Penbridge ADVISORS

PRT Index Guide

This Guide explains the Penbridge PRT Index and how it may be used.

Summary

The PRT Index represents the premium that an insurance provider would charge for a buy-out of a generic DB plan. It is intended to illustrate relatively advantageous or disadvantageous times for a plan sponsor to purchase annuities from insurance providers. The PRT Index reflects changes in the providers' targeted investment universe, expense structure, regulatory environment and pricing aggressiveness. It does not capture the census characteristics and features of any particular plan, which would require specific insurer underwriting. The generic plan is deemed not to change over time.

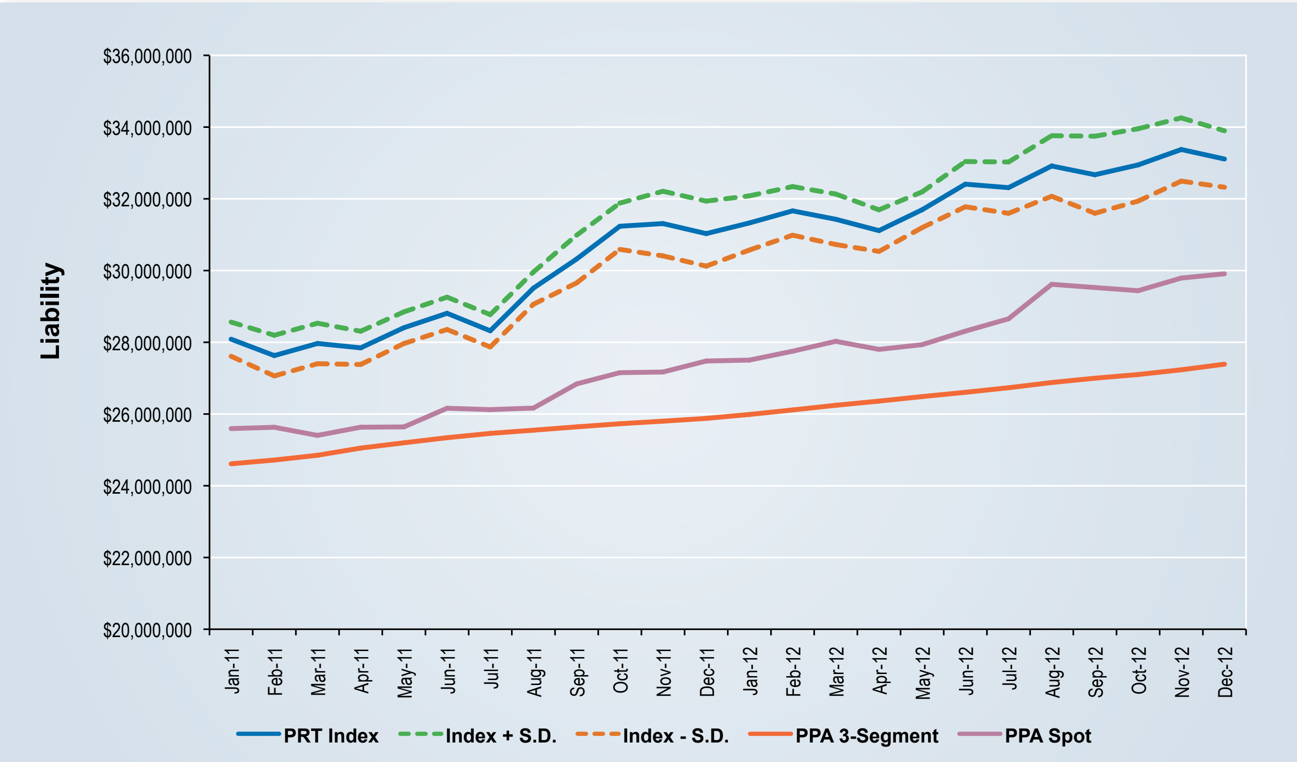
The Penbridge PRT Index Defined

The Index is the present value of a fixed series of cash flows. The cash flows ("Index Cashflow") are chosen to be representative of a typical DB pension plan seeking a buy-out. The present value is calculated by discounting the cash flows at a single interest rate. The interest rate is derived in two steps. First, market rates are collected on a confidential basis from participating insurance providers for various specific sizes and durations of buy-outs, and those rates are averaged. Second, a mathematical interpolation of those average rates is performed in order to match the size and duration of the Index Cashflow. Each month, providers update their rates on the PRT database, and a new PRT Index value is calculated.

Choice of an Index Cashflow

The Index Cashflow does not come from any particular pension census. But the size and shape of the cash flow is quite similar to what would come from a "typical" plan with a present value in the neighborhood of $25 million, a liability mix of approximately 80% retirees and 20% terminated vesteds, and a duration near 10. [The duration will be higher at lower interest rates, and vice versa].

Comparison of PRT Index to PPA Rates



It is useful to examine the difference between the PRT Index and the present value of the same Index Cashflow on the basis of funding rates mandated by the Pension Protection Act of 2006 ("PPA Rates").

The PPA established new minimum funding standards for DB plans. Plans must establish their fully-funded status based on a choice of either the "PPA Spot" rates or the "PPA 3-Segment" rates. Both sets of PPA rates are derived from an index of investment-grade U.S. corporate bonds.

The PRT Index may be compared to the present value of the Index Cashflow discounted at the PPA Spot rates and at the PPA 3-Segment rates*. Times when the PRT Index is closer to PPA rate present values would represent more opportunistic times to transact an annuity purchase. To illustrate the pricing variability among insurers, one (1) standard deviation above and below the Index is shown.

* The 3-Segment rates are a simple average of all the Spot rates over the last 24 months that fall within each segment domain [i.e., 0-5 years; 5-20 years; and 20-60 years]. Moreover, plan sponsors may choose 3-Segment rates as of any month up to four months prior to the start of a plan year in which valuations are made. The monthly values shown here are calculated using the most recent 3-Segment rates a plan could use. In practice 3-segment rates are updated only once per year on the valuation date, in a month that depends on the particular plan.

Reconciling the PPA and PRT Index costs for an actual Buy-out

It should not be a surprise that the PRT index cost appears higher than the present value of the Index Cashflow on the PPA bases. But one should not necessarily conclude that a buy-out would be financially disadvantageous. It is important to consider what is included and what is not included in these two measures.

	Full funding target at PPA Rates (Spot or 3-Segment)	PRT Index
Includes:	Retirees only	Current interest rates Insurer Profit Margin Administrative expenses
Does not reflect:	Plan-specific mortality Cost of additional plan features Ongoing administrative expenses Ongoing actuarial expenses Annual PBGC premiums Ongoing internal management cost Intangible considerations	Plan-specific mortality Cost of additional plan features One-time transaction expenses Intangible considerations

Although the PRT Index only illustrates the interest rate (net of profit margin) and expense elements of pricing a buy-out, interest rates are actually the most dynamic and critical element. A plan sponsor [perhaps with the help of a consultant] could estimate the effect of any pricing difference between the plan's estimates for mortality and plan design features and an insurer's pricing of those same elements. Note that there should not be a significant difference between the two bases IF the plan sponsor has established realistic assumptions.

But, in order to make a full apples-to-apples cost comparison between maintaining and terminating a plan, the plan sponsor must account for the present value of future expenses that a plan sponsor incurs with an ongoing plan. This can be quite significant, and is often not fully recognized. Administrative expenses, actuarial expenses and PBGC premiums should be relatively easy to estimate for any particular plan. Internal management costs should include the value of time senior executives devote to plan-related business matters and the cost of fiduciary liability insurance [or an equivalent value to recognize the risk, if uninsured]. Note that for a buy-in or carve-out transaction which does not result in plan termination, some of these expenses remain.

Note that the PRT Index does not address intangibles that are not easily quantifiable, e.g., the effect of a plan termination on human resources, or the perception of shareholders, financial analysts and rating agencies. Such subjective elements would have to be considered carefully before a plan sponsor decides to proceed with a buy-out. Please use the Penbridge PRT Index only for the purposes stated herein.