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CASH BALANCE PENSION PLANS:  
A STUDY OF FINANCIAL REPORTING FAILURE

Abstract

Unlike other post-industrial nations, the United States relies much more on private provision of welfare benefits like pensions and health care. Perhaps surprisingly, the percentage of GDP spent on such social welfare benefits in the U.S. exceeds the percentages spent in nations such as Australia, Canada, Ireland, and Italy. However, in the U.S. the proportion of those expenditures that are private rather than public is much greater (Hacker, 2002). This greater reliance on private provision of welfare benefits is unique among so-called advanced, post-industrial economies. Whereas the beneficiaries of social welfare payments in other nations must rely almost exclusively on the mechanisms for holding governments accountable to hold the payer accountable, beneficiaries in the U.S. must rely more extensively on the mechanisms of private accountability to assure and protect their benefits. Thus, the design of financial reporting systems for private firms is much more significant in the U.S. for consummating accountability relationships between providers and recipients of social welfare benefits.

A major component of social welfare is a pension. In the U.S. workers depend on employer provided pensions or personal savings for adequate support once they are beyond working age. The government provided Social Security is subsistence support designed only to supplement private provision for old age. A new form of pension plan is being adopted by a sizable number of the largest U.S. firms -- the cash balance plan. This type of pension plan is being used to replace the traditional defined benefit plan with a plan that retains the legal standing of a defined benefit plan, but with many of the advantages (to the firm) of the defined contribution plan. In this paper, we explore financial reporting's role in providing transparency to employees about the consequences for them of conversion to cash balance plans. From numerous sources including media reports and personal discussions with affected individuals, we demonstrate that current accounting systems provide scant disclosures for allowing workers to ascertain the effects of conversion. This, in turn, facilitates the ease with which firms can shift income risk from shareholders to workers.

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Accounting for and ownership of employee pensions has long been a controversial and contested arena in the U.S. Much research has focused on assessing current accounting rules, or on examining forces affecting how standards setters establish the rules (e.g., Daley and Tranter; 1990; Francis, 1987). Other researchers have focused on whether pension liabilities or “excesses” (as defined by applicable accounting standards) are impounded in equity prices and debt prices (e.g., Tinker and Ghicas, 1993; Reiter, 1991; Pontiff, et al, 1990; Barth, 1991). Historically, the controversy over pension accounting centers round ownership of pension funds, and the role of accounting in this issue.

The newest development is the emergence of cash balance pension plans. Extensive press coverage of concerns that arose among employees when companies changed from traditional defined benefit pension plans to cash balance plans raises the question about how accounting rules facilitated or failed to facilitate informing employees about the consequences of the transition.

This paper begins by reviewing the nature of how social benefits like retirement income are provided in the U.S. Next the characteristics of cash balance plans are discussed. The next section explores the role of accounting and analyzes the disclosures of firms converting to cash balance pensions. The role of other players in the pension arena is then discussed. Particular emphasis is placed on popular and financial press coverage because of the visibility created by these forums. Throughout the paper, individual examples and stories will be used to show the impact on workers when companies convert to cash balance plans.
Social Welfare Benefits in the United States

The two largest social welfare benefits that are provided to citizens in the so-called Western, industrialized nations are health care and pensions. Among these countries, the U.S. stands apart from the others by virtue of the fact that these fundamental social benefits are provided by private means to a much greater extent in the U.S. than in other OECD countries. The U.S., alone among economically advanced nations, has no universal health insurance for working age adults and their children, instead relying on employer provided private insurance as the primary means by which health benefits are provided. The elderly and the poor are insured through a national health insurance program, but the working age population relies upon employer provided private plans for health benefits.

Likewise, pensions are much more extensively a private affair in the U.S. than in other western countries. How that came to pass is a rather complex series of historical events. Hacker (2002) provides a historical analysis of the development of pension benefits in the U.S. Institutions and the policy choices about welfare benefits they make through time determine what the configuration of those benefits will be. The historical path leading to the current state of the distribution of welfare benefits is often directed in certain ways by the early choices made and the subsequent extent to which large institutions with vested interests are erected to accommodate the policies. This path dependent nature of the provision of pension benefits in the U.S. is traced by Hacker (2002) commencing with the passage of Social Security legislation as part of Franklin Roosevelt's "New Deal" programs to help the U.S. recover from the Great Depression. It is not the purpose of this paper to delve extensively into the historical circumstances leading to the current state of pension provision in the U.S. Historically, the advent of Social Security, which provided only a minimum level of retirement income, coupled
with the exploitation of that program by the powerful U.S. business interests, has led to the U.S.

system of old-age income provision. This system is more extensively skewed toward private

provision of pension benefits than in any other western country. Consequently, benefits are more

extensively skewed toward the highest income earners.

The distribution of pension benefits among the populace of different countries is
determined by the institutional structures of the various welfare states. The U.S. model of
retirement income provision is one described by Korpi and Palme (1998) as one of "basic
security," i.e., everyone pays a flat rate and is guaranteed minimum benefits. Other models exist:
"targeted," i.e., social insurance aimed at only the poorest citizens; "voluntary state-subsidized;"
"corporatist," i.e., earnings related by occupational category with labor force participation in

governance; and "encompassing," i.e., both a flat rate and earnings related, which is the
Scandinavian model (Korpi and Palme, 1998, p. 666). As Korpi and Palme report on their
comprehensive study of the distribution effects of various models, there is a paradox in the re-
distributive effects associated with the various models. Because the encompassing model links
the interests of the poor and the middle classes to the same pension system, the end result is less
poverty and income inequality than in those systems where the focus of the government provided
program is on only provision of minimal means for all. As Korpi and Palme (1998, p. 671) state
it,

We hypothesize that the structure of social insurance institutions can emphasize
differences in risks and resources by increasing homogeneity within risk pools
in terms of their socioeconomic composition, or they can play down these
differences by pooling resources and sharing risks across socioeconomically
heterogeneous categories. Social insurance institutions thereby can shape the
processes of defining interests and identities among citizens, the rational
choices citizens are likely to make, and the ways in which they are likely to combine
for collective action.
Consistent with their hypothesis, K & P's study, using data from 1985, found that income inequality and poverty rates for the elderly were lowest in those countries employing an encompassing model and highest in those countries employing a basic security model (K&P, 1998, p. 678). Of the eleven OECD countries included in the study, the U.S. had the highest Gini coefficient (a measure of income inequality) and the highest poverty rate (defined as the percentage of the population below 50 percent of the median income).

The position of the U.S. relative to other nations re retirement incomes is to a considerable degree a function of the extensiveness with which social benefits are privatized. As noted above, no other country relies to such a great extent on private protection for the two fundamental risks that every citizen faces -- sickness and subsistence beyond the age of employment. Providing for health care and old-age income are political decisions; they are not inevitably the result of natural capitalistic economic order since there is diversity among capitalist nations in the means and, consequently, the distribution of these risks among all of the citizens. Hacker (2002, p. xiii) describes the consequence of privatized social benefits in terms of their political ramifications:

The politics of private social benefits … is "subterranean" politics -- far less visible to the broad public, far more favorable to the privileged, far less constrained by the features of American politics the routinely stymie major social reforms, and far more dominated by conservative actors than the making of public social programs.

In the U.S. these privatized benefits for retirement income are provided, for the most part, only by corporate employers, it at all.

Two salient consequences of privatized pensions provided by employers have been that, 1) lower paid workers are much more likely not to be included in a plan and, 2) since institutionally the provider and recipient have conflicting interests with respect to the provision
of benefits, there has been a recent movement to shift risk more toward recipients (employees). As corporate interests come to increasingly dominate the U.S. political process (Phillips, 2002; Kelly, 2003; Bakan, 2004; Nace, 2003; Drutman and Cray, 2004), it has emboldened employers to shift risks from themselves onto employees. The recent increase in the number of employers switching to cash-balance pension plans is symptomatic of this risk-shifting phenomenon.

Overview of Cash Balance Plans

During recent years, companies in the United States have attracted publicity in both the popular and financial press by changing their defined benefit pension plans. More than three hundred companies, with hundreds of billions of dollars in pension assets, have switched from conventional defined benefit plans to cash balance plans (Hitt, December 15, 1999). Sixteen of the 100 largest U.S. companies had cash balance plans in 1999; none of this group had these plans a decade ago (Oppel, July 14, 1999). A GAO study (00-185, p. 9) reports that as of July, 2000, about 19 percent of the Fortune 1000 sponsored cash balance plans.

Though legally cash balance pensions are classified as defined benefit plans, these plans involve changes to the corporate pension formula so that they resemble defined contribution pensions. Most traditional defined benefit plans base pension payments to retirees on a formula that combines a percentage of final pay (or highest final average pay) with the number of years worked (GAO, 00-185, pp. 6-7). Under typical cash balance plans, companies contribute a percentage of an employee's pay to an account every year, and then guarantee that money will

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1 George W. Bush's proposal to privatize Social Security is an attempt to do with the public pension benefit what firms have done with the private pension benefits. If Social Security is privatized it will no longer be social or security since the state will no longer guarantee a minimum subsistence to everyone in old age. Instead, each individual will control his or her retirement account. The value will depend on the luck each citizen has with respect to the investment decisions they make and, also, the luck that the value of those investments during that specific
grow at a certain rate, e.g., the yield on a U.S. Treasury bill. A GAO study (00-185, p. 15) found that 80 percent of companies surveyed tied interest rate credits to the return on a Treasury security. Many firms credit interest based on the yield for 30-year Treasury bonds; others use the one-year Treasury bond. At retirement, or when employment is terminated (if vesting requirements are met), the amount in that account is the pension. Cash balance plans are subject to the same ERISA funding regulations as traditional benefit plans (Rohrer, 1995), and also are insured by the Pension Benefit Guaranty Corporation (Stewart and Yaffe, 1989).

One of the more controversial accounting and reporting aspects of cash balance pension conversion is determining the beginning balance in each employee’s account. Firms are legally prohibited from amending a plan’s benefit formula to reduce benefits that have already accrued. However, the law does not govern how companies set opening account balances, and it does not protect future benefit accruals (GAO, 00-207, pp. 11-12). Conversions to cash balance plans frequently result in situations, called “wearaway” periods, where some workers do not earn additional benefits for several years after conversion. A wearaway period occurs when the employee’s opening cash balance amount at conversion is less than the present value of his/her accrued benefits. During this wearaway period, pay and interest credit contributions do not really result in “new” pension benefit accruals until the cash balance account exceeds the value of benefits accrued under the previous formula. Workers who leave during this wearaway period are entitled by law to receive the higher benefit accrued under the earlier pension benefit formula. Companies are free to set the opening balances with any discount rate and set of mortality assumptions they choose (GAO, 00-185, pp. 28-30), thus whether or not a wearaway period exists is a function of employers’ decisions at the time of conversion.

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time period when they are not longer able to work is sufficient to their basic needs. Under such a scheme, the volatility of retirement income is certain to increase.
A primary appeal for companies implementing cash balance plans is that these plans are less costly than traditional defined benefit plans. *The New York Times* reports that cash balance plans often save companies millions of dollars a year (Oppel, July 14, 1999). A PriceWaterhouseCoopers survey (2000) finds that 56 percent of employers anticipated their accounting costs would decrease in the short-term following a cash balance conversion. According to a GAO survey (00-185, p. 12) several of the Fortune 1000 cited financial implications of changing to a cash balance plan as a key reason for their decision. A major allure is that companies can benefit without incurring the costs related to plan termination. For example, by converting to a cash balance plan, the company can extend the period of time to forego making contributions while still having the plan considered to be fully funded (00-185, p. 13).

Some companies candidly acknowledge the cost-saving motivation generated by switching to cash balance plans. "Reducing front-end costs was one reason Thompson Consumer Electronics . . . switched from a traditional defined benefit to a cash balance plan . . . We could not afford the final average earning plan," says Linda Wych, pension fund manager for Thompson's U.S. division (Elgin, 1991). When CBS switched from its conventional pension plan to a cash balance plan, it openly acknowledged that the cash balance pension plan would save the company money and reduce employee pensions (Schultz and Pope, 1999). IBM’s initial approach when converting was to give all Canadian workers, but only certain U.S. workers, the right to remain in the old pension plan. When asked the rationale for such disparate treatment, J. Thomas Bouchard, IBM's senior vice president for human resources, said it "simply would have cost too much" to allow all employees to remain in the original plan (Burkins, 1999). IBM subsequently altered its stance to include more U.S. workers.
Constructing the Pension Problem

Because of the extreme importance of private pension benefits to employees, one would expect managers to verbalize less shareholder-serving rationales than "cost cutting" for altering pension plans. Analogous to what Arnold and Oakes (1998) concluded about the discursive construction of retirement health benefits, we find parallels in how the corporate sector constructed the pension problem. Companies offered numerous employee-centered rationales to suggest that cash balance plans would be more appealing to younger employees, with the subtle message that this appeal to younger workers is implicitly more desirable. "Cash balance plans are often seen as damaging to people on the brink of retirement, but there's a pro side to that -- they are also enormously beneficial to younger workers," according to Richard Thau, executive director of The Third Millennium, a New York-based non-partisan research organization working on issues of concern to Generation X (Anand, April 19, 1999). The apparent logic is that traditional defined benefit plans were designed for a workforce where employees spent the bulk of their career with one company, and that this model no longer portrays today’s economy.

Employer rhetoric emphasizes the claim that cash balance plans are advantageous for employees both because they promote a better understanding/appreciation of retirement benefits and because they are portable. Gordon Gould, chief actuary at Towers Perrin, says that cash balance plans can be an effective way for companies to attract younger workers who are likely to change jobs frequently (Dugas, 1999). According to the legislative bulletin for the Erisa Industry Committee, a group of employers, law firms and actuarial consultants, “Cash-balance designs offer significant advantages [to those] who move in and out of the workforce. [Such employees] are more likely to accrue a significant and secure retirement benefit under cash balance plans than under many other designs,” (Schultz, December 16, 1999). A spokesperson for Casual
Corner Group says, “With a young work force with high turnover, the cash-balance plan provides a significantly bigger benefit for younger associates.” (Schultz, December 16, 1999). Lucent supported establishing a cash balance plan for non-union workers hired after January 1, 1999 because "younger workers prefer these hybrid plans to stodgy traditional pension plans" (Anand, May 17, 1999).

Employers also attempt to position cash balance plans as fairer, because traditional plans are heavily weighted toward older, longer-serving workers and away from the shorter-term employees that make up an increasingly visible segment of the U.S. labor force. The BOC Group, an international company with about 35,000 employees worldwide, and 10,000 based in the United States, was one of the first companies to adopt cash balance plans in 1986. A spokesperson for the BOC Group suggests that the cash balance plan provides "equal pay for equal service, regardless of the participant's age at hire. For example, a 25-year-old new hire and a 45-year-old new hire who consistently earn the same compensation accumulate equal cash-balance pension benefits during the time they work for BOC. This is a shift away from the earlier plan, which would provide higher benefits to the 45-year old and cost the company more.” (Murray and Murphy, 1997)

However, emerging evidence suggests that this appeal to younger employees may be simply a rhetorical ploy to create an antagonism of interests between younger and older workers (much as the Bush administration is attempting to do with the Social Security program). Despite espoused advantages of these plans for today’s workforce, many young employees do not benefit from cash balance plans because companies typically do not change the vesting requirement. According to Labor Department data, the median job tenure for workers aged 25 to 34 is 2.7 years (Schultz, December 16, 1999). Since a majority of firms have five-year cliff-vesting requirements (GAO, 00-185, p. 14), it is clear that substantial numbers of employees do not benefit from the much-touted portability feature of cash balance plans. For example, at SBC
Corporation’s Southern New England Telephone unit, fifty-four percent of unionized employees who were in cash balance plans (but had not yet vested) left the company in 1997. At MCI Communications, fifty-seven percent of those who were in the plan but had not yet vested left in 1997. Based on a review of pension documents filed with the IRS for 1997, The Wall Street Journal also reports that the five-year vesting requirement prevents countless younger employees from gaining any benefit at all from cash balance plans (Schultz, December 16, 1999). In a recent study D'Souza, et al. (2004) tested the portability rationale versus the cost cutting rationale and found that rather than promoting portability the decision to convert to cash balance plans "…represent cost reduction measures that reduce benefits implicitly promised to employees (D'Souza, et al., 2004, p. 1)."

Companies, also, frequently tout the perceived simplicity of cash balance plans compared to traditional defined benefit plans as one of their primary benefits. The BOC Group notes that, "Instead of an esoteric formula, participants see a straight dollar amount, and they understand that better. This allows participants to appreciate the value of the pension benefit that the company is providing to them." (Murray and Murphy, 1997, p. 33). David Clements, director of compensation and benefits for Catholic Health Corporation, asserts that employees like the cash balance plan because it is similar to having a savings account with a balance that they can watch grow (Elgin, 1991).

While cash balance plans per se may be easier to understand, comparing benefits before and after cash balance conversions is far from clear. When Central & South West Corporation announced its changeover to cash balance plans, Jim Bruggeman, a company engineer, spent about a year trying to understand the new system (“Employers Win Big,” 1998). Schultz notes
that, "Short of hiring an actuary, you probably can't figure out whether you're better or worse off if you're a veteran at your company" (December 4, 1998).

Unlikely alliances develop when companies convert to cash balance plans. Schultz observes that the impact of cash balance plans increasingly extends beyond unionized labor to the executive floor (July 1, 1999). Generally, employers can unilaterally reduce or eliminate future pension benefits for nonunionized workers. In contrast, collectively bargained employees typically have the option of rejecting cash balance plans or negotiating better provisions – if they understand the issues. When Niagara Mohawk Power Corporation adopted a cash balance plan for salaried employees in 1999, it convinced the International Brotherhood of Electrical Workers union that it was good for those workers as well. Several union members subsequently filed charges against the company and the union with the National Labor Relations Board, charging that the company did not provide sufficient information for the union to make an informed decision. At the same time, midlevel managers at the utility were trying to determine how their benefits under the new plan compared to benefits under the old plan. A group of managers worked with the union to construct computer models, and they estimated that pensions for some longtime employees had been reduced by forty percent (Schultz, January 21, 1999). This is indicative of the lower visibility and traceability of private versus public benefits (Hacker, 2002, p. 42). For example, with the U.S. government Social Security program the visibility is pronounced. A fixed amount is withheld from pay every pay period and the benefits of this policy are easily traceable because the Social Security Administration provides each citizen with an accounting of what his/her expected benefit will be.² Private plans lack the visibility and traceability of public ones as evidenced by the cases noted where individual employees were able

²This is why the Bush administration's plan to replace traditional Social Security with a "cash-balance" plan will likely meet more organized opposition because the costs and benefits to each recipient will be easier to ascertain.
to assess consequences only through great effort. Also, this major change in pension policy is affected through thousands of employers, so the ability of employees to question the policy as national policy is limited because the policy appears to be isolated to each employer. Employees of say, IBM and Bank of America, have a much more difficult time understanding they have mutual interests vis a vis U.S. pension policy than they will understanding their mutual interests vis a vis Social Security.

An additional advantage to cash balance plans for investors is the opportunity to utilize pension assets to generate earnings in excess of those promised and paid to employees. This interest arbitrage strategy is possible because from the employee perspective, cash balance plans by company rhetoric are made to appear similar to defined contribution plans. However, many companies anticipate that actual return on pension assets will exceed the return promised to employees (and credited to their pension accounts), and they can keep the excess amount earned (Rohrer, 1995; Gold, 2000). For some companies, the intent is to set the rate paid below the rate of anticipated investment return, thereby allowing the company to reduce future contributions to the pension fund (Stewart and Yaffe, 1989; Anand, May 17, 1999).

NationsBank Corp. (now Bank of America) has taken a somewhat different approach to its cash balance plans, apparently in hope of the same interest arbitrage gains. Instead of guaranteeing a specified rate of return, the plan allows participants to direct cash balance pay credits to as many as eleven investment options. An employee's cash balance plan account is then credited with the rate of return earned by the chosen funds, even if that return is negative. But because the cash balance plan is a defined benefit plan, NationsBank has the right to invest those contributions as it sees fit, which may differ from investment options selected by employees. "While NationsBank won't discuss the matter, those who have studied the plan and
plan documents say NationsBank believes its actual investments will earn a higher rate of return than the options selected by employees. And that, in turn, will mean lower future pension contributions by NationsBank” (“Don’t Bank,” 1998). This, once again, clearly illustrates the risk shifting that occurs from shareholders to employees.

**FASB's Construction of Pensions**

Standard setters and regulators purport to be increasing efforts toward “transparency” in financial reporting (e.g., SEC, 1999). Specifically, the FASB describes its role as, “Serving the investing public through transparent information resulting from high quality financial reporting standards developed in an independent, private-sector, open due process” (FASB, October 31, 2001). FASB Chairman Jenkins notes that, “Our objective is to make sure that investors have the financial information they need to make well-informed investment decisions. Having credible, comparable, and transparent information is essential to that process.” (FASB, October 15, 2001).

The Financial Accounting Standards Board has consistently portrayed the role of accounting as a neutral one. In its Conceptual Framework, the FASB states that, “Neutrality means that either in formulating or implementing standards, the primary concern should be the relevance and reliability of the information that results, not the effect that the new rule may have on a particular interest” (FASB, 1980, paragraph 98). The FASB accentuates this point by including a quote from then-Securities and Exchange Commission chair Harold Williams noting that, “If it becomes accepted or expected that accounting principles are determined or modified in order to secure purposes other than economic measurement . . . we assume a grave risk that confidence in the credibility of our financial information system will be undermined (FASB, 1980, paragraph 104).”
Critical accountants do not share the FASB’s view of accounting as a neutral arbiter, but assert that by its very nature, accounting plays a major role in constructing reality rather than portraying reality (Morgan, 1988; Tinker, 1988; Chua, 1986; Hines, 1988). Arnold (1998) credits post-modern thought with enriching accounting theory by its insistence on viewing accounting as a social construct. Specific to the pension debate, Tinker and Ghicas (1993) assert that, “Accounting is not merely a reporter in such conflicts, it may help constitute them by encouraging takeovers and terminations without considering the full social costs of such restructuring.”

Inherent in positioning the role of accounting is establishing the role for whom. After exploring myriad potential users and why they might need accounting information, the FASB narrows its focus to concentrate on

...the informational needs of external users who lack the authority to prescribe the financial information they want from an enterprise and therefore must use the information that management communicates to them (FASB, 1978, paragraph 28).

The Board then further refines its focus to assert that

Financial reporting should provide information to help present and potential investors and creditors and other users in assessing the amounts, timing, and uncertainty of prospective cash receipts from dividends or interest and the proceeds from the sale, redemption, or maturity of securities or loans (1978, paragraph 37).

Though the FASB acknowledges other users in the financial reporting process, it is clear that the primary user focus is on capital providers.

It is apparent that, in spite of the FASB's claims of neutrality, accounting rule making is decidedly not neutral. The avowed position of neutrality is a rhetorical devise to legitimate the power of the FASB to write law without the normal democratic accountability. By serving an idealized, imaginary "investor" located in an idealized "efficient" market rather than serving any real economic actors with real economic interests, the FASB claims to be performing a valuable
social role by mandating the provision of information that results in the economically efficient allocation of society's resources. However, society is also political terrain, particularly when the issues are the provision and distribution of social benefits like health care and retirement income. Investors are not the only constituency with something at stake and investors interests are in conflict with those of employees -- placed emphatically so by accounting's characterization of employee pensions as a "cost" to investors.

A thought experiment suggested by Kelly (2003) illustrates the way accounting rule makers gloss the essential political nature of its alleged economic naturalism. As Kelly (2003, p. 21) succinctly puts it, "A primary bias built into financial statements is the notion that stockholders are to be paid as much as possible, whereas employees are to paid as little as possible. Income for one group is declared good, and income for another group is declared bad." Obviously, a neutral system of accounting rules would be indifferent to which constituency's interests were more important. But, as Kelly illustrates, this preference for one constituency is embedded in the way rule makers valorize profit (euphemistically now called "earnings") in the simple profit equation, Profit = Revenues - Expenses. Profit is understood by accounting rule makers as synonymous with "capital income." Since employee income (including pension benefits) is regarded as an expense, the profit model that informs the FASB's alleged neutrality becomes: Capital income = Revenues - (Employee income + other factor costs). However, simple algebra permits us to retain the arithmetic identity by rearranging terms to yield, Employee income = Revenues - (Capital income + other factor costs). That is, maximizing employee income could be as equally valid an objective for corporate management as maximizing shareholder income. Indeed, the early history of corporations in the U.S. illustrates that corporations were chartered by states to perform only functions in the public interest, e.g.,
construction of canals, highways, etc. (Nace, 2003). Maximizing shareholder income was not an objective for corporations contemplated in state law.

What is the inherent bias in the FASB model of the world is the mistaken supposition that the corporation is a "natural" being. It is decidedly not, but is a creation of the state. It is a being inherently political in its creation and evaluation. Indeed, its motivation and goals must be provided to it via law and the political process, since as a non-sentient being, it is not capable of providing those things for itself (Baken, 2004). The accounting narrative of the FASB constructs the corporation as a natural economic being synonymous with shareholders. But the history of the corporate form in the U.S. belies that narrative. The FASB model is mythology (Yamaji, 2003). The corporate being is an institution created by the state, which over time has, through the political process, been afforded rights and powers that had been reserved earlier for only flesh-and-blood humans. In the U.S. it is an instrument of the state used as a primary deliverer of health and retirement benefits. Without adequate "information" about the performance of that institution with respect to provision of those benefits, relative to other policy options, citizen/employees are disadvantaged in the process of political decision making over the provision and distribution of basic social welfare.

We can observe the inherent bias in the rule making process via the fact that the definition and measurement of corporate pension obligations has long been contested territory. Were it simply a matter of "faithful representation," the coherent, cognitive foundation established over the past century should unambiguously point to a reliable measurement rule.\(^4\) But an unresolved issue has been determining what is the nature of the pension promised to employees. A fundamental question is whether the obligation to employees is the explicit

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\(^3\) The following series of equations are adapted from Kelly's (2003, p. 22).

\(^4\) That accounting lacks such a coherent cognitive foundation has been cogently argued recently by West (2003).
written legal liability or the implicit economic liability implied by past and existing company practice (Frances and Reiter, 1987). Because of the politically contested nature of the pension agreement, perceptions of market players and stakeholders become important. Reiter (1992) found that participants in debt markets view pension contracts in terms of implicit agreements to continue plans into the future, i.e., as obligations in the form of a permanent covenant with employees. Reiter’s research added to the work of Pesando (1985) and Ippolito (1985) that found that participants in labor and equity markets view pension agreements this way (implicit contract model), rather than merely termination obligations (explicit contract model). Barth’s (1992) work provides further support that investors view pension obligations, including projected future salary progressions, as firm liabilities resulting from a continuing employment promise.

Tinker and Ghicas (1993) analyzed the constitutive role of accounting by asserting that current accounting practice is consistently biased against employee interests and may help constitute conflicts. Specifically, they found that pension “excesses” motivated a significant number of corporate takeovers between 1981 and 1985. Though their study was based on existing GAAP (SFAS 36) during that time period, current GAAP does not resolve the ambiguities inherent in pension conflicts.

Current U.S. pension accounting and reporting rules relevant to this paper are governed by Statement of Financial Accounting Standards 87, “Employers’ Accounting for Pensions,” and Statement of Financial Accounting Standards 132, “Employers’ Disclosures About Pensions and Other Postretirement Benefits.” From a balance sheet perspective, a case can be made that SFAS 87 misstates pension obligations by requiring recognition only of the minimum liability. The service cost component of pension expense is based on projected future salary levels, so this
particular understatement does not impact the income statement. Since the balance sheet minimum liability recognition is based on current salary levels, the pronouncement adopts the explicit contract view, and not the generally more prevalent implicit contract perspective (Wolk and Tearney, 1997).

Admittedly, when establishing current pension rules, the FASB did not adopt its own preferred method of accounting. Though SFAS 87 corrected some problems with its predecessor statement, SFAS 36, the Board noted that some preferred methods would represent “too great a change from past practice to be adopted at the present time” (FASB, 1985, paragraph 107). In its background discussion of SFAS 87, the FASB acknowledges the contested nature of the ownership of pension assets.

In addressing the notion that pensions do not belong to the employer, the Board observes that, “numerous recent situations in which significant amounts of assets have been withdrawn by employers provide compelling evidence that rebuts that argument” (FASB, 1985, paragraph 112). In the background information for SFAS 132, the Board re-states its conceptual preference “to recognize a net pension liability or asset measured as the difference between the projected benefit obligation and plan assets, either with no delay in recognition of gains and losses, or perhaps with gains and losses reported currently in comprehensive income but not earnings” (paragraph 25.) The Board then positions SFAS 132 as a partial remedy of this non-recognition:

However, because Statement 87 did not require that accounting, the Board decided that this Statement should require disclosure of additional information about the changes in the benefit obligation and the fair value of plan assets during the period, including unrecognized gains and losses (paragraph 25).

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5 SFAS 88, “Employers’ Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,” provides accounting rules for events noted in its title. However, that pronouncement is not relevant for this research because cash balance conversions generally represent neither settlements nor curtailments.
Changes in accounting standards are generally reactive rather than proactive (Reither, 1997). Since standard setters tend to act in response to perceived problems, construction and visibility of problems is an essential component of revising accounting rules. Issues that emerge onto the FASB’s agenda must first be constructed as problems (Young, 1993). According to the FASB, existing pension disclosures were problematic because discussions with certain users of financial statements indicated that the disclosures required by Statements 87 and 106, although extensive, did not provide sufficient information to understand the changes in the benefit obligation or to analyze the quality of earnings. This Statement is intended to enhance the utility of the information disclosed (SFAS 132, paragraph 24).

The Board then positions SFAS 132 as an appropriate resolution to this problem:

The Board believes that an explanation of the changes in the benefit obligation and fair value of plan assets in the form of a reconciliation of the beginning and ending balances will provide a format for more complete disclosure that also should be more understandable to users of financial statements (paragraph 31).

Clearly, the FASB has constructed the pension problem as one of a cost to shareholders.

The FASB sets forth six components of pension expense in SFAS 87. When companies change from traditional defined benefit plans to cash balance plans, some components of pension expense may be affected to varying degrees. The following paragraphs will explore the potential impact on the service cost, return on plan assets, and prior service cost components of pension expense.

Service Cost. The FASB defines service cost as, “the actuarial present value of benefits attributed by the plan’s benefit formula to services rendered by employees during the period” (FASB, 1985, paragraph 16). Thus, according to the requirements of SFAS 87, since conversion to cash balance plans constitutes a change in the benefit formula, and benefit formulas drive service cost, the service cost component may be affected.
Since most traditional defined benefit plans utilize final-pay or career-average pay, the bulk of expense tends to be recognized in the later periods of employment. This results in companies recognizing more expense for older workers near retirement than for younger workers earlier in their career, largely because service cost is recorded at present value, and as employees near retirement, present value increases. It would appear that service cost tends to decrease when companies convert to cash balance plans, but specific circumstances vary based on many factors, including actuarial assumptions and age of the workforce. Most importantly, SFAS 132 contains no requirement to disclose changes in service cost when plan formulas are altered.

**Return on Plan Assets.** Return on plan assets is a negative component of pension expense (it serves to reduce this cost), and it is not directly impacted when companies change plan types. However, as discussed earlier, companies frequently anticipate an interest arbitrage advantage by earning a greater return on plan assets than the amount credited to employees’ pension accounts. How interest arbitrage strategies flow through the components of pension expense appears to be subjective, but successful strategies could serve to increase the return on plan assets, thereby reducing pension expense.

**Unrecognized Prior Service Cost.** When companies alter existing plans, SFAS 87 generally requires amortization of the net impact of the change as prior service cost. Conversion from traditional defined benefit plans to cash balance plans generally constitutes a negative plan amendment, thereby reducing the firm’s PBO, so the benefit is amortized prospectively (Arcady and Mellors, 2000). If material, this PBO reduction must be disclosed in a single line item reconciling beginning and ending PBOs. While the required reconciliation appears to be the most visible disclosure requirement for cash balance conversions, it is possible for the impact of
conversion to be “netted out” with other prior service cost items, rendering this component of the conversion virtually invisible.

This section has explored alternative views concerning the role of accounting, particularly in the pension arena. The most restrictive view comes from the FASB itself, based on their objective of helping users (defined as present and potential investors and creditors) assess future cash flows. But even using this narrow view, the FASB appears to fail its own stated objective in the area of cash balance pension conversions. Even the revised pension disclosure rules contain no provisions to disclose any information – either components of pension expense or the total PBO – that would let users assess the change in cash flows resulting from the conversion. Clearly, if the FASB has failed to establish rules that signal cash flow changes to investors; employees, the people most directly affected by pension conversions certainly are not receiving relevant information to assess conversions through the financial reporting process. Accounting’s rule makers consistently defined the nature of pensions as a cost to investors and consequently contributed to help make invisible to employees the consequences of private pension policies.

Accounting – What is Invisible?

The previous sections explored how current accounting rules fail to portray cash balance conversions that informs the persons most directly affected (i.e., not representationally faithful from the perspective of employees). To assess the extent to which cash balance conversions were rendered invisible by accounting rules, analyses of financial statement disclosures for companies that converted to cash balance plans were undertaken. In addition, conversions with employees directly affected by conversions are provided to illustrate the degree to which
financial disclosures were inadequate to enable employees to understand the ramifications of what the conversion to cash balance plans meant for them.

The interviews with employees emerged only after one of the author’s earlier works in the cash balance pension area was presented at the 2000 Interdisciplinary Perspectives on Accounting Conference, and subsequently posted on the website as part of the Conference Proceedings (http:les1.man.ac.uk/ipa/). A few months after the conference, the author began receiving a barrage of e-mail from employees and retirees who had been negatively affected by their employer’s cash balance pension conversion. These workers were generally delighted that the inequity of cash balance pension conversions was finally receiving attention from the academic community. Many messages were focused on ensuring that I was exposed to the “real,” or “human” side of cash balance conversions. Their stories will be shared in a later portion of this section.

These individuals directed us to a website (www.cashpensions.org) that serves as a repository for cash balance pension plan information. One obstacle in the research had been identifying companies that converted since conversions do not constitute required financial reporting disclosures. This website contained a link listing companies with cash balance pension plans or other hybrid plans; that listing of 101 companies constituted the population for the current study.

To obtain the pension disclosures, a search of individual corporate websites for annual reports was conducted. Some companies’ financial statements were not available using this approach, and so a search of the SEC’s EDGAR database was also done. If conversions were disclosed, the disclosure for the year of the change was used, if noted. When conversions were
not disclosed, earlier financial statements were searched to the extent that they were available via any online format, using the same approach.

Of the 101 companies in the population, 57 made no reference to any sort of pension plan amendment or conversion. Three companies referenced other types of conversions (e.g., pension equity or pension savings) not encompassed by this study. Four companies referenced cash balance conversions, but were unusable for this study. The remaining 37 companies discussed or noted a cash balance conversion; these disclosures were reviewed to further explore the amount of information provided.

**Insert Table 1 about here**

Clearly, the majority of companies made no mention of conversions in their pension footnotes. As noted in Table 1, even among the disclosing group, little information was provided that would allow any user to assess the impact of the change. Specifically, two companies described the conversion as immaterial to their financial statements, ten described the conversion as material, and 25 made no reference to the impact of the change.

**Insert Table 2 about here**

The ten companies that addressed materiality of the conversions clearly provided more information than others in the population. But even from the disclosing companies, users would generally find it difficult to gain any substantive insights regarding how these changes impact future cash flows, pension costs, or pension benefits. Given the small number of companies involved in this subset, disclosures for each company individually are provided.

- American Express disclosed in its 1996 annual report that the “initial consequence of the changes [to a cash balance plan] was to decrease significantly the Plan’s projected benefit obligation and annual pension cost.”
• Central and South West reported that it “realized a savings in 1997 of approximately $20 million in pension expense and will also realize significant ongoing reductions.”

• Hannaford disclosed the impact of conversion as an amendment in the beginning and ending benefit obligation reconciliation in its 1998 financial statements.

• Herman Miller disclosed that, “The amendment converting the plan to the cash-balance formula was the primary reason for the 43.9 million change in the projected benefit obligation in 1998.” (Not stated was that the “change” was a decrease.)

• National City Corp disclosed both the impact on the PBO and on pension costs in its 1998 annual report. Specifically, the company reported a decrease of $95.8 million in the PBO, and a reduction of $14.9 in pension costs resulting from the cash balance plan.

• Niagara Mohawk disclosed a net curtailment/settlement gain of $35.3 million in its 1999 financial statements. However, this gain results from a combination of factors, and the company did not provide disclosure that would allow users to isolate the impact of the cash balance conversion.

• Owens Corning reported that the pension plan amendment to a cash balance formula resulted in a reduction in the PBO of $20 million. The company also reported that it expected “a reduction in future pension expense through the amortization of the reduction in the projected benefit obligation, reduced service cost and reduced interest cost on the projected benefit obligation.”

• Reliant Energy reported a $161 million decline in the projected benefit obligation in its 1999 financial statements.
• Tektronix reported a reduction in the projected benefit obligation of $38.9 million in its 1998 financial statements.

• U.S. Bancorp, after describing the conversion in its 1998 financial statements, reported only that the changes “resulted in a reduction in the benefit obligation during 1998.”

Clearly, the disclosures vary greatly in terms of information provided. Some companies address the impact on the PBO – the accounting measure designed to report the obligation. Others focus on earnings by noting the impact on pension expense. Still others note the significance of the change, but provide no dollar estimate of the amount.

**Insert Table 3 about here**

Next the disclosures for information regarding approaches used to credit interest to participant accounts were searched. The objective was to explore how companies might be implementing arbitrage strategies, but there was far too little detail describing how interest was credited to participant accounts to allow this analysis. Specifically, of the 37 companies disclosing cash balance conversions, 11 made no mention of how interest is credited to participant accounts and only six disclosed specific interest credit formulas. Twenty companies use a combination of factors, including experience and interest credits, that render specific calculations of amounts credited to employee accounts impossible. Since only six companies disclosed the interest credit formula, those, too, are described individually:

• Alliant Energy credits each participant’s account with a benefit credit equal to 5 percent of base pay as well as a guaranteed minimum interest credit equal to 4 percent.
• Allmerica Financial notes that in 1997-1999, eligible participants were allocated 7.0 percent of their salary.

• Bank of America allows participants to select various investment vehicles that determine earnings credited to individual accounts.

• Dun & Bradstreet notes that the percentage of compensation allocated annually to participants’ retirement accounts ranges from 3 percent to 12.5 percent, based on age and service. Participants also receive interest credits based on 30-year Treasury Bonds with a minimum interest credit rate of 3 percent.

• Eastman Kodak credits employees’ accounts with an amount equal to 4 percent of their pay, plus interest based on the 30-year treasury bond rate.

• Reliant Energy allocates credits annually based on a percentage of participant’s pay. It also discloses that the rate for 1999 and 2000 was 4 percent.

The above six companies disclosed the most information regarding how interest is allocated to individual accounts, yet without substantive additional assumptions, analyses, and reviews of documents outside the financial reporting process, it cannot be ascertained whether interest arbitrage is occurring. Since the clear majority of companies do not disclose formulas, any attempt at uncovering this tactic would require substantive further investigation.

It is clear from the results of this review that current FASB pension disclosure rules governing annual reports and SEC filings shed little light on the impact of cash balance conversions. Even employing the limited FASB-designated capital provider perspective, this section provides support for the following conclusions:

1. Most companies do not disclose cash balance conversions through the financial reporting process.
2. Of those that disclose, there is no consistency in the disclosures, and few provide sufficient information that would allow capital providers to assess the impact on future cash flows.

3. Information is not disclosed that would allow users to assess the existence or impact of interest arbitrage strategies.

Changes in accounting rules and reporting requirements tend to lag the underlying events triggering concern. However, in the cash balance conversion arena, even the revised pension disclosure rules shed little light on the impact of conversion. Employees are forced to rely on alternative sources for information regarding conversions to cash balance pension plans. Since pension policy is a political decision, politicians, the courts, employees, and the press are all significant players in identifying and adjudicating differences. The role of these other participants is explored below.

**Popular and Financial Press**

Because of the political nature of pension benefit provision, the popular and financial press, play a key role in formulating positions for players in the cash balance pension issue. Some press coverage has focused on the impact of cash balance conversions from a global perspective. The *New York Times* reports that cash balance plans can reduce the money older workers receive in retirement by one-third or more (Oppel, July 14, 1999). The *Wall Street Journal* reports that for older workers near the end of their careers, switching to cash balance plans can mean a loss in some cases of as much as fifty percent of the value of their pensions (Hitt, December 15, 1999; Schultz, September 22, 1999).

Other examples of press coverage have highlighted the plight of workers at specific companies. When both SmithKline and Aetna converted to cash balance pension plans in 1999,
the *Wall Street Journal* reported that the companies were phasing out generous early-retirement subsidies built into the pension plans. The *Journal* further noted that Aetna softened the impact on affected workers by providing the better of the old or new benefit for vested employees who left the company within the subsequent eight years. In contrast, SmithKline provided no transition benefits for workers over the age of sixty years (Schultz, April 8, 1999).

The June 15, 1999 issue of *The Wall Street Journal* describes the case of Cheryl Clevenger, a fifty-year old widow with two dependent children who had worked at Mercantile’s department store for 12 years and planned to work there until retirement. After Mercantile was purchased by Dillard’s, the new owner terminated the over-funded pension fund. Ms. Clevenger got a lump sum for the pension’s current worth of approximately $6,000 and lost her job. Dillard’s exploited a loophole in the tax code allowing companies to pay only a twenty percent excise tax (rather than the fifty percent excise tax) if one-fourth of the plan’s surplus goes into a “replacement plan.” Even after paying the twenty percent excise tax, Dillard’s was still left with nearly $117 million of former pension assets to use for any purpose (Schultz, June 15, 1999).

**Employee Activists**

Personal perspectives help to understand the human cost of cash balance conversions, as well as the unstated subtleties of the plans. Arnold’s (1998) work supports the view that accounting research is enriched by illuminating individual experiences. She uses narrative information to convey experiences of workers in a Caterpillar plant as they struggled with plant modernization efforts, noting that these narratives allowed her to see the issues through a different lens than earlier researchers who had studied modernization at the same facility. Hammond and Sikka (1996) suggest that histories of accounting are generally written in a way that ignores both the impact on and the contributions of ordinary people’s struggles. Hammond
and Preston (1992) also call for more accounting research emphasizing the inextricable nature of theory and experience. When an earlier cash balance pension works was found by an aggrieved employee, the lead author received a barrage of information subsequently via email. Their individual stories provided valuable insights to the pension problem that are obscured by the 

pension = cost model utilized by accounting standard setters.

Paula was contacted by a retired Boeing engineer and self-labeled activist on pension issues. His primary concern is that the much-touted portability aspect of cash balance plans is “a near myth” at Boeing. If employees leave the company before the earliest possible retirement date (age 55), Boeing does not allow employees to take money out of the plan, even if the employee has vested. He notes that they “stick it in an account, pay you an interest rate until you are of age to draw it, then convert the cash balance to an annuity, with severe penalty re age at first draw if below 65.”

A representative of SBC Employees for Retirement Fairness echoes the portability feature’s lack of usefulness:

It has been my experience that most employers continue to retain a vesting requirement (5 years is the norm), effectively removing the portability benefit from being applied to a ‘job-hopper’ (the last I read, a job hopper isn’t likely to remain with the same company for longer than 3 years).

Another retiree shares an additional concern about cash balance conversions:

I read with some interest your paper on Cash Balance and the role accounting plays in this issue. I have done a significant amount of work in this area and want to point out a more subtle issue, which goes to the heart of the matter. While Cash Balance is driven by accounting changes, the true issue is based on statistics. It can be shown that if an employee can reach a retirement age of 65, Cash Balance still pays a generous retirement benefit similar to what might have been possible under a previous tradition defined benefit plan. The architects of the Cash Balance plan point to this reality as if to say nothing has been lost. What they fail to mention is the statistical probabilities that anyone will actually reach age 65 in this new age work environment. This is the issue that most people have missed. The
architects knew of this issue since they were sitting on the statistics of the number of employees who would reach age 65. The also saw the future downsizings through outsourcing and mergers that even if an employee did not leave their appointed job, they were bound to lose the job under the old company to some new company and thereby lose the availability of the pension. Accounting changes in the rate of accrual from the implementation of Cash Balance was only the tool to implement this plan. It was truly the next closest thing to complete elimination of a pension plan without the associated tax liabilities.

Please don't think that age discrimination would prevent this. In reality, no employee could ever point to their own personal discrimination. It is simply a statistics game. Even if an occasional employee slips into the higher age bracket of their 60's, the reality of large numbers missing the target is all that matters. So the bottom line is, accounting was the tool, statistics were the motivation, higher profits were the outcome.

A former IBM employee focuses on the inequity of the cash balance plan. Following is his story:

At the time of the conversion, I was a multi-degreed professional at IBM for 18 yrs working in fields ranging from Space Shuttle onboard flight guidance software to business intelligence datamining. My wife, an ordained minister, was active in her denomination for 8 yrs (2 of them part-time) and earned a CB-like pension benefit. Her ministerial 8-yr pension was valued at $75,478; my 18-yr IBM pension was valued at $66,117. So, in summary, I worked over ten years longer for a benefit nearly $10K less than what a minister earned. Is it a wonder IBMers were outraged?

Another former IBM employee, now with IBM Employee Benefits Action Coalition, shares the following story:

I am one of the victims of cash balance conversions; as a 23-year veteran of IBM in 1999, I saw over half a million dollars of my projected pension benefits evaporate in a plan amendment. I'm now the head of a coalition of IBM employees dedicated to finding every legal means possible to reverse the changes and preserve the remaining pension benefits.

The litmus test on this claim [cash balance plans helping attract young skilled workers], in my mind, is whether the employers use the newly revamped plans in any of their recruitment materials. The answer, gleaned from searching both the recruiting sections of their web sites and the brochures they mail to prospective employees, is clear. The new cash balance plans either aren't mentioned at all, or are so deeply buried in the literature that you can't find them...
As clearly illustrated by the individual stories documented above, IBM was the subject of employee outrage when it converted its pension plan. An employee coalition dissatisfied with the change sponsored a plane with a banner reading, “IBM’s pension theft could happen to you!” to fly over the Minnesota State Fair (Anderson, 1999). Because of employee protests, IBM altered its initial decision and decided that anyone forty years old or older with at least ten years of service could remain in the old plan; this doubled the number of employees who had a choice.

The controversial switch to a cash balance plan led four older employees at Onan Corp., a Cummins Engine company, to file suit in 1997 alleging that the cash balance plan adopted in 1989 discriminates in favor of younger employees. The suit was originally expected to go to trial in December, 1999 (Corry, 1999). However, the courts certified the case as a class action under the age-discrimination and pension laws, and the trial date was postponed as the case expanded to include about 1450 workers. The Internal Revenue Service (IRS) sided with employees and asked the court to disqualify Onan’s pension plan (Schultz, Auerbach, and Burkins, 1999). A federal judge ruled that the Onan conversion did not violate age discrimination laws, while simultaneously leaving unanswered the question of whether or not the plan violated federal retirement income laws. A settlement was reached in 2001 requiring Onan to pay between $23 - $53 million to workers, depending on their benefits choices. Jim Eaton, one of the original four plaintiffs, notes that, “We got the company to modify the plan, to go back and, I guess one would say, give us what was rightly ours,” (Hughlett, 2001).

When Prudential agreed to sell its Prudential HealthCare unit to Aetna, many longer-service Prudential employees realized that their pensions would be cut by as much as forty percent. After vigorous employee complaints, the company agreed to allow departing employees
to remain eligible for an early-retirement subsidy that workers usually lose when their units are spun off to new owners. (Schultz, July 1, 1999).

AT&T adopted cash balance pension plans as part of a strategy initially designed to eliminate about one-fourth of its 50,000 manager population during 1998. Only approximately three percent of the management population was over age fifty-five and thus eligible to retire under the old defined benefit plan. Even if all employees over fifty-five elected to leave, targeted downsizing still would not have been achieved, so AT&T exposed a broader group of people to an early retirement incentive program. According to the transition plan, for employees with at least five years of service who voluntarily decided between April 1 and May 22, 1998 to leave (at a later date), the company agreed to place a specified percentage of eligible pay per year of service into that employee's cash balance account. This strategy allowed AT&T to use pension assets instead of operating cash to encourage early retirements (Burlingame and Gulotta, 1998). Employees were clearly dissatisfied with the change; a class-action suit was filed against AT&T (Schultz, Auerbach, and Burkins, 1999).

In many of these situations, employee activists changed corporate positions. They gathered information on their own, and working collectively, to determine the impact of the cash balance conversion. In other cases, employees are still fighting for what they believe to be the pension rights they have earned. Information needed for all of these struggled was not available through any financial reporting process, but was gleaned from other sources, frequently only after media attention identified conversions as problematic.

Political And Legal Arena

In late 1998, the U.S. Senate began to draft legislation tightening disclosure rules for employers shifting from traditional pensions to cash balance plans. Senate staffers noted that
their concerns arose following a series of Wall Street Journal articles reporting that these conversions could significantly reduce pension benefits for longer-term employees. A member of the Senate Finance Committee expressed specific concern about disclosure adequacy for pension changes. He noted that employees appear unaware of how much their pensions can be cut, and often do not know that they may be working for years - a decade or more in some cases - to regain their previous pension standing (“Senate Bill,” 1998).

In early 1999, legislation to address these concerns was introduced into both the U.S. House and Senate. Senators Daniel Patrick Moynihan, Chuck Robb, and Bob Kerrey (all Democrats) introduced the Pension Right to Know Act, which would require companies to provide greater disclosure when making changes to pension plans. A companion bill was introduced in the House of Representatives by Jerry Weller, a Republican, and Representative Ken Bentsen, a Democrat. If adopted, the legislation would require employers who make changes to their pension plan to provide individualized benefits statements for employees comparing their pensions before and after the changes over various periods: on the date of conversion; three, five and ten years after conversion; and at normal retirement age (“Bill Seeks,” 1999). Both bills have been referred to committee, and have not been passed at this time. With the Bush administration set to begin a second term, it is likely they will not be passed in the next two Congresses, either.

The Clinton administration also proposed in mid-1999 that companies changing from traditional plans to new plans be required to tell workers roughly how much retirement money they stand to lose. The Administration’s proposal required companies to provide specific examples of how the change would affect different groups of workers. In addition to the Right to Know legislation Senator William V. Roth (Republican) considered introducing cash balance
disclosure language as part of a tax bill. Bill Archer, chair of the House Ways and Means Committee, included language in his tax bill requiring that employees be given "sufficient information" to understand the effect of conversions when companies change to cash balance plans (Oppel, July 14, 1999).

The Internal Revenue Service and the Equal Employment Opportunity Commission have also been drawn into the debate. Representative Bernie Sanders leaked an IRS memo (dated September, 1998) to the press saying that the cash balance plan at an unnamed company “does not satisfy the clear and straightforward requirement” of age bias law because the benefit accrual rate “decreases as a participant attains each additional year of age” (Anderson, 1999). The IRS’s position that there appears to be age discrimination in this pension plan is a critical issue because the IRS is the government body responsible for granting tax-deferred status to pension plans. Sanders is among forty members of Congress who requested an investigation of these changes by the EEOC and the Labor Department. He notes that, "If the rate of accrual goes down as workers get older, then the plan violates the law" (Anderson, 1999). Sanders is pushing legislation requiring companies to make a detailed disclosure forty-five days before converting to a cash balance plan. The bill would impose a fifty-percent tax on a company's pension surplus if the concern failed to give employees the option to remain in the old plan (Oppel, September 2, 1999; Hitt, October 8, 1999).

In August, 1999, the Justice Department (representing the IRS) filed an amicus brief on behalf of employees of Georgia-Pacific Corporation. The workers had sued their employer alleging that it had miscalculated when it made lump-sum payments from the cash balance plan to departing employees. A footnote to the brief states that, "A determination letter from the IRS applied only to the tax consequences and is meaningless as to participant litigation." The Justice
Department’s position is that it does not matter that the plan received an IRS letter confirming
tax-favored status; these plans still might violate pension laws (Schultz, September 2, 1999).

Throughout the month of September, 1999, U.S. legislators increased pressure on several
groups that had legal or regulatory jurisdiction with cash balance plans. A bipartisan coalition of
twenty-one lawmakers asked Labor Secretary Herman to investigate consultants helping
companies set up cash balance plans. The group accuses the consultants of "contempt and
disregard" for employees. Lawmakers also stepped up pressure on IRS Commissioner Rossotti
to curb tax benefits for these plans (“Pension Tensions,” September 10, 1999).

Following Senate hearings in September of 1999, Senator Paul Wellstone (Democrat)
called for investigating consulting firms that advised companies on changing pension plans.
Specifically, Wellstone wanted more information on how human resource consulting firms are
analyzing “aging population trends” for companies considering conversions to cash balance
plans (Schultz, September 22, 1999). He notes, “I am deeply concerned that serious age
discrimination may be taking place . . . [Congress should find out whether cash balance pension
plans are] appropriate, and how common the practice is” (Schultz, September 22, 1999).
Wellstone also notes that if legislation mandating that all workers be allowed to choose between
their old and new pension plans were brought to the floor, "It would be very difficult for people
to vote against [it]" (Hitt, December 15, 1999). However, attempts to push through a proposal in
the waning days of that legislative session fell short. "What we're concerned about is that this is
going to become a political football," according to Mark Ugoretz, president of the ERISA
Industry Committee. "Democrats are going to want to make Republicans look bad, and
Republicans won't want to look bad, and the real policy issues of how to provide good solid
information are going to get lost in a spitting contest" (Hitt, December 15, 1999).
The debate over cash balance pension plans also found its way into the rhetoric of the 2000 U.S. presidential election. Candidates Al Gore (Democrat) and Gary Bauer ("social conservative" Republican) aired concern regarding the American people's pervasive unease surrounding their financial security at retirement. Gore spokesman Chris Lehane says, "It might not dominate the front page of the paper, but it's an issue people talk about at the breakfast table. . . We're at the breakfast table" (Hitt, December 15, 1999). Bauer says, "The move by IBM and others violates basic American fairness . . . In fact, it is kind of like changing the rules of the game in the third quarter. This is the kind of thing that invites government regulation, which no one wants" (Hitt, December 15, 1999).

A pervasive theme is that players in the legal and political arena are concerned with the ability of participants to understand the impact of corporate conversions to cash balance plans. Clearly the current accounting rules, crafted to serve imaginary "investors" are woefully inadequate; legislative action is considered to require companies to provide details disclosures. A second pervasive theme is the concern that cash balance conversions violate age discrimination laws. Again, current accounting rules do little to illuminate issues that would help to make that determination.

**Concluding Observations and Implications**

Based on the results of this study, it seems reasonable to generalize that converting traditional defined benefit plans to cash balance plans frequently allows companies to benefit at the expense of employees. It seems equally valid to assert that current accounting rules do little to illuminate the impact of this change for either employees or other financial statement users. While failure to provide insight is always a disquieting issue for the accounting profession, it is particularly disturbing given the pervasiveness of public concern and social welfare in the
pension arena. This lack of performance on the part of the FASB is attributable to the bias the FASB harbors that assumes that corporations are "natural" beings. Accounting constructs all problems as maximization of profit for these natural beings without any consideration given to the fact that these beings are products of the political process and what their aims are to be are politically determined. Financial reporting required of corporations might better serve if it was driven by consideration of providing information to citizens rather than just to investors. The pension issue seems clearly to illustrate the inadequacy of the facile assumption that information produced to serve capital providers serves others equally as well.

The common theme is that employee benefits are being reduced, and accounting provides a paucity of information to illuminate this reduction. Employees in companies that have changed to cash balance plans and other stakeholders in this domain have relied upon internal calculations and analyses, politicians, or the courts to adjudicate the contested nature of the pension promise. Absent press coverage and employee activism, it appears doubtful that any legal or regulatory remedies to protect employee interests would be pursued. Financial reporting is about political decision making, as well.
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**Table 3**

**Disclosures of Interest Credits**

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