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Older pensions being retired

IBM latest company to drop traditional defined-benefit plan

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When Baxter International Inc.'s shareholders asked tough questions about pension funding last year, they got an unequivocal answer.

Baxter's pensions are "sacred," Chief Executive Robert Parkinson said at the annual meeting in May.

But traditional pensions are far from sacrosanct in an age when more companies, including big, profitable employers with well-funded plans, are shifting the risk of saving for retirement onto their workers.

The pension freeze announced this week by IBM Corp. will make it easier for large employers to stop offering retirement plans that promise a steady stream of payments for life, some experts said Friday. And, they said, it could hasten the shift to plans such as 401(k) savings accounts that provide no such guarantees.

"Now that a large, well-funded sponsor did it, it may be that some of these other sponsors won't consider it a third rail that they can't touch," said Temple University professor Jack Vanderhei, who directs a research program for the non-profit Employee Benefit Research Institute.

IBM froze its pension plan for U.S. employees, one of the nation's biggest at more than $48 billion in assets at the end of 2005, more than enough assets to meet its future obligations, the company said. The freeze follows an earlier decision to close the plan to new hires at the end of 2004.

The latest freeze will not affect the company's 125,000 retirees. But about 120,000 active employees will not earn additional benefits after 2007. Instead, they will receive larger payments to 401(k) accounts.

IBM said the change would save as much as $3 billion in retirement-related expenses through 2010 and put costs more in line with its rivals in the competitive technology industry.

The action drew sharp criticism Friday from union leaders and employee-rights groups.

"We're not looking at situations like with the steel companies and the airlines, where these industries had been deeply troubled and had to enter bankruptcy to save themselves," said John Hotz, deputy director of the Washington, D.C.-based Pension Rights Center.

"This is coming out of the workers' pockets and going somewhere else in the corporation. It's an arbitrary cut in compensation of the sneakiest kind, because employees won't realize it until retirement age."

IBM said its 401(k) plan would be one of the richest in the country, offering company contributions of as much as 10 percent of pay for some participants.

"We also believe these are prudent and balanced steps at a time of uncertainty and conflicting legislative and regulatory directions about defined-benefit retirement plans in the United States," Randy MacDonald, IBM senior vice president for human resources, said in a statement.

In addition to revisions to federal pension law and accounting rules, IBM faces a pending lawsuit alleging that changes to its pension plan in the late 1990s discriminated against older workers.

The suit discouraged some other companies from adopting hybrid "cash balance" plans, in which workers receive a percentage of their annual compensation, plus interest, in retirement accounts.

Traditional defined-benefit pension plans cover an increasingly smaller slice of the workforce, though about two-thirds of Fortune 1000 companies still offer them, studies show.

The percentage of private-sector employees with defined-benefit pensions has fallen to less than 20 percent from 35 percent in 1980, according to the Employee Benefit Research Institute. About 21 million full-time private-sector workers were covered by traditional pensions in 2003, the latest year for which data was available. About 43 million were covered by so-called defined contribution plans such as 401(k) accounts.

Plan freezes are increasingly common as companies try to limit the unpredictability of traditional pension plans, in which the value of assets and estimates of liabilities can swing wildly from year to year, pension experts said. Stricter accounting rules and pending federal legislation are expected to increase the volatility.

There are two kinds of freezes: closing a plan to new hires or freezing the entire plan for all covered employees, who get only the benefits they already had accrued.

Companies that recently have frozen plans to new hires include Motorola Inc. and Aon Corp. Sears, Roebuck and Co. and Verizon Communications opted for "hard freezes" affecting all employees.

In total, about one in 10 companies froze pension plans in 2003, the latest year for which information was available from the Pension Benefit Guaranty Corp., a quasi-government agency that insures private pension programs. Most of the freezes were by small employers with plans covering fewer than 100 participants, the study said.

"The [private pension] system is going to continue to shrink rather dramatically, and of those that remain, more will be these frozen plans," said James Klein, president of the American Benefits Council, which represents plan sponsors and service providers.

The shift will mean a loss of flexibility for employers that used the plans to manage their workforce, experts said. Instead of firing workers in hard times, companies offer sweetened pension payouts to induce them to take early retirement.

During the 2001 recession, workers whose primary retirement vehicle was a 401(k) plan couldn't retire because their accounts were under water.