation's recorded payments to related authorized limitations on certain payments and apportionments.

In fulfilling our responsibilities, we have relied on audit work performed by an independent public accounting firm under the direction of the Corporation's Inspector General. The scope of this work, performed in conjunction with our audit, included an audit of the Corporation's liabilities for future benefits on terminated plans and related losses, expenses, and cash flows, as well as related internal controls and compliance. We worked with the Inspector General to establish the scope of the work. We reviewed the work and concur with its scope, opinions, conclusions, and recommendations, which are presented in Pension Benefit Guaranty Corporation Inspector General Report No. 94-6/23079-1.

We limited our work to accounting and other controls necessary to achieve the objectives outlined in our opinion on internal controls. Because of inherent limitations in any system of internal control, losses, noncompliance, or misstatements may nevertheless occur and not be detected. We also caution that projecting our evaluation of controls to future periods is subject to the risk that controls may become inadequate because of changes in conditions or the degree of compliance with controls may deteriorate.

Our audit was conducted pursuant to provisions of 31 U.S.C. 9105, as amended, and in accordance with generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions.

Financial Statements

Statements of Financial Condition

(Dollars in millions)	Single-Employer Program September 30, 1993	Single-Employer Program September 30, 1992	Multiemployer Program September 30, 1993	Multiemployer Program September 30, 1992	Memorandum Total September 30, 1993	Memorandum Total September 30, 1992
Assets						
Investments, at market (Note 3):						
Fixed maturity securities	**$5,844**	$4,065	**$384**	$267	**$6,228**	$4,332
Equity securities	**1,412**	1,235	**2**	3	**1,414**	1,238
Real estate	**88**	106	**0**	0	**88**	106
Other	**209**	253	**0**	0	**209**	253
Total investments	**7,553**	5,659	**386**	270	**7,939**	5,929
Cash and cash equivalents	**313**	238	**19**	9	**332**	247
Receivables, net:						
Due from sponsors of terminated plans	**65**	102	**0**	0	**65**	102
Due from sponsors of restored plans (Note 8)	**0**	17	**0**	0	**0**	17
Premiums	**32**	47	**0**	1	**32**	48
Notes—financial assistance (Note 4)			**0**	0	**0**	0
Due from sale of securities	**29**	86	**0**	0	**29**	86
Lease receivable	**75**	116	**0**	0	**75**	116
Due from insurance companies	**6**	0	**0**	0	**6**	0
Accrued investment income	**45**	40	**2**	3	**47**	43
Other (Note 8)	**53**	3	**0**	0	**53**	3
Total receivables	**305**	411	**2**	4	**307**	415
Furniture and fixtures, net	**1**	0	**0**	0	**1**	0
Restricted assets (Note 8)	**95**	0	**0**	0	**95**	0
Assets of terminated plans pending trusteeship, at market, net (Note 3)	**154**	73	**0**	0	**154**	73
Total assets	**$8,421**	$6,381	**$407**	$283	**$8,828**	$6,664

The accompanying notes are an integral part of these financial statements.

(Dollars in millions)	Single-Employer Program September 30, 1993	Single-Employer Program September 30, 1992	Multiemployer Program September 30, 1993	Multiemployer Program September 30, 1992	Memorandum Total September 30, 1993	Memorandum Total September 30, 1992
Liabilities						
Present value of future benefits, net (Note 5):						
Trusteed plans	**$8,655**	$7,553	**$ 13**	$13	**$8,668**	$7,566
Terminated plans pending trusteeship	**565**	210	**0**	0	**565**	210
Net claims for probable terminations	**1,627**	1,027	**0**	0	**1,627**	1,027
Total present value of future benefits, net	**10,847**	8,790	**13**	13	**10,860**	8,803
Present value of nonrecoverable future financial assistance (Note 6)			**110**	94	**110**	94
Claim on contingent valuation rights (Note 8)	**96**	0	**0**	0	**96**	0
Unearned premiums	**207**	204	**8**	7	**215**	211
Accounts payable and accrued expenses (Note 7)	**168**	124	**0**	0	**168**	124
Commitments and contingencies (Notes 9, 10, and 18)						
Total liabilities	**11,318**	9,118	**131**	114	**11,449**	9,232
Equity						
Accumulated results of operations (deficit)	**(2,897)**	(2,737)	**276**	169	**(2,621)**	(2,568)
Total liabilities and equity	**$8,421**	$6,381	**$407**	$283	**$8,828**	$6,664

The accompanying notes are an integral part of these financial statements.

Statements of Operations and Changes in Equity

(Dollars in millions)	Single-Employer Program September 30, 1993	Single-Employer Program September 30, 1992 Unaudited	Multiemployer Program September 30, 1993	Multiemployer Program September 30, 1992 Unaudited	Memorandum Total September 30, 1993	Memorandum Total September 30, 1992
Underwriting:						
Income:						
Premium income (Note 11)	$ 890	$ 875	$ 23	$ 23	$ 913	$ 898
Other income (Note 12)	38	118	(1)	1	37	119
Total	928	993	22	24	950	1,017
Expenses:						
Losses from completed and probable terminations (Note 13)	894	896	0	0	894	896
Losses from financial assistance (Note 6)			20	46	20	46
Loss on contingent valuation rights (Note 8)	96	0	0	0	96	0
Administrative expenses	97	90	0	0	97	90
Actuarial adjustments (Note 5)	33	(256)	0	(1)	33	(257)
Total	1,120	730	20	45	1,140	775
Underwriting income (loss)	(192)	263	2	(21)	(190)	242
Financial:						
Investment income (Note 14):						
Fixed	1,465	441	107	27	1,572	468
Equity	150	106	0	0	150	106
Other	(77)	67	0	0	(77)	67
Total	1,538	614	107	27	1,645	641
Expenses:						
Investment expenses	10	7	0	0	10	7
Actuarial charges (credits) (Note 5):						
Due to passage of time	372	427	1	(1)	373	426
Due to change in interest rates	1,124	677	1	1	1,125	678
Total	1,506	1,111	2	0	1,508	1,111
Financial income (loss)	32	(497)	105	27	137	(470)
Net income (loss)	(160)	(234)	107	6	(53)	(228)
Accumulated results of operations (deficit), beginning of year	(2,737)	(2,503)	169	163	(2,568)	(2,340)
Accumulated results of operations (deficit), end of year	$(2,897)	$(2,737)	$276	$169	$(2,621)	$(2,568)

The accompanying notes are an integral part of these financial statements.

Statements of Cash Flows

(Dollars in millions)	Single-Employer Program September 30, 1993	Single-Employer Program September 30, 1992 Unaudited	Multiemployer Program September 30, 1993	Multiemployer Program September 30, 1992 Unaudited	Memorandum Total September 30, 1993	Memorandum Total September 30, 1992
Operating Activities:						
Premium receipts	$ 907	$ 873	$23	$ 22	$ 930	$ 895
Benefit payments - trusteed plans	(657)	(626)	(2)	(2)	(659)	(628)
Interest and dividends received, net	266	214	12	10	278	224
Cash received from plans upon trusteeship	9	18	0	0	9	18
Receipts of due from sponsors	66	35	0	0	66	35
Receipts of lease receivable	130	29	0	0	130	29
Purchase LTV stock rights	(50)	0	0	0	(50)	0
Financial assistance payments			(4)	(4)	(4)	(4)
Payments for administrative and other expenses	(105)	(85)	0	0	(105)	(85)
Net cash provided by operating activities (Note 17)	566	458	29	26	595	484
Investing Activities:						
Proceeds from sales of investments	2,972	4,203	25	87	2,997	4,290
Payments for purchases of investments	(3,463)	(4,655)	(44)	(124)	(3,507)	(4,779)
Net cash used in investing activities	(491)	(452)	(19)	(37)	(510)	(489)
Net increase (decrease) in cash and cash equivalents	75	6	10	(11)	85	(5)
Cash and cash equivalents, beginning of year	238	232	9	20	247	252
Cash and cash equivalents, end of year	$ 313	$ 238	$19	$ 9	$ 332	$ 247

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 1993 AND 1992

Note 1 -- Organization and Purpose

The Pension Benefit Guaranty Corporation (PBGC) insures pensions, within statutory limits, of participants in covered single-employer and multiemployer defined benefit pension plans that meet the criteria specified in Section 4021 of the Employee Retirement Income Security Act of 1974 (ERISA).

PBGC is a federal corporation subject to the provisions of the Government Corporation Control Act. PBGC was created by Title IV of ERISA. Its activities are defined in ERISA as amended by the Multiemployer Pension Plan Amendments Act of 1980 (MPPAA), the Single-Employer Pension Plan Amendments Act of 1986 (SEPPAA), and the Pension Protection Act of 1987 (PPA).

ERISA requires that the PBGC programs be self-financing. The Corporation finances its operations through premiums collected from covered plans, assets assumed from terminated plans, collection of employer liability payments due under ERISA as amended, and investment income. In addition, PBGC may borrow up to $100 million from the U.S. Treasury to finance its operations. The Corporation did not use this borrowing authority during the years ended September 30, 1993, or September 30, 1992, nor is use of this authority currently planned. ERISA provides that the U.S. Government is not liable for any obligation or liability incurred by PBGC.

Under the single-employer program, PBGC is liable for the payment of guaranteed benefits with respect only to underfunded terminated plans. An underfunded plan may terminate only if PBGC finds that one of the four conditions for a distress termination, as defined in ERISA, is met or if PBGC involuntarily terminates a plan under one of four specified statutory tests. The net liability assumed by PBGC is generally equal to the present value of the future guaranteed benefits less (1) the amounts that are provided by the plan's assets and (2) the amounts that are recoverable by PBGC from the plan sponsor and members of the plan sponsor's controlled group, as defined by ERISA.

Under the multiemployer program, if a plan becomes insolvent, it receives financial assistance from PBGC to allow the plan to pay participants their guaranteed benefits. Such assistance is recognized as a loss, to the extent that the plan is expected to be unable to repay these amounts from future plan contributions.

Note 2 -- Significant Accounting Policies

Certain items on the 1992 financial statements have been reclassified to conform with present year classifications.

Revolving and Trust Funds: PBGC accounts for each program's revolving and trust funds on an accrual basis. The revolving and trust funds each pay a pro-rata portion of the benefits paid each year. The revolving and trust funds have been combined for presentation purposes in the financial statements. The single-employer and multiemployer programs are separate entities by law and, therefore, are reported separately.

ERISA provides for the establishment of revolving funds to be used by PBGC "in carrying out its duties." The revolving funds support the administrative functions of PBGC and fund any deficits incurred by PBGC in trusteeing plans or providing financial assistance. Premiums collected from ongoing plans are accounted for through the revolving funds. The Pension Protection Act of 1987 created a new single-employer program revolving fund (the seventh fund) that is credited with all premiums in excess of $8.50 per participant, including all penalties, interest charged on these amounts and investment income. This fund may not be used to pay PBGC's administrative costs or the benefits of any plan terminated prior to October 1, 1988, unless no other amounts are available.

The trust funds reflect accounting activity associated with: (1) trusteed plans--plans for which PBGC has legal responsibility, (2) plans pending trusteeship--terminated plans for which PBGC has not become legal trustee by fiscal yearend, and (3) probable terminations--plans that PBGC expects will terminate and incur a loss for PBGC. PBGC cannot exercise control over the assets of plans until it becomes trustee, which may be several years after the date of plan termination.

Allocation of Revolving and Trust Funds: Total revolving and trust fund investment assets and the earnings on those investment assets, net of investment expenses, are allocated to each program's revolving and trust funds to the extent that such amounts are not directly attributable to a specific fund. Revolving fund investment earnings are allocated on the basis of each program's average cash available for investment during the year. Revolving fund investment assets are allocated on the basis of the yearend equity of each program's revolving funds. The plan assets acquired by PBGC and commingled at PBGC's custodian bank, as well as the earnings on the commingled investment assets, are allocated to each program's trust funds on the basis of each trust fund's value, relative to the total value of the commingled fund.

Valuation Method: PBGC reports its assets and liabilities on a market basis because PBGC believes that this provides the most realistic measure of its financial condition and that it is the most appropriate basis on which to evaluate its performance.

Investment Valuation and Income: Market values are based on the last sale of a listed security, or the mean of the "bid-and-asked" for nonlisted securities, and on a valuation model in the case of fixed-income securities that are not actively traded. These valuations are determined as of the end of each fiscal year. Purchases and sales of securities are recorded on the trade date. Investment income is accrued as earned. Dividend income is recorded on the ex-dividend date. Realized gains and losses on sales of investments are calculated using average cost (see Notes 3 and 14).

Cash and Cash Equivalents: Cash and cash equivalents includes cash on hand, demand deposits, and securities with a maturity of one business day.

Due from Sponsors of Terminated Plans: The amount due from sponsors of terminated plans is the settled claims for employer liability (underfunding as of plan termination) and for contributions due from sponsors or members of their controlled group (collectively, the sponsors) less an allowance for uncollectible amounts. Amounts expected to be received beyond one year are discounted for time and risk factors. Some agreements between PBGC and plan sponsors provide for contingent payments based on future profits of the sponsors. Any such future amounts realized will be reported in the period in which they accrue or are paid.

Premiums: Premiums receivable represent the earned portion of the premium for plans that have a plan year commencing before the end of PBGC's fiscal year but have not paid their premium by fiscal yearend and past due premiums deemed collectible, including collectible penalties and interest. Unearned premiums represent an estimate of payments received during the fiscal year that cover the portion of a plan's year after the Corporation's fiscal yearend (see Note 11). Premium income represents revenue generated from self-assessments received from defined benefit pension plans as required by Title IV of ERISA.

Notes--Financial Assistance and Present Value of Nonrecoverable Future Financial Assistance: PBGC provides financial assistance in the form of loans to certain multiemployer plans, in exchange for interest-bearing promissory notes, so the plans can continue to pay guaranteed benefits. These notes constitute an obligation of each plan and, in the event of the plan's financial recovery, are to be repaid. It is anticipated that the circumstances leading to the distress of each plan will continue and the notes, including accrued but unpaid interest, will be uncollectible. To the extent that financial assistance payments have previously been accrued, as discussed below, they are treated as a reduction to the present value of nonrecoverable future financial assistance.

The present value of nonrecoverable future financial assistance represents the estimated nonrecoverable payments to be provided by PBGC in the future to multiemployer plans that cannot meet their benefit obligations. The present value of nonrecoverable future financial assistance is based on the difference between the present value of future benefits and the market value of plan assets, including the present value of future amounts expected to be paid by plan sponsors, for those plans that are expected to require future assistance. The amount reflects the rates at which these liabilities could be settled in the market for single-premium nonparticipating annuities issued by private insurers.

Assets of Terminated Plans Pending Trusteeship, Net: The net assets of terminated plans pending trusteeship represent all assets anticipated to be received less liabilities, other than the present value of future benefits and the present value of expected recoveries from sponsors. Assets are accounted for using market values consistent with PBGC's investments. Any increase or decrease in the market value of the assets occurring after the date on which the plan is terminated must, by law, be credited to or suffered by PBGC.

Present Value of Future Benefits (PVFB): The PVFB is the estimated liability for future pension benefits that PBGC is or will be obligated to pay with respect to trusteed plans and terminated plans pending trusteeship. This liability is stated as the actuarial present value of estimated future benefits less the present value of estimated recoveries from sponsors. For financial statement purposes, the estimated liabilities (net of estimated assets and recoveries) attributable to probable future plan terminations are also included in the PVFB. To measure the actuarial present value, PBGC used assumptions to adjust the value of those future payments to reflect the time value of money (by discounting) and the probability of payment (by means of decrements, such as for death or retirement). PBGC also included anticipated expenses to settle the benefit obligation in the determination of the PVFB.

(1) Trusteed Plans--represents the present value of future payments of benefits less the present value of expected recoveries, for which an agreement has not been reached, from sponsors of plans that have terminated and been trusteed by PBGC prior to fiscal yearend.

(2) Terminated Plans Pending Trusteeship--represents the present value of future payments of benefits less the present value of expected recoveries, for which an agreement has not been reached, from sponsors of plans that have terminated but not been trusteed by PBGC prior to fiscal yearend.

Any changes after the date of plan termination in the amounts for trusteed plans and terminated plans pending trusteeship are reported as an actuarial charge (credit) in the Statements of Operations and Changes in Equity.

(3) Net Claims for Probable Terminations--includes estimates of the losses, net of plan assets and the present value of expected recoveries from sponsors, from plans that were expected to terminate based on the occurrence of an identifiable event by fiscal yearend and the expectation that the distress tests will be met or PBGC itself will seek termination of the plan.

Benefit payments to participants of pension plans trusteed by PBGC, or that are terminated and pending trusteeship, represent a reduction to the PVFB (see Note 5).

Losses from Completed and Probable Terminations: Amounts reported as losses from completed and probable terminations on the Statements of Operations and Changes in Equity represent the difference as of the date of plan termination between the present value of future benefits (including amounts owed under Section 4022(c) of ERISA) assumed, or expected to be assumed, by PBGC, less related plan assets and the present value of expected recoveries from sponsors (see Note 13).

Actuarial Charges and Adjustments: Actuarial charges (credits) related to changes in method and the effect of experience are classified as underwriting activity. Actuarial charges (credits) related to changes in interest rates and passage of time are classified as financial activity. These charges, credits, and adjustments represent the change in the PVFB that results from applying actuarial assumptions in the calculation of future benefit liabilities.

Depreciation: Depreciation of PBGC's furniture and equipment is calculated on a straight-line basis over the estimated useful lives of the assets. The useful lives range from 5 to 10 years. Routine maintenance repairs and leasehold improvements (the amounts of which are not material) are charged to operations as incurred.

Note 3 -- Investments

Premium receipts are invested in securities issued by the U.S. Government.

The trust funds include assets PBGC acquires or expects to acquire from terminated plans, missed contributions, employer liability, and investment income thereon. These assets are held by custodian banks.

The basis and market value of the investments by type are detailed below. The basis indicated is cost of the asset if acquired after the date of plan termination or the market value at date of plan termination if the asset was acquired as a result of a plan's termination.

Investments of Single-Employer Revolving Funds and Single-Employer Trusteed Plans
(Dollars in millions)

	September 30, 1993		September 30, 1992	
	Basis	Market Value	Basis	Market Value
Fixed maturity securities:				
U.S. Government securities	$4,104	$5,353	$3,299	$3,642
Commercial paper	1	1	3	3
Corporate bonds	451	490	393	420
Subtotal	4,556	5,844	3,695	4,065
Equity securities	1,068	1,412	908	1,235
Real estate funds	100	88	114	106
Insurance contracts	25	29	67	115
Mortgages	126	135	92	98
Foreign securities	42	45	38	40
Total	$5,917	$7,553	$4,914	$5,659

Investments of Multiemployer Revolving Funds and Multiemployer Trusteed Plans
(Dollars in millions)

	September 30, 1993		September 30, 1992	
	Basis	Market Value	Basis	Market Value
Fixed maturity securities:				
U.S. Government securities	$279	$383	$239	$267
Corporate bonds	1	1	0	0
Subtotal	280	384	239	267
Equity securities	2	2	3	3
Total	$282	$386	$242	$270

Investments (Assets) of Single-Employer Terminated Plans Pending Trusteeship, Net
(Dollars in millions)

	September 30, 1993		September 30, 1992	
	Basis	Market Value	Basis	Market Value
U. S. Government securities	$ 26	$ 26	$13	$13
Corporate bonds	45	46	2	2
Equity securities	25	25	23	23
Insurance contracts	26	15	27	18
Other	10	11	0	0
Cash and cash equivalents	31	31	17	17
Total, net	$163	$154	$82	$73

Note 4 -- Notes - Financial Assistance

(Dollars in millions)

	September 30, 1993	September 30, 1992 Unaudited
Balance at beginning of year, net	$ 0	$ 0
Financial assistance payments	4	4
Interest accrued and not paid	1	1
Allowance for uncollectible amounts	(5)	(5)
Balance at end of year, net	$ 0	$ 0

Note 5 -- Present Value of Future Benefits

The following table summarizes the actuarial charges (credits) and adjustments that explain how the Corporation's single-employer program liability for the present value of future benefits changed for the years ended September 30, 1993 and 1992. In 1992, PBGC improved its estimates through enhanced computer software used for the calculations and through significant changes to its assumptions that made them individually reasonable. PBGC made minor refinements to individual assumptions in 1993 to better approximate its anticipated experience.

PBGC changed the interest assumptions used for the September 30, 1992, valuation from those prescribed in the Valuation of Plan Benefits regulation (29 CFR 2619) to a 20-year select interest rate of 7.2% followed by an ultimate rate of 6.25%. For the September 30, 1993, valuation, PBGC changed the interest assumption from those prescribed in the Valuation of Plan Benefits regulation, as revised, to a 20-year select interest rate of 6% followed by an ultimate rate of 5.5%. These rates were determined as those needed to continue to match the survey of insurance company prices provided by the American Council of Life Insurance (ACLI).

For 1992, PBGC changed the mortality table used from the Unisex Pension Table for Healthy Lives (UP84) prescribed in the Valuation of Plan Benefits regulation to the 1983 Group Annuity Mortality Table with margins (83GAM loaded). This was the most current standard mortality table for group annuity business. For 1993, PBGC changed from the 83GAM loaded mortality table prescribed in the Valuation of Plan Benefits regulation, as revised, to the 83GAM loaded projected to 1993 by Scale H. PBGC has found that this table is very similar to tables used by insurance companies to price annuities and is generally consistent with its experience.

For 1992, the administrative expense assumption was changed from an implicit reduction in the immediate interest rate to an explicit formula consisting of (1) an initial case processing cost of $8,000 per plan (prorated over the first $200,000 of liability) plus $200 per plan participant, both of which costs are to be phased out over four years following the date of termination; and (2) a flat 1 percent of total plan liability. PBGC also derived this formula from the ACLI survey. For 1993, the formula was revised to $10,800 per plan (prorated) plus $270 per plan participant, phased out over four years following the date of trusteeship, and a flat 1.35% of total plan liability.

The total actuarial charge for 1992 for changes in method decreased liabilities by $328 million. Of this, $299 million (or 4 percent of the PVFB at September 30, 1992) was due to the changes in assumptions described above. The effect for 1993 of revisions to individual assumptions was not material.

The resulting liability represents PBGC's best estimate of the measure of anticipated experience under these programs.

Reconciliation of the Present Value of Future Benefits for the Years Ended September 30, 1993 and 1992
(Dollars in millions)

	September 30, 1993		September 30, 1992 Unaudited	
Present value of future benefits, at beginning of year – Single-Employer, net		$ 8,790		$7,594
Estimated recoveries		188		251
PVFB at beginning of year, gross		8,978		7,845
Net claims for probable terminations, prior year		(1,027)		(776)
Actuarial adjustments (underwriting):				
Changes in method	$ 22		$ (328)	
Effect of experience	11		72	
Total actuarial adjustments (underwriting)	33		(256)	
Actuarial charges (financial):				
Passage of time	372		427	
Changes in interest rate	1,124		677	
Total actuarial charges (financial)	1,496		1,104	
Total actuarial charges		1,529		848
Terminations:				
Current year	564		789	
Changes in prior year	11		(121)	
Total terminations		575		668
Benefit payments*		(720)		(634)
Estimated recoveries		(115)		(188)
Net claims for probable terminations:				
Future benefits**	3,645		2,726	
Estimated plan assets and recoveries from sponsors	(2,018)		(1,699)	
Total net claims, current year		1,627		1,027
Present value of future benefits, at end of year – Single-Employer, net		10,847		8,790
Present value of future benefits, at end of year – Multiemployer		13		13
Total present value of future benefits, at end of year, net		$10,860		$8,803

* The benefit payment amounts of $720 million and $634 million include $21 million and $8 million for benefit payments of plans pending trusteeship for fiscal years 1993 and 1992, respectively, and $42 million in benefits paid from plan assets by plans trusteed in 1993.

** The future benefits amount of $3,645 million and $2,726 million for fiscal years 1993 and 1992, respectively, for probable terminations includes $175 million and $26 million, respectively, in net claims (future benefits less estimated plan assets and recoveries) for probables not specifically identified.

The present value of future benefits for trusteed multiemployer plans for 1993 and 1992 reflect changes due to benefit payments, change in interest assumption, passage of time, and effect of experience.

Net Claims for Probable Terminations: As these claims are estimates, factors that are presently not fully determinable may be responsible for actual experience differing from the estimates used. The values recorded in the following reconciliation table have been adjusted to the expected dates of termination.

Reconciliation of Net Claims for Probable Terminations
(Dollars in millions)

	September 30, 1993	1992 Unaudited
Net claims for probable terminations, at beginning of year	$1,027	$ 776
New claims	487	710
Actual terminations	(220)	(394)
Eliminated probables	(12)	(20)
Change in benefit liabilities	429	(43)
Change in plan assets	36	69
Change in expected recoveries	(120)	(71)
Net claims for probable terminations, at end of year	$1,627	$1,027

Included in new claims for fiscal year 1993 is a provision for future benefit liabilities associated with certain previously terminated plans.

Note 6 -- Present Value of Nonrecoverable Future Financial Assistance and Losses from Financial Assistance

The losses from financial assistance reflected in the Statements of Operations and Changes in Equity include annual changes in the estimated present value of nonrecoverable future financial assistance. All financial assistance payments made during the years ended September 30, 1993 and 1992, had previously been accrued as losses.

Present Value of Nonrecoverable Future Financial Assistance and Losses from Financial Assistance
(Dollars in millions)

	September 30, 1993	1992 Unaudited
Balance at beginning of year	$ 94	$52
Change in allowance:		
Losses from financial assistance	20	46
Financial assistance payments (previously accrued)	(4)	(4)
Balance at end of year	$110	$94

Note 7 – Accounts Payable and Accrued Expenses

The following table itemizes accounts payable and accrued expenses reported in the accompanying Statements of Financial Condition:

Accounts Payable and Accrued Expenses
(Dollars in millions)

	September 30, 1993	1992
Due for purchase of securities	$144	$ 83
Annual leave	2	2
Other payables and accrued expenses	22	39
Accounts payable and accrued expenses	$168	$124

Note 8 – The LTV Corporation

On January 1, 1991, the restoration of three LTV Steel plans that were the subject of a 1990 Supreme Court case was finally implemented, following a district court order enforcing the Supreme Court's decision.

On June 28, 1993, LTV emerged from bankruptcy. PBGC's settlement with LTV and LTV's major creditor groups provides for an initial $2 billion infusion of funding by LTV to its restored pension plans and elimination of the remaining underfunding over 28 years. In the settlement, PBGC agreed to provide contingent value rights (CVRs) to all creditors of LTV Steel Corporation who received common stock of the reorganized entity. Under these CVRs, if LTV's common stock trades at an average price of less than $17.26 per share over the 20 trading days immediately preceding December 23, 1993, PBGC will pay cash to CVR holders to make up the difference, up to a maximum outlay of $96.25 million. Of that amount, $13.75 million will go to the restored plans. As of September 30, 1993, LTV's common stock was trading at $10.75 per share. Based on the market price at September 30, 1993, PBGC expects to pay the maximum outlay of $96.25 million to the CVR holders. This amount has been accrued as a loss as of September 30, 1993. PBGC has purchased an equivalent face amount of government obligations, with a carrying amount as of September 30, 1993, of $95 million, which are being held in a special purpose custody account and are reflected as restricted assets in the Statements of Financial Condition.

In return for the CVRs, LTV provided PBGC with stock appreciation rights (SARs), under which PBGC will receive shares of LTV common stock with an aggregate value equal to the amount by which the average price at which LTV's common stock is trading over the 20 trading days immediately preceding June 28, 1994, exceeds $18.00. There is no upper limit on the amount of shares PBGC may receive. PBGC's financial advisors determined that the CVRs and the SARs had equal and offsetting value at the time of LTV's emergence. PBGC also received two 28-year zero coupon bonds, with face amounts of $454 million and $270 million, respectively, in settlement of its claims with respect to receivables from the restored plans and the underfunding in the Republic Retirement Plan. As of September 30, 1993, the bonds have been written down to their present value, which is $28 million and $17 million, respectively.

In addition, PBGC purchased $50 million of LTV common stock, the proceeds of which were contributed to LTV's plans on June 28, 1993. PBGC paid this amount on June 28, 1993; on June 28, 1994, PBGC will receive LTV common stock worth $54.3 million at the then-current market price. As of September 30, 1993, the $50 million along with accrued interest of $3 million is included in other receivables in the Statements of Financial Condition.

Note 9 -- Contingencies

There are a number of other possible large single-employer plan terminations and some multiemployer plans that may require future financial assistance. The amounts disclosed below represent the Corporation's best estimates, given the inherent uncertainties in the process.

PBGC estimates that the range of total unfunded vested benefits on termination of single-employer plans that represent reasonably possible losses as of September 30, 1993, is approximately $13 billion to $18 billion. The lower end of the range ($13 billion) has been calculated as in previous years by using data obtained from corporate annual reports for fiscal years ending in calendar 1992. The value reported for liabilities has been adjusted to the December 31, 1992, PBGC select interest rate of 6.4%. When available, data has been adjusted to a consistent set of mortality assumptions. Plans not insured by PBGC have been eliminated from the data. Since these figures are generally based on the Financial Accounting Standards Board's Statement of Financial Accounting Standard #87 ("Employers' Accounting for Pensions") reporting requirements, no provision has been made for the possible failure of the plan sponsor to make subsequent contributions or for plan liabilities that would be incurred after that date.

The upper end of the range ($18 billion) has been calculated for some plans for which the Corporation has access to more detailed plan and participant information. This additional information allows the application of more refined estimation techniques in determining plan underfunding, including the ability to estimate the effect of termination on early retirement subsidies, as pointed out in the General Accounting Office's (GAO) December 1992 report entitled "Pension Plans: Hidden Liabilities Increase Claims Against Government Insurance Program." Thus, this number is usually higher than the number derived from publicly available information. The additional effect of shutdown benefits, where applicable, has not been estimated for either the upper or lower bound. There also are a number of other sponsors of single-employer plans with significant unfunded guaranteed benefits who could, subsequently, qualify for a distress or involuntary termination if they were to encounter serious financial difficulty.

For 1993, PBGC developed and implemented new criteria and methodology for identifying, classifying, and valuing the range of loss for multiemployer plans that probably or may possibly require future financial assistance. For those multiemployer plans that PBGC estimates will probably require future financial assistance, an amount has been included in the liability for present value of nonrecoverable future financial assistance (see Note 6). PBGC estimates the loss for those multiemployer plans that may possibly require future financial assistance as a range of approximately $140 - $230 million as of September 30, 1993.

The future financial assistance liability for each multiemployer plan identified as probable or reasonably possible requiring future financial assistance was calculated as the present value of future benefit and expense payments as of the later of September 30, 1993, or the projected (or actual, if known) date of plan insolvency, discounted back to September 30, 1993, using interest only. The present value of future benefits was calculated using the current aging model. An expense loading based on plan information was added. The projected date of insolvency was calculated using a cash flow model for which future benefit payments were developed using the current aging model. Expense payments, future contributions, and benefit accruals, up to the later of the date of insolvency or the date the last active participant is assumed to retire, were entered into the cash flow model using plan information and the aging model. Current plan assets as of September 30, 1993, were calculated using an actuarial program and were also entered into the cash flow model.

The Corporation's identification of plans that are likely to require such assistance and estimation of related amounts require complex consideration of many factors. These factors are affected by future events, including actions by plans and their sponsors, most of which are beyond the Corporation's control.

A select and ultimate interest rate assumption of 6% for the first 20 years after October 1, 1993, and 5.5% thereafter was used. The 83GAM loaded mortality table projected to 1993 using Scale H was also used.

Note 10 -- Commitments

PBGC leases its office facility under a commitment that expires on December 31, 1993. The facility has significant physical plant problems and does not meet fire safety local building codes or the requirements of the Americans with Disabilities Act. During fiscal years 1993 and 1992, lease expense for such space was $5,638,000 and $5,032,000, respectively. Future minimum lease payments remaining under this commitment are approximately $1.7 million. A proffered continuation of the lease would have increased space costs substantially.

Following a competitive bid process, PBGC contracted with the low bidder for office space with a lease of 15 years beginning on December 15, 1993. The lease provides for periodic rate increases based on increases in operating costs and real estate taxes over a base amount. The General Services Administration (GSA) concurred that the lease rate was comparable to recent government transactions in the metropolitan Washington, D.C., area. Future minimum lease payments under the agreement are approximately $9 million annually.

Note 11 -- Premiums

For both the single-employer and multiemployer programs, ERISA provides that PBGC shall continue to guarantee basic benefits despite the failure of a plan administrator to pay premiums when due. PBGC assesses interest and penalties up to 100 percent for late payment or underpayment (see Note 12). Premiums for the single-employer program are $19 per participant for a fully funded plan with an underfunded plan paying up to an additional $53 per participant based on funding levels. The multiemployer premium is $2.60 per participant.

Note 12 -- Underwriting: Other Income

Other Income - Single-Employer Program
(Dollars in millions)

	For the Years Ended September 30, 1993	1992 Unaudited
Interest income - premiums	$ 1	$ 4
Penalty income - premiums	(2)	21
Interest income - employer liability	5	79
Interest income - due and unpaid contributions	22	8
Other	11	7
Total	$37	$119

Note 13 -- Losses from Completed and Probable Terminations

Amounts reported as losses are the present value of future benefits (including amounts owed under Section 4022(c)) less related plan assets and the present value of expected recoveries from sponsors. The following table details the components that make up the losses:

Losses from Completed and Probable Terminations - Single-Employer Program
(Dollars in millions)

	For the Years Ended September 30, 1993			1992 Unaudited		
	New Terminations	Changes in Prior Year Terminations	Total	New Terminations	Changes in Prior Year Terminations	Total
Present value of future benefits	$564	$ 11	$575	$789	$(121)	$668
Less: Plan assets	203	113	316	274	(278)	(4)
Plan asset insufficiency	361	(102)	259	515	157	672
Less: Estimated recoveries	20	(55)	(35)	29	(2)	27
Subtotal	$341	$(47)	294	$486	$159	645
Probables			600			251
Total			$894			$896

Note 14 -- Financial Income

Financial Income
(Dollars in millions)

	For the Years Ended September 30, 1993			1992 Unaudited		
	Terminated Plans Pending Trusteeship	Revolving Funds & Trusteed Plans	Total	Terminated Plans Pending Trusteeship	Revolving Funds & Trusteed Plans	Total
Fixed-income securities:						
Interest earned	$ 8	$ 218	$ 226	$4	$188	$192
Realized gains (losses)	(1)	226	225	2	122	124
Unrealized gains	3	1,118	1,121	0	152	152
Total fixed-income securities	10	1,562	1,572	6	462	468
Equity securities:						
Dividends earned	0	19	19	0	11	11
Realized gains	0	119	119	2	15	17
Unrealized gains	1	11	12	0	78	78
Total equity securities	1	149	150	2	104	106
Other income (losses)	(1)	(76)	(77)	(8)	75	67
Total financial income	$10	$1,635	$1,645	$0	$641	$641

Note 15 -- President's Budget

The Chief Financial Officer's Act of 1990 mandates the preparation of a reconciliation to the Budget. The reconciliation adjusts the operating expenses as reported in the Fiscal Year 1993 Statement of Operations and Changes in Equity to selected budgetary accounts--obligations, budget authority, and outlays--reported in the program and financing accounts as actual for Fiscal Year 1993 in the President's Fiscal Year 1995 Budget. Consistent with the pension insurance program's budgetary treatment, the program and financing accounts in the Budget reflect the collections and outlays for the Corporation's revolving funds and authorized use of trust fund assets to pay a portion of operating expenses. The program and financing accounts do not include off-budget accounts for the Corporation's trust funds.

The reconciliation adjusts the reported operating expenses by adding outlays that are not operating expenses and subtracting operating expenses that do not require outlays in Fiscal Year 1993 and/or are charged to the off-budget trust funds. Amounts presented represent the combined total for the Corporation's Single-Employer and Multiemployer Programs.

Reconciliation Of Operating Expenses To The Budget
For Fiscal Years Ended September 30, 1993 and 1992

(Dollars in millions)

	September 30, 1993	September 30, 1992 Unaudited
Underwriting expenses	$1,140	$ 775
Financial expenses	1,508	1,111
Total operating expenses as reported in Statement of Operations and Changes in Equity	$2,648	$1,886
Add adjustments for:		
Current year benefit payments	$ 659	$ 628
Prior year benefit payments	40	
Financial assistance payments	4	4
Adjustments added	$ 703	$ 632
Less adjustments for:		
Loss from completed terminations	$ 294	$ 645
Loss from probable terminations	600	251
Loss from financial assistance	20	46
Loss on contingent valuation rights	96	
Actuarial adjustments-underwriting	33	(257)
Actuarial charges due to		
Passage of time	373	426
Changes in interest rate	1,125	678
Prior Year adjusting entries	(23)	(37)
Adjustments subtracted	$2,518	$1,752
Total obligations per the budget	$ 833	$ 766
Plus: Obligated balance, start of year	$ 149	$ 219
Adjustments in unexpired accounts	(17)	
Less: Obligated balance, end of year	150	149
Outlays (gross)	$ 815	$ 836
Adjustments to gross budget authority from Offsetting collections		
Interest on U.S. securities	$1,054	$ 233
Premium income	911	933
Other income	10	0
Reimbursements from trust funds	348	325
Total offsetting collections	$2,323	$1,491
Outlays (net)	$(1,508)	$ (655)

Note 16 – Employee Benefit Plans

All permanent full-time and part-time PBGC employees are covered by the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Full-time and part-time employees with less than five years service under CSRS and hired after December 31, 1983, are automatically covered by both Social Security and FERS. Employees hired before January 1, 1984, participate in CSRS unless they elected to transfer to FERS by June 30, 1988.

The Corporation's contribution to the CSRS plan equals the 7 percent of base pay contributed by employees covered by that system. For those employees covered by FERS, the Corporation's contribution was 13.7 percent of base pay for 1993 and 1992. In addition, for FERS-covered employees, PBGC automatically contributes 1 percent of base pay to the employee's Thrift Savings account, matches the first 3 percent contributed by the employee, and matches one-half of the next 2 percent contributed by the employee. Total retirement plan expenses amounted to $4 million and $3 million in 1993 and 1992, respectively.

These financial statements do not reflect CSRS or FERS assets, accumulated plan benefits, or any unfunded plan liabilities applicable to PBGC employees. These amounts are reported by the U.S. Office of Personnel Management (OPM) and are not allocated to the individual employers. OPM accounts for federal health and life insurance programs for those retired PBGC eligible employees who had selected federal government-sponsored plans. PBGC does not offer other supplemental health and life insurance benefits to its employees.

Note 17 – Cash Flows

The following is a reconciliation between the net income (loss) as reported in the Statements of Operations and Changes in Equity and net cash provided by operating activities as reported in the Statements of Cash Flows.

Reconciliation of Net Income (Loss) to Net Cash Provided by Operating Activities for Years ended September 30, 1993 and 1992
(Dollars in millions)

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	1993	1992 Unaudited	1993	1992 Unaudited	1993	1992
Net income (loss)	$ (160)	$ (234)	$107	$6	$ (53)	$(228)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:						
Net appreciation in fair value of investments	(1,247)	(395)	(97)	(17)	(1,344)	(412)
Net income of terminated plans pending trusteeship	(8)	0	0	0	(8)	0
Loss on completed and probable terminations	894	896	0	0	894	896
Loss on contingent valuation rights	96	0	0	0	96	0
Actuarial charges and adjustments	1,529	848	2	(1)	1,531	847
Benefit payments - trusteed plans	(657)	(626)	(2)	(2)	(659)	(628)
Cash received from plans upon trusteeship	9	18	0	0	9	18
Changes in assets and liabilities, net of effects of trusteed and pending plans:						
(Increase) decrease in receivables	105	(68)	2	(2)	107	(70)
Increase in present value of nonrecoverable future financial assistance	0	0	16	42	16	42
Increase in unearned premiums	3	7	1	0	4	7
Increase (decrease) in accounts payable	2	12	0	0	2	12
Net cash provided by operating activities	$ 566	$ 458	$29	$26	$ 595	$ 484

Note 18 – Litigation

PBGC records as a liability on its financial statements an estimated cost for unresolved litigation to the extent that losses in such cases are probable and estimable in amount. In addition to such recorded costs, PBGC estimates that possible losses of up to $300 million could be incurred in the event PBGC does not prevail in these matters.

Note 19 -- Restatement of 1992 Multiemployer Financial Statements

The Multiemployer Program's 1992 liability for the Present Value of Non-Recoverable Future Financial Assistance, and related losses from financial assistance, were restated to reflect additional liabilities of $34 million as a result of obtaining information on certain plans which was not previously available. Accordingly, the accumulated results of operations as of September 30, 1992 has been restated from $203 million, as previously reported, to $169 million.

Comments From the Pension Benefit Guaranty Corporation

Pension Benefit Guaranty Corporation
PBGC 1200 K Street, N.W., Washington, D.C. 20005-4026
(202) 326-4010

Office of the Executive Director

April 26, 1994

The Honorable Charles A. Bowsher
Comptroller General of the United States
United States General Accounting Office
Washington, D.C. 20548

Re: FINANCIAL AUDIT - Pension Benefit Guaranty Corporation's 1993 and 1992 Financial Statements

Dear Mr. Bowsher:

Thank you for the opportunity to comment on the draft report of the GAO's audit of the PBGC's 1993 and 1992 financial statements.

It has been a major objective of the PBGC to receive a "clean opinion" from the GAO on our financial statements. We are delighted that your report finds that the PBGC's single-employer and multiemployer statements of financial condition and our statements of operations and changes in equity and cash flow to be reliable in all material respects. We concur with the findings and we are grateful for GAO's assistance in achieving this milestone.

Your report also notes significant progress in the development of internal controls affecting financial reporting and the agency's initiatives to upgrade our management information systems. Again, your assistance has been invaluable.

It is in this context that we address the issues raised in your report: the long-term viability of the single-employer program, employee benefit plan audits and reporting, and certain internal controls.

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1. Long-Term Viability of the Single-Employer Fund. Assuring the long-term viability of the single-employer fund is a major priority of this Administration. On October 27, 1993, the Administration sent the Retirement Protection Act of 1993 to Congress. We seek swift passage of this legislation. If enacted, it will markedly reduce pension plan underfunding and close the PBGC deficit.

The Honorable Charles A. Bowsher
April 26, 1994
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2. Employee Benefits Plan Audit and Reporting. These issues fall within the purview of the Pension and Welfare Benefits Administration at the Department of Labor. It is our understanding that the Department of Labor will be introducing legislation on these matters in the near future.

3. Internal Controls. The agency is making significant progress in strengthening our internal controls relating to financial systems, multiemployer plans, and nonfinancial participant data.

a. Financial Systems and Controls. Accounting, premium collection, and systems issues are the subject of careful attention and progress. We have expanded our accounting policies and procedures manual and established a financial policy, procedures and control oversight division. We are implementing interim financial statements. In addition, we established a centralized audit function to monitor and test all financial operations and supporting information systems.

As you are aware, the agency has reached back and collected almost $60 million in overdue premiums, and we are now current in our collection efforts. We are developing a state-of-the-art automated premium system. It will account for and process premiums for single-employer and multiemployer plans, and strengthen our collection efforts. We anticipate this system will be operational by October 1, 1994.

The PBGC is developing data and systems framework that will integrate our current financial systems and ensure standards for consistent future applications development. We have recently completed a joint effort with GAO to assess our information resources infrastructure, planning, and project management. We have initiated a staged systems integration project which will eventually result in an enterprise systems architecture encompassing network infrastructure, corporate business processes, data, and computer hardware and software. This system will fully integrate our primary and subsidiary financial systems.

b. Multiemployer Fund. The PBGC is improving its controls over the assessment of the Multiemployer Fund's liability for future financial assistance. We are finalizing an automated multiemployer plan financial database, to be operational in July. This system will provide a single database containing historical data which can be used to assess multiemployer plan financial trends and serve as a source to verify the reasonableness of current plan data.

We have also strengthened our internal processing and oversight of multiemployer plan cases. We now receive Form 5500's for multiemployer plans monthly from the Department of Labor rather than annually; forms for the 200 most critical

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multiemployer plans are received directly from the IRS. We adopted new procedures governing the input of financial data for multiemployer plans into the PBGC's financial statement. We have established a Multiemployer Plan Contingency Group which assesses the documentation of the financial data for multiemployer plans. Finally, we are developing revisions for PBGC Form 1 for premium payments that will ensure that we receive more complete and current financial data.

c. Nonfinancial Participant Data. We are continuing to take steps to ensure that the nonfinancial participant data that is required for the PBGC's financial statements is accurate. For example, the automated transfer of participant data to the PLUS payment system maintained by State Street Bank contains edits to ensure that the data is consistent and logical. We will soon be implementing similar edits for data that is input manually. We also operate a "plan close-out program" which matches participant data in the paper file to the data maintained on the PLUS system when a plan is "closed."

We are computer-imaging all participant records. This will preserve records against loss and make them easier to use when servicing plan participants. We expect that at least 50% of our participant records will be imaged by the end of fiscal year 1994.

We have upgraded internal controls in our Field Benefit Administration offices ("FBA's"). Actual benefit payments are now reconciled monthly. We will perform operational audits of all 17 FBA's during fiscal year 1994.

Finally, the PBGC will implement team processing of plan termination cases. Under team processing, PBGC auditors, actuaries, and benefit administrators will simultaneously perform inter-related tasks that are currently being performed in series. We expect that team case processing will significantly improve the quality of the participant data used for financial statement purposes.

* * *

We believe that these efforts and achievements will prove fruitful. We appreciate GAO's assistance and insight and look forward to our continued cooperative efforts.

Very truly yours,

Martin Slate

Martin Slate
Executive Director

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