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GM, Others Boost Their Earnings By Pouring Billions Into Pensions

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For all the wailing about how the so-called pension crisis might force many employers to put money into their pension plans, there may, in fact, be no better investment for most companies. And many of them are taking advantage of it.


Companies have pumped billions of dollars into their pension plans this year, even though most haven't been required to contribute a dime. Rather, by contributing to their pension plans, companies are assured of a guaranteed, effective return that can exceed 40% in the first year, thanks to an interplay of tax and accounting rules.

Consider **General Motors Corp.** Wednesday, GM shares shot up more than 5% after a Goldman Sachs analyst drew attention to the good performance of the auto maker's pension plan. But while the stock-market recovery may have helped GM's pension plan, that isn't the entire story.

The company -- like many others -- also made some pension moves that will help its bottom line handsomely.

In the third quarter, GM shoveled \$13.5 billion into its pension plans, bringing its total contributions for the year to \$14.4 billion. Because the company assumes that the pension assets will return 9% over the next year, the move automatically guarantees the auto maker a \$1.3 billion boost to its bottom line over the next year. Not only that, but GM can deduct the entire contribution, which will shave \$5 billion from its taxes. Combined, the effective guaranteed return in the first year is 44%.

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Over the past year, employers have complained that a combination of low interest rates and investment losses have caused liabilities to balloon, prompting companies with seriously underfunded pensions to make mandatory contributions to their plans. In response, many employers have cut pensions, and next week the Senate is slated to vote on a measure that would let employers with the sickest pension plans suspend contributions for years.

But many companies are only too happy to put money into their pensions.

Boeing Co. stuffed \$1.7 billion into its pension plan this year, ensuring the plane maker of a gain of \$153 million in 2004, plus a tax benefit of \$595 million. **Caterpillar** Inc. contributed \$563 million to its pension, which will generate \$51 million in gains over the next 12 months, while **3M** Co. contributed \$600 million to its pension program, which will bring the company a return of \$54 million. With the tax deductions for these contributions, the effective first-year returns for these companies will be 44%.

A spokeswoman for Boeing says the company made its voluntary contributions while it had "strong cash flow." "This is a good use of this cash," she adds. "When you can fund voluntarily, it makes sense to do so."

PENSION PAYOFF

Companies voluntarily pumped billions of dollars into their pension plans this year. This triggers deductions and guaranteed investment returns, which combine to provide companies with an effective return of 44% to 45% in the first 12 months.

Company	2003 Contribution (in millions)	Guaranteed Rate*	12-Month Return (in millions)	Tax Break** (in millions)	Effective First Year Return
General Motors	\$14,400	9.00%	\$1,296	\$5,040	44%
Boeing	1,700	9	153	595	44
3M	600	9	54	210	44
Caterpillar	563	9	51	197	44
PepsiCo	500	8.2	41	175	43
Sprint PCS	400	9.5	38	140	45
Aetna	180	9	16	63	44
Whirlpool	162	8.8	14	57	44

*Most recent available

**Either current or deferred, at a 35% tax rate

Source: company filings

For its part, GM says it made the pension-plan contributions to avoid paying higher premiums through 2007 to the Pension Benefit Guaranty Corp., a quasipublic pension insurer.

"I don't think the motivation in contributing to the pension is its earnings impact," GM spokesman Jerry Dubrowski says. He adds that some of the financial gain will be offset by interest costs, because GM borrowed the bulk of the money it contributed to the pension, at an average annual rate of about 7.5%. Mr. Dubrowski says the company will disclose more details of its pension expectations in a Dec. 12 conference call with analysts and investors.

A spokesman for 3M confirmed the figures but declined further comment. A spokeswoman for Caterpillar said that it is misleading to combine the effect of the tax deduction and the pension income.

Part of the secret to the companies' pension-investing success lies in accounting rules that allow companies to use hypothetical returns on their pension assets -- instead of the actual returns -- when calculating the pension plans' impact on company earnings. Boeing assumed its pension assets would return 9%, for example. In 2002, large companies generally assumed rates of return between about 8.5% and 9%, with some assumptions reaching as high as 10%.

Analysts have criticized this practice in recent years, complaining that some companies are using unrealistically high hypothetical -- or "expected" -- rates of return to enhance earnings. Last year, for example, GM assumed its pension assets would return 10%, while they actually lost 5.2%.

In response, employers have argued that the accounting rules cushion company earnings from the ups and downs of their pension investments, and that the company ultimately pays the piper. If the investments exceed their "expected" return, the company can stockpile the gains to use later, which is what happened commonly throughout the 1990s. But if the investments do worse than expected, which has typically been the case in the past three years, the losses can be postponed.

Indeed, in the first nine months of 2003, GM's pension assets have enjoyed a 14% return, exceeding the 9% assumed rate. This means that the extra gains of \$675 million can be stockpiled and used to reduce pension expenses in later years. Boeing says its pension assets have returned 17% this year.

In 4 p.m. composite trading on the New York Stock Exchange Wednesday, GM shares rose 5.2% to \$45.54.

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