Pension Benefit Guaranty Corporation

Office of Inspector General

Audit Report

Audit of the Pension Benefit Guaranty Corporation's Fiscal Year 2012 and 2011 Financial Statements

November 14, 2012

AUD-2013-1/FA-12-88-1

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Pension Benefit Guaranty Corporation
Office of Inspector General
1200 K Street, N.W., Washington, D.C. 20005-4026

To the Board of Directors
Pension Benefit Guaranty Corporation

The Office of Inspector General contracted with CliftonLarsonAllen LLP, an independent certified public accounting firm, to audit the financial statements of the Single-Employer and Multiemployer Program Funds administered by the Pension Benefit Guaranty Corporation (PBGC) as of and for the years ended September 30, 2012 and 2011. They conducted their audit in accordance with auditing standards generally accepted in the United States of America; *Government Auditing Standards*, issued by the Comptroller General of the United States; attestation standards established by the American Institute of Certified Public Accountants; and OMB audit guidance.

In their audit of PBGC's Single-Employer and Multiemployer Program Funds, CliftonLarsonAllen found:

- The financial statements were presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

- PBGC did not have effective internal control over financial reporting (including safeguarding assets) and compliance with laws and regulations and its operations as of September 30, 2012. Serious internal control weaknesses in PBGC's programs and operations resulted in three material weaknesses: (1) Benefits Administration and Payment Department management and oversight, (2) entity-wide security program planning and management, and (3) access controls and configuration management.

- PBGC did not determine the fair market value of plan assets at the date of plan termination in accordance with the regulation established in Title 29 of the Code of Federal Regulation Part 4044.41(b) in certain instances.

The PBGC Annual Report includes other information such as management's discussion and analysis, improper payment assessment, actuarial valuation, and organizational wide data, in addition to the financial statements. CliftonLarsonAllen applied limited procedures to this data and is not providing an opinion or any assurance on the information.

CliftonLarsonAllen is responsible for the accompanying auditor's report dated November 14, 2012 and the conclusions expressed in the report. We do not express opinions on PBGC's financial statements or internal control, nor do we draw conclusions on compliance with laws and regulations.

The financial statement audit report (AUD-2013-1 / FA-12-88-1) is also available on our website at http://oig.pbgc.gov.

Sincerely,

Rebecca Anne Batts

Rebecca Anne Batts
Inspector General

November 14, 2012

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Contents

Acronyms

A&A	Assessment and Authorization
ASD	Actuarial Services Division
BAPD	Benefits Administration Payment Department
CFR	Code of Federal Regulations
CCRM	Configuration, Change, and Release Management
CFS	Consolidated Financial System
CCRD	Contracts and Controls Review Department
CAP	Corrective Action Plan
DoPT	Date of Plan Termination
ERISA	Retirement Income Security Act of 1974
ETA	Enterprise Target Architecture
FIPS PUB	Federal Information Processing Standards Publication
FMFIA	Federal Managers' Financial Integrity Act of 1982
FY	Fiscal Year
IPS	Image Processing System
IT	Information Technology
IPVFB	Integrated Present Value of Future Benefit
NIST SP	National Institute of Standards and Technology Special Publication
OIG	Office of Inspector General
OIT	Office of Information Technology

OMB	Office of Management and Budget
PAM	Portfolio Accounting and Management
POA&M	Plan of Action and Milestones
PAS	Premium Accounting System
PVFB	Present Value of Future Benefit
PBGC	Pension Benefit Guaranty Corporation
TAS	Trust Accounting System
TIS	Trust Interface System
TPD	Trusteeship Processing Division
U.S.C.	United States Code

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Section I

Independent Auditor's Report

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To the Board of Directors, Management,
and Inspector General of the
Pension Benefit Guaranty Corporation
Washington, DC

Independent Auditor's Report

In our audits of the Single-Employer and Multiemployer Program Funds administered by the Pension Benefit Guaranty Corporation (PBGC or the Corporation) for fiscal years (FY) 2012 and 2011, we found:

- The financial statements are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America (U.S.).
- PBGC did not have effective internal control over financial reporting (including safeguarding assets) and compliance with laws and regulations and its operations as of September 30, 2012.
- One instance of reportable noncompliance with selected provisions of laws and regulations we tested.

The following sections discuss in more detail (1) these conclusions; (2) our conclusions on other accompanying information; (3) management's responsibility for the financial statements; (4) our responsibility for the audit; and (5) management's comments and our evaluation.

Opinion on the Financial Statements

The financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with accounting principles generally accepted in the U.S., the financial condition of the Single-Employer and Multiemployer Program Funds administered by PBGC as of September 30, 2012 and 2011, and the results of their operations and cash flows for the FYs then ended.

By law, PBGC's Single-Employer and Multiemployer Program Funds must be self-sustaining. As of September 30, 2012, PBGC reported in its financial statements net deficit positions (liabilities in excess of assets) in the Single-Employer and Multiemployer Program Funds of $29.14 billion and $5.24 billion, respectively. As discussed in Note 9 to the financial statements, loss exposure for the Single-Employer and Multiemployer Programs that are reasonably possible as a result of unfunded vested benefits are estimated to be $295 billion and $27 billion, respectively. Management based the Single-Employer Program estimate on data for FYs ending in calendar year 2011 that was obtained from filings and submissions to the government and from corporate annual reports. A subsequent adjustment for economic conditions through September 30, 2012 has not been made, and as a result the exposure to loss for the Single-Employer Program as of September 30, 2012 could be substantially different. In addition, PBGC's net deficit and long-term viability could be further impacted by losses from plans classified as reasonably possible (or from other plans not yet identified as potential losses) as a result of deteriorating economic conditions, the insolvency of a large plan sponsor, or other factors. PBGC has been able to meet its short-term benefit obligations; however, as discussed in Note 1 to the financial statements, management believes that neither program at present has the resources to fully satisfy PBGC's long-term obligations to plan participants.

Opinion on Internal Control

Because of the effect of the material weaknesses described below on the achievement of the objectives of the control criteria contained in the Federal Managers' Financial Integrity Act of 1982 (FMFIA) at 31 U.S.C. 3512(c) and (d), PBGC did not maintain effective internal control over financial reporting (including safeguarding assets) and compliance with laws and regulations and its operations as of September 30, 2012.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

We identified certain deficiencies in internal control over financial reporting (including safeguarding assets) and compliance with laws and regulations and its operation that we consider material weaknesses, and other deficiencies that we consider to be a significant deficiency. These material weaknesses adversely affected PBGC's ability to meet the internal control objectives listed in management's responsibility for the financial statements section of this report, or to meet Office of Management and Budget (OMB) criteria for reporting matters under FMFIA.

We consider the deficiencies in the following areas material weaknesses:

1. Benefits Administration and Payment Department (BAPD) Management and Oversight
2. Entity-wide Security Program Planning and Management
3. Access Controls and Configuration Management

A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies in the following area a significant deficiency:

4. Integrated Financial Management Systems

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PBGC protects the pensions of approximately 43 million workers and retirees in more than 25 thousand private defined benefit pension plans. Under Title IV of the Employee Retirement Income Security Act of 1974, PBGC insures, subject to statutory limits, pension benefits of participants in covered private defined benefit pension plans in the U.S. To accomplish its mission and prepare its financial statements, PBGC relies extensively on the effective operation of the Benefits Administration and Payment Department (BAPD) and information technology (IT). Internal controls over these operations are essential to ensure the confidentiality, integrity, and availability of critical data while reducing the risk of errors, fraud, and other illegal acts.

BAPD manages the termination process for defined benefit plans, provides participant services (including calculation and payment of benefits) for PBGC-trusteed plans, provides actuarial support for PBGC, and carries out PBGC's responsibilities under settlement agreements. BAPD has several distinct divisions including Trusteeship Processing Divisions (TPDs) and the Actuarial Services Division (ASD). The TPDs are responsible for capturing the participant data for benefit determinations, managing the benefit payments to participants and beneficiaries, and maintaining the pension plan and participant files that include underlying documentation used to support the calculation of benefit amounts for the participant and the pension liabilities recorded on PBGC financial statements. The ASD is responsible for calculating the Present Value of Future Benefits (PVFB) liability, based on actuarial assumptions and methods. ASD uses the underlying documentation maintained by the TPDs, as well as mortality tables and interest rate factors, as key inputs to calculate pension plan liabilities recorded on PBGC’s financial statements.

BAPD continues to have serious control weaknesses throughout the department. These weaknesses are attributed to BAPD’s management and oversight over the processes needed to calculate and value participant’s benefits and the related liabilities, as well as to value plan assets. Such weaknesses increase significant risks to PBGC’s operations, including accurate calculation of plan participants’ benefits, accurate financial reporting and compliance with prescribed laws and regulations. In FYs 2012 and 2011, PBGC hired a contractor to perform a review of its programs and activities for improper payments in accordance with the Improper Payment Elimination and Recovery Act. In addition to identifying that actual improper payments occurred, the contractor found that the underlying documentation used to support the benefit payments was not always available. Similar documentation is used to support the actuarial calculations of PBGC pension plan liabilities and related expenses. During FY 2012, we continued to identify numerous deficiencies in BAPD controls that included inadequate documentation to support the calculation of participants’ benefits and liabilities, errors in their liability calculations, and errors in valuing plan assets.

The establishment and implementation of the appropriate internal controls is critical to PBGC operations. Furthermore, reliable internal controls ensure that the programs achieve their intended results; resources are used consistent with agency mission; programs and resources are protected from waste, fraud, and mismanagement; laws and regulation are followed; and reliable and timely information is obtained, maintained, reported and used for decision making as stated in the OMB Circular A-123, *Management’s Responsibility for Internal Control*. In order to mitigate operational and financial reporting risks to PBGC as a whole, active involvement from BAPD’s senior leadership in the monitoring and response to such risks is warranted on a continuous basis.

In response to weaknesses previously identified above, BAPD continues to undergo a strategic review with the intention of addressing the organizational structure and operational issues. In FY 2012, BAPD hired a new Director and continued efforts to develop a plan to address the deficiencies noted in prior OIG financial statements and performance audit reports. PBGC intends the plan to focus on fundamental issues such as internal controls, processes, contractor oversight, training, and staff competencies.

IT continues to be a challenge for management. The safeguarding of PBGC’s systems and data is essential to protect PBGC’s operations and mission. The OIG and others have consistently identified serious internal control vulnerabilities and systemic security control weaknesses in the IT environment over the last several years. PBGC's delayed progress in mitigating these deficiencies at the root-cause level continued to pose increasing and substantial risks to PBGC's ability to carry out its mission during FY 2012. Due to the persistent nature and extended time required to mitigate such vulnerabilities, additional risks threaten PBGC's ability to safeguard its systems. These risks include technological obsolescence, inability to execute corrective actions, breakdown in communications, and poor monitoring.

PBGC has made some progress in addressing IT security weaknesses at the root-cause level by continuing the implementation of its FY 2010 Enterprise Corrective Action Plan (CAP), and introducing additional reporting controls to track progress. Additional tracking controls include the Enterprise Plan of Action and Milestones (POA&M) and the Progress Status Reports on corrective actions. However, the current PBGC corrective action process was disjointed, with stove-piped responsibilities that did not provide a holistic view to inform key decision makers on progress made and resources needed to complete critical tasks. PBGC is in the process of improving its corrective action process to be more cohesive where the CAP will inform the POA&M which will, in turn, provide the Contracts and Control Review Department (CCRD) with the official status of corrective actions to be included in the Listing of Open OIG Recommendations.

The Corporation has also made progress in addressing the design of its infrastructure, account management, enterprise security management, and configuration management, but the control processes have not reached a level of maturity to prove their effectiveness. PBGC is implementing a disciplined and integrated approach to Configuration, Change, and Release Management (CCRM) Process & Procedures consistent with National Institute of Standards and Technology (NIST) Special Publication (SP) 800-53, Rev 3. The Corporation has also developed and is implementing additional policies and procedures; additional technical and configuration management tools are also being deployed. However, much remains to be done, and the pace of progress remains slow.

PBGC anticipated completing the assessment and authorization (A&A) process, formerly referred to as a certification and accreditation process, on the Corporation's major applications in FY 2012, but was unable to complete the process. The work on the A&As that has been performed through FY 2012 identified significant fundamental security control weaknesses in PBGC's general support systems, many of which were reported in prior year's audits and remain unresolved. We continued to find deficiencies in the areas of security management, access controls, configuration management, and segregation of duties. Control deficiencies were also found in policy administration, and the completion of A&A for all major applications.

PBGC developed an information security policy framework, including the *Information Security Policy* which is supported by standards, processes, procedures, and a guide published in June 2012, *The Office of Information Technology (OIT) Security Authorization Guide*. This *Guide* provides steps and templates for use in preparing and completing the Security Authorization and Assessment process which follows NIST 800-37. Also, the *Guide* provides a checklist to support OIT's review of submitted artifacts as evidence of controls implemented. PBGC is documenting the review process with the checklist. The new information security policy framework has not reached a level of maturity to determine its effectiveness. PBGC is still in the process of establishing an enterprise-wide continuous monitoring program; and deploying additional network management, monitoring and configuration tools in its environment.

The serious weaknesses in BAPD's internal controls such as inadequate documentation to support the benefit and liability calculations, errors in liability calculations and valuing plan assets, as well as the limited progress of mitigating PBGC's systemic security control weaknesses create an environment that could lead to improper application of benefits to plan participations, inaccurate financial reporting, fraud, waste, and abuse.

Based on our findings, we are reporting that the deficiencies in the following areas constitute three material weaknesses for FY 2012:

1. BAPD Management and Oversight
2. Entity-wide Security Program Planning and Management
3. Access Controls and Configuration Management

We are also reporting the deficiencies in the following area to be a significant deficiency for FY 2012:

4. Integrated Financial Management Systems

Detailed findings and recommendations follow.

1. BAPD Management and Oversight

BAPD is the core department within PBGC to maintain plan and participant information and to calculate plan benefits and related liabilities. BAPD's management and oversight function is a key component of the control environment in which its division managers and staff operates. The continuous deficiencies of the aforementioned function increase PBGC's operational and financial reporting risks.

<u>Calculation of the Present Value of Future Benefits Liability</u>

During FY 2012, BAPD made errors in calculating the PVFB liability for some participants. ASD is primarily responsible for the calculation of the PVFB liability that is recorded on PBGC's financial statements, based on actuarial assumptions and methods. These calculation errors were primarily due to two reasons: (1) the actuarial liability factors were applied to incorrect or incomplete data inputs and (2) a plan's particular benefit provisions were not sufficiently reviewed to correctly calculate individual participants' PVFB liability. Specifically, BAPD's ASD used actuarial assumptions because the best available data was not updated into the applicable information system. For example, in some instances an actual date of birth was used to calculate a specific benefit but the estimated date of birth was entered into the applicable information system causing the calculation of the liability to be incorrect. In other instances, ASD incorrectly calculated certain liabilities of the participants using a single life annuity benefit plan provision instead of the joint and survivorship benefit. During our June 30 interim testing, we identified an error in the calculation of the participant liability for one large plan related to one of the plan's unique provisions. Management was not aware of this unique plan benefit and that it had been inappropriately excluded from the participants' liability calculations. This error required additional efforts by BAPD management to determine the underlying cause and to calculate an overall plan adjustment to PBGC's liability at September 30. Due to these errors noted during the interim period, we adjusted our year-end audit procedures to address the increased operational and financial reporting risks. Using a statistically based sampling technique, we noted approximately 13% of the samples tested in which the liability calculated for a plan participant was either overstated or understated. The projected value of the error to the entire PVFB liability of approximately $106 billion at September 30, 2012, had an estimated range of approximately $507 million understatement to $875 million overstatement and a point estimate of $185 million overstatement.

We also noted deficiencies in BAPD's maintenance of underlying documentation used to support the calculation of the PVFB. BAPD's TPDs are primarily responsible for maintaining the plan and participant files utilized to determine the benefit and liabilities amounts owed to plan participants. The information system that maintains the participant documentation such as birth certificates, marriage certificates, participant benefit applications, plan provisions, salary data, etc., is the Image Processing System (IPS). During our testing at June 30 and September 30, BAPD was not able to provide the documentation needed to support liability calculations for some samples. We also noted that the documentation was not maintained in a single systematic manner and required herculean efforts by BAPD and other PBGC departments to locate and provide the documentation. The lack of appropriate documentation results in limited physical and financial reporting controls, and could lead to improper benefit payment and participant liability calculations by PBGC. Consequently, we could not determine whether the benefits or the associated liability was calculated properly for those selected samples at June 30 and September 30.

Last year we reported several deficiencies in BAPD related to documentation, including the need to require archival of source documents, implementation of controls to ensure monitoring and enforcement of procedures requiring document maintenance, and to improve the training of persons tasked with calculating and reviewing benefit determinations. These deficiencies have not yet been corrected.

Because of errors in the liability calculations and the lack of supporting documentation, PBGC is at risk for inaccurately valuing the plan liabilities reported in its financial statements. Also, these deficiencies could impact PBGC management's ability to provide meaningful and accurate information to its key stakeholders such as the plan participants, the Board, Congress, and OMB.

Valuation of Plan Assets and Benefits

Although BAPD has undertaken efforts to revalue assets for certain pension plans trusteed by PBGC, internal control weaknesses in this area continue to merit focus. The fair market value of a pension plan's assets at the date of plan termination (DoPT) is an essential factor needed to determine the retirement benefit amounts owed to plan participants. The lack of BAPD's effective oversight and monitoring of contracted reviews over asset valuations continued to pose significant risks to the participants' benefit determinations. During FY 2012, BAPD hired contractors to perform revaluations of plan assets for some large plans which resulted in increased benefits owed to certain plan participants. BAPD management stated that a risk analysis is currently underway to determine which additional pension plans may have asset valuation misstatements and pose the greatest risks to the participants' benefit payments. This risk analysis was not complete at September 30, 2012. In addition, management has yet to finalize a quality control review process to verify and validate the satisfactory completion of contracted DoPT plan asset valuation audits, and to establish a detailed process to ensure the consistent application of a methodology to determine the fair market value of plan assets at DoPT at September 30, 2012.

Additional weaknesses identified as part of the prior year financial statement audit stemmed from inadequate management of contractors, a condition that continues to exist. As previously discussed, these contractors perform critical functions such as the valuing of plan assets. Services provided by contractors should be subject to an effective system of internal controls. Management has not always fully considered the exposure and risk that contractors introduce into its environment. BAPD intended to develop corrective action plans in FY 2012 to focus on fundamental issues such as internal controls, processes, contractor oversight, and training and staff competencies. However, the development of these plans was still in progress at September 30, 2012.

Recommendations: We recommend that PBGC management:

Promptly correct the errors in its calculations identified by the auditors.

Develop and implement a comprehensive documentation retrieval system that clearly identifies the location of the participants' census data and benefit calculation elements in a systematic manner.

Update the technical reference guide used by ASD to document the procedures used to calculate the qualified pre-survivor annuity and deferred retirement ages.

Update current procedures to ensure that all plan provisions are considered in the calculation of the individual participant liability. The procedures should be documented in formal procedural manual and/or checklist.

Refine their current procedures for processing plans and uploading participant data in the Genesis database to ensure that the best available data is used to support benefit payments and IPV liabilities.

Modify the BAPD Operations Manual to explicitly incorporate policies and procedures to archive source records. The BAPD Operations Manual details the process of creating the participant database, but does not explicitly require the archival of source records.

Ensure that adequate documentation is maintained, which supports, substantiates, and validates benefit payment calculations by implementing proper monitoring and enforcement measures in compliance with approved policies and procedures.

Improve the training of persons tasked with the calculation and review of benefit determinations to ensure their skills are matched with the complexities of the tasks assigned.

Continue to implement procedures to verify that future contracts for plan asset valuations clearly outline expectations and deliverables in the statement of work.

Continue to develop a quality assurance program aimed to ensure that plan asset valuations meet the regulatory standard of determining fair market value based on the method that most accurately reflects fair market value.

Continue to enhance and formalize efforts to improve staff skills, whether federal or contactor, in planning the valuation reviews, understanding the risks, and developing appropriate scopes and procedures to support credible and reliable results.

Identify those plans that might potentially have a pervasive misstatement to the financial statements if DoPT asset values were originally misstated. Management should then re-evaluate the DoPT asset values for those identified plans and consider the impact of any known differences on the financial statements.

2. Entity-wide Security Program Planning and Management

In prior years, we reported that PBGC's entity-wide security program lacked focus and a coordinated effort to adequately resolve control deficiencies. Deficiencies persisted in FY 2012, which prevented PBGC from implementing effective security controls to protect its information from unauthorized access, modification, and disclosure. Without a well-designed and fully implemented information security management program, there is increased risk that security controls are inadequate; responsibilities are unclear, misunderstood, and improperly implemented; and controls are inconsistently applied. Such conditions may lead to insufficient protection of sensitive or critical resources and disproportionately high expenditures for controls over low-risk resources.

An entity-wide information security management program is the foundation of a security control structure and a reflection of senior management's commitment to addressing security risks. The security management program should establish a framework and a continuous cycle of activity for assessing risk, developing and implementing effective security procedures, and monitoring the effectiveness of these procedures.

In the *Federal Information Security Management Act of 2002*, Congress required each federal agency to establish an agency-wide information security program to provide security to the information and information systems that support the operations and assets of the agency, including those managed by a contractor or other agency. OMB Circular No. A-130, Appendix III, *Security of Federal Automated Information Resources,* requires agencies to implement and maintain a program to assure that adequate security is provided for all agency information collected processed, transmitted, stored, or disseminated in general support systems and major applications.

Recommendations: We recommend that PBGC management:

Develop and implement a well-designed security management program that will provide security to the information and information systems that support the operations and assets of the Corporation, including those managed by contractors or other federal agencies.

Effectively communicate to key decision makers the state of PBGC's IT infrastructure and environment to facilitate the prioritization of resources to address fundamental weaknesses.

3. Access Controls and Configuration Management

Although access controls and configuration management controls are an integral part of an effective information security management program, access controls remain a systemic problem throughout PBGC. PBGC's decentralized approach to system development, system deployments, and configuration management created an environment that lacks a cohesive structure in which to implement controls and best practices. Weaknesses in the IT environment contributed significantly to deficiencies in system configuration, segregation of duties, role-based access controls, and monitoring. PBGC realizes these challenges, and is implementing a disciplined and integrated approach through development of *Configuration, Change, and*

Release Management (CCRM) Process & Procedures consistent with NIST 800-53, Rev 3. The Corporation has also developed and is implementing additional policies and procedures, including deploying technical and configuration management tools. Technical tools have been or are being deployed to better manage configuration of common operating platforms. Once these tools are fully operational in the infrastructure, they will help ensure that controls related to the configuration of infrastructure components remain consistent and provide alerting capabilities when components are changed. Other complementary processes, such as the Tiger Team focus on system scanning and vulnerability management, support PBGC's capability to carefully document and validate system vulnerabilities and also provide evidence as to the operating effectiveness of some technical common controls.

Access controls should be in place to consistently limit and detect inappropriate access to computer resources (data, equipment, and facilities); and monitor access to computer programs, data, equipment, and facilities. These controls protect against unauthorized modification, disclosure, loss, or impairment. Such controls include both logical and physical security controls to ensure that federal employees and contractors will be given only the access privileges necessary to perform business functions. Federal Information Processing Standards Publication (FIPS PUB) 200, *Minimum Security Requirements for Federal Information and Information Systems,* specifies minimum access controls for federal systems. FIPS PUB 200 requires PBGC's information system owners to limit information system access to authorized users.

Industry best practices, NIST SP 800-64, *Security Considerations in the System Development Life Cycle,* and other federal guidance recognize the importance of configuration management when developing and maintaining a system or network. Through configuration management, the composition of a system is formally defined and tracked to ensure that an unauthorized change is not introduced. Changes to an information system can have a significant impact on the security of the system. Documenting information system changes and assessing the potential impact on the security of the system, on an ongoing basis, is an essential aspect of maintaining the security posture. An effective entity-wide configuration management and control policy, and associated procedures, are essential to ensuring adequate consideration of the potential security impact of specific changes to an information system. Configuration management and control procedures are critical to establishing an initial baseline of hardware, software, and firmware components for the entity, and subsequently controlling and maintaining an accurate inventory of any changes to the system.

Inappropriate access and configuration management controls do not provide PBGC with sufficient assurance that financial information and financial assets are adequately safeguarded from inadvertent or deliberate misuse, fraudulent use, improper disclosure, or destruction.

Recommendation: We recommend that PBGC management:

Develop and implement a coherent strategy for correcting IT infrastructure deficiencies and a framework for implementing common security controls, and mitigating the systemic issues related to access control by strengthening system configurations and user account management for all of PBGC's information systems.

4. Integrated Financial Management Systems

The risk of inaccurate, inconsistent, and redundant data is increased because PBGC lacks a single integrated financial management system. The current system cannot be readily accessed and used by financial and program managers without extensive manipulation, excessive manual processing, and inefficient balancing of reports to reconcile disbursements, collections, and general ledger data.

OMB Circular A-127, *Financial Management Systems*, requires that federal financial management systems be designed to provide for effective and efficient interrelationships between software, hardware, personnel, procedures, controls, and data contained within the systems. The Circular states:

> A financial system, hereafter referred to as a core financial system, is an information system that may perform all financial functions including general ledger management, funds management, payment management, receivable management, and cost management. The core financial system is the system of record that maintains all transactions resulting from financial events. It may be integrated through a common database or interfaced electronically to meet defined data and processing requirements. The core financial system is specifically used for collecting, processing, maintaining, transmitting, and reporting data regarding financial events. Other uses include supporting financial planning, budgeting activities, and preparing financial statements. Any data transfers to the core financial system must be: traceable to the transaction source; posted to the core financial system in accordance with applicable guidance from the Federal Accounting Standards Advisory Board; and in the data format of the core financial system.

OMB's Office of Federal Financial Management, *Core Financial System Requirements*, lists the following financial management system performance goals, outlined in the framework document, applicable to all financial management systems. All financial management systems must do the following:

- Demonstrate compliance with accounting standards and requirements.
- Provide timely, reliable, and complete financial management information for decision making at all levels of government.
- Meet downstream information and reporting requirements with transaction processing data linked to transaction engines.
- Accept standard information integration and electronic data to and from other internal, government-wide, or private-sector processing environments.
- Provide for "one-time" data entry and reuse of transaction data to support downstream integration, interfacing, or business and reporting requirements.
- Build security, internal controls, and accountability into processes and provide an audit trail.
- Be modular in design and built with reusability as an objective.
- Meet the needs for greater transparency and ready sharing of information.

- Scale to meet internal and external operational, reporting, and information requirements for both small and large entities.

Because PBGC has not fully integrated its financial systems, PBGC's ability to accurately and efficiently accumulate and summarize information required for internal and external financial reporting is impacted. Many of the weaknesses include the lack of standard data classifications and common data elements, duplication of transaction entry and obsolete and antiquated technologies.

If managed effectively, IT investments can have a dramatic impact on an organization's performance and accountability. If not correctly managed, they can result in wasteful spending and lost opportunities for achieving mission goals and improving mission performance. PBGC had several false starts in modernizing its systems and applications that have either been abandoned (such as the suspension of work on the Premium and Practitioner System to replace PAS) or have been ineffective in leading to the integration of its financially significant systems. Unless PBGC develops and implements a well-designed IT architecture and infrastructure to guide and constrain modernization projects, it risks investing time and resources in systems that do not reflect the Corporation's priorities, are not well integrated, are potentially duplicative, and do not optimally support mission operations and performance.

To its credit, PBGC began to develop an overall strategy, but much work remains before the strategy can be completed and implemented. Specific steps PBGC has taken in FY 2012 include the following:

- Continued work on its Enterprise Target Architecture (ETA), which provides the road map for all PBGC system development and integration, including financial management system integration.

- Implemented interface enhancements for CFS, including the payroll interface modernization, procurement interface, travel interface, and invoice automation. These interfaces provide additional automated capabilities for CFS and reduce the amount of manual data inputs for certain transactions.

However, major work remains to be completed to provide PBGC with integrated financial management capabilities. PBGC plans to implement the Trust Accounting and FY File System (TAS) in January 2013 after completing the TAS user acceptance testing. TAS will replace the following existing financial applications: Portfolio Accounting and Management (PAM), FY File, Trust Interface System (TIS), and TIS Transfer. Additionally, TAS will have automated interfaces with the CMS, CFS, and IPVFB. Lastly, PBGC has identified future capabilities in its financial management to-be architecture including a procurement system and an online budgeting system.

PBGC's IT initiatives include further corrective actions through the implementation of TAS and the Premium and Practitioner System (PPS). Also during FY 2012, PBGC began the development of PPS. PPS will be fully integrated with the Oracle eBusiness Suite COTS solution used for PBGC's Consolidated Financial Systems, and will replace the PAS in December 2013.

Recommendation: We recommend that management:

Implement and execute a plan to integrate its financial management systems in accordance with OMB Circular A-127.

Report on Compliance and Other Matters

Except as discussed below, our tests of PBGC's compliance with selected provisions of laws and regulations for FY 2012 disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards or OMB audit guidance. However, the objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

Title 29 of the Code of Federal Regulation (C.F.R.) Part 4044.41 Subpart (b), General valuation rules, states "Plan assets shall be valued at their fair market value, based on the method of valuation that most accurately reflects such fair market value."

As reported above in material weakness number one, we noted instances where PBGC failed to determine the fair market value of plan assets at DoPT as required by this regulation.

This conclusion is intended solely for the information and use of PBGC's OIG, Board of Directors, management of PBGC, Government Accountability Office, OMB, the U.S. Congress, and the President and is not intended to be and should not be used by anyone other than these specified parties.

Management's Responsibility for the Financial Statements

PBGC's management is responsible for (1) preparing the financial statements in conformity with accounting principles generally accepted in the U.S.; (2) designing, implementing and maintaining internal control to provide reasonable assurance that the broad control objectives of FMFIA are met; (3) its assertion of the internal control over financial reporting is included in PBGC's FY 2012 Annual Report; and (4) complying with applicable laws and regulations.

Auditor's Responsibility

We are responsible for conducting our audit in accordance with standards generally accepted in the U.S.; the standards applicable to the financial audits and examination engagements contained in Government Auditing Standards, issued by the Comptroller of the U.S.; and OMB Bulletin 07-04. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether (1) the financial statements are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the U.S.; and (2) management maintained effective internal control as of September 30, 2012 based on management's assertion included in PBGC's FY 2012 Annual Report and on the criteria contained in FMFIA, the objectives of which are the following:

- Financial reporting: Transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in conformity with accounting principles generally accepted in the U.S., and assets are safeguarded against loss from unauthorized acquisition, use, or disposition.
- Compliance with applicable laws and regulations: Transactions are executed in accordance with laws and regulations that could have a direct and material effect on the financial statements and any other laws, regulations, and government wide policies identified by OMB audit guidance.

We are also responsible for testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements, and laws for which OMB Bulletin 07-04 requires testing and performing limited procedures with respect to certain other information appearing in PBGC's FY 2012 Annual Report.

In order to fulfill these responsibilities, we (1) examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements; (2) assessed the appropriateness of the accounting principles used and significant estimates made by management; (3) evaluated the overall presentation of the financial statements; (4) obtained an understanding of PBGC and its operations, including its internal control related to financial reporting (including safeguarding of assets) and compliance with laws and regulations; (5) evaluated the effectiveness of the design of internal control; (6) tested the operating effectiveness of relevant internal controls over financial reporting (including safeguarding assets) and compliance, for the FY ended September 30, 2012; (7) considered the design of the process for evaluating and reporting on internal control and financial management systems under FMFIA; and (8) tested compliance for FY 2012 with selected provisions of certain laws and regulations. The procedures selected depend on the auditors' judgment, including our assessment of risks of material misstatement of the financial statements, whether due to fraud or error. We believe we obtained sufficient and appropriate audit evidence on which to base our opinion.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting and compliance. Because of inherent limitations in internal control, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected. We also caution that projecting our audit results to future periods is subject to risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate. In addition, we caution that our internal control testing may not be sufficient for other purposes.

We did not test compliance with all laws and regulations applicable to PBGC. We limited our tests of compliance to selected provisions of laws and regulations that have a direct and material effect on the financial statements, and to those required by OMB Bulletin 07-04 that we deemed applicable to PBGC's financial statements for the FY ended September 30, 2012. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We considered the material weaknesses identified above in determining the nature, timing, and extent of our audit procedures on the 2012 financial statements.

Management Comments and Our Evaluation

In commenting on the draft of this report (see section III of this report), PBGC's management concurred with the facts and conclusions in our report. We did not audit PBGC's written response and, accordingly, we express no opinion on it.

CliftonLarsonAllen LLP

Calverton, Maryland
November 14, 2012

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Audit of the Pension Benefit Guaranty Corporation's
Fiscal Year 2012 and 2011 Financial Statements

Audit Report AUD-2013-1 / FA-12-88-1

Section II

Pension Benefit Guaranty Corporation's Fiscal Year 2012 and 2011 Financial Statements

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF FINANCIAL CONDITION

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	September 30,		September 30,		September 30,	
(Dollars in Millions)	**2012**	2011	**2012**	2011	**2012**	2011
ASSETS						
Cash and cash equivalents	**$ 3,767**	$ 5,021	**$ 25**	$ 5	**$ 3,792**	$ 5,026
Securities lending collateral (Notes 3 and 5)	**3,425**	4,587	**0**	0	**3,425**	4,587
Investments, at market (Notes 3 and 5):						
Fixed maturity securities	**48,176**	46,257	**1,767**	1,720	**49,943**	47,977
Equity securities	**22,619**	17,997	**0**	0	**22,619**	17,997
Private equity	**1,339**	1,459	**0**	0	**1,339**	1,459
Real estate and real estate investment trusts	**511**	536	**0**	0	**511**	536
Other	**77**	22	**0**	0	**77**	22
Total investments	**72,722**	66,271	**1,767**	1,720	**74,489**	67,991
Receivables, net:						
Sponsors of terminated plans	**41**	31	**0**	0	**41**	31
Premiums (Note 11)	**1,086**	561	**1**	1	**1,087**	562
Sale of securities	**1,353**	1,807	**0**	0	**1,353**	1,807
Derivative contracts (Note 4)	**83**	178	**0**	0	**83**	178
Investment income	**452**	469	**12**	12	**464**	481
Other	**4**	3	**0**	0	**4**	3
Total receivables	**3,019**	3,049	**13**	13	**3,032**	3,062
Capitalized assets, net	**40**	32	**2**	1	**42**	33
Total assets	**$ 82,973**	$78,960	**$ 1,807**	$1,739	**$84,780**	$80,699

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

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF FINANCIAL CONDITION

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	September 30,		September 30,		September 30,	
(Dollars in Millions)	**2012**	2011	**2012**	2011	**2012**	2011
LIABILITIES						
Present value of future benefits, net (Note 6):						
Trusted plans	**$103,126**	$ 91,718	**$1**	$ 1	**$103,127**	$ 91,719
Plans pending termination and trusteeship	**418**	346	**0**	0	**418**	346
Settlements and judgments	**56**	56	**0**	0	**56**	56
Claims for probable terminations	**2,035**	833	**0**	0	**2,035**	833
Total present value of future benefits, net	**105,635**	92,953	**1**	1	**105,636**	92,954
Present value of nonrecoverable future financial assistance (Note 7)						
Insolvent plans	**0**	0	**1,388**	1,232	**1,388**	1,232
Probable insolvent plans	**0**	0	**5,622**	3,243	**5,622**	3,243
Total present value of nonrecoverable future financial assistance	**0**	0	**7,010**	4,475	**7,010**	4,475
Payables, net:						
Derivative contracts (Note 4)	**94**	173	**0**	0	**94**	173
Due for purchases of securities	**2,557**	4,079	**0**	0	**2,557**	4,079
Payable upon return of securities loaned	**3,425**	4,587	**0**	0	**3,425**	4,587
Unearned premiums	**328**	366	**30**	31	**358**	397
Accounts payable and accrued expenses (Note 8)	**76**	68	**3**	2	**79**	70
Total payables	**6,480**	9,273	**33**	33	**6,513**	9,306
Total liabilities	**112,115**	102,226	**7,044**	4,509	**119,159**	106,735
Net position	**(29,142)**	(23,266)	**(5,237)**	(2,770)	**(34,379)**	(26,036)
Total liabilities and net position	**$82,973**	$ 78,960	**$1,807**	$1,739	**$84,780**	$ 80,699

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

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	For the Years Ended September 30,		For the Years Ended September 30,		For the Years Ended September 30,	
(Dollars in Millions)	**2012**	2011	**2012**	2011	**2012**	2011
UNDERWRITING						
Income:						
Premium, net (Note 11)	**$ 2,642**	$ 2,072	**$ 92**	$ 92	**$ 2,734**	$ 2,164
Other	**13**	17	**-**	0	**13**	17
Total	**2,655**	2,089	**92**	92	**2,747**	2,181
Expenses:						
Administrative	**360**	353	**20**	14	**380**	367
Other	**-**	21	**-**	0	**-**	21
Total	**360**	374	**20**	14	**380**	388
Other underwriting activity:						
Losses from completed and probable terminations (Note 12)	**2,006**	201	**-**	0	**2,006**	201
Losses from insolvent and probable plans-financial assistance (Note 7)			**2,466**	1,461	**2,466**	1,461
Actuarial adjustments (credits) (Note 6)	**229**	1,672	**(6)**	37	**223**	1,709
Total	**2,235**	1,873	**2,460**	1,498	**4,695**	3,371
Underwriting gain (loss)	**60**	(158)	**(2,388)**	(1,420)	**(2,328)**	(1,578)
FINANCIAL:						
Investment income (loss) (Note 13):						
Fixed	**4,699**	3,502	**91**	148	**4,790**	3,650
Equity	**4,073**	(276)	**-**	0	**4,073**	(276)
Private equity	**42**	144	**-**	0	**42**	144
Other	**(22)**	76	**-**	0	**(22)**	76
Total	**8,792**	3,446	**91**	148	**8,883**	3,594
Expenses:						
Investment	**83**	71	**-**	0	**83**	71
Actuarial charges (Note 6):						
Due to expected interest	**3,927**	3,880	**54**	52	**3,981**	3,932
Due to change in interest rates	**10,718**	1,009	**116**	10	**10,834**	1,019
Total	**14,728**	4,960	**170**	62	**14,898**	5,022
Financial income (loss)	**(5,936)**	(1,514)	**(79)**	86	**(6,015)**	(1,428)
Net loss	**(5,876)**	(1,672)	**(2,467)**	(1,334)	**(8,343)**	(3,006)
Net position, beginning of year	**(23,266)**	(21,594)	**(2,770)**	(1,436)	**(26,036)**	(23,030)
Net position, end of year	**$ (29,142)**	$ (23,266)	**$ (5,237)**	$ (2,770)	**$ (34,379)**	$ (26,036)

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

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF CASH FLOWS

(Dollars in millions)	Single-Employer Program For the Years Ended September 30, 2012	2011	Multiemployer Program For the Years Ended September 30, 2012	2011	Memorandum Total For the Years Ended September 30, 2012	2011
OPERATING ACTIVITIES:						
Premium receipts	**$ 2,079**	$ 2,268	**$ 92**	$ 91	**$ 2,171**	$ 2,359
Interest and dividends received	**2,122**	2,155	**58**	74	**2,180**	2,229
Cash received from plans upon trusteeship	**126**	36	**0**	0	**126**	36
Receipts from sponsors/non-sponsors	**114**	70	**0**	0	**114**	70
Receipts from the missing participant program	**7**	6	**0**	0	**7**	6
Other receipts	**1**	1	**0**	0	**1**	1
Benefit payments – trusteed plans	**(5,333)**	(5,382)	**0**	0	**(5,333)**	(5,382)
Financial assistance payments			**(95)**	(115)	**(95)**	(115)
Settlements and judgments	**0**	0	**0**	0	**0**	0
Payments for administrative and other expenses	**(413)**	(428)	**(20)**	(13)	**(433)**	(441)
Accrued interest paid on securities purchased	**(234)**	(310)	**(3)**	(6)	**(237)**	(316)
Net cash provided (used) by operating activities (Note 15)	**(1,531)**	(1,584)	**32**	31	**(1,499)**	(1,553)
INVESTING ACTIVITIES:						
Proceeds from sales of investments	**77,382**	85,242	**667**	1,216	**78,049**	86,458
Payments for purchases of investments	**(77,105)**	(83,079)	**(679)**	(1,248)	**(77,784)**	(84,327)
Net change in investment of securities lending collateral	**(1,162)**	(841)	**0**	0	**(1,162)**	(841)
Net change in securities lending payable	**1,162**	841	**0**	0	**1,162**	841
Net cash provided (used) by investing activities	**277**	2,163	**(12)**	(32)	**265**	2,131
Net increase (decrease) in cash and cash equivalents	**(1,254)**	579	**20**	(1)	**(1,234)**	578
Cash and cash equivalents, beginning of year	**5,021**	4,442	**5**	6	**5,026**	4,448
Cash and cash equivalents, end of year	**$ 3,767**	$ 5,021	**$ 25**	$ 5	**$ 3,792**	$ 5,026

The accompanying notes are an integral part of these financial statements

NOTES TO FINANCIAL STATEMENTS

September 30, 2012 and 2011

Note 1: Organization and Purpose

The Pension Benefit Guaranty Corporation (PBGC or the Corporation) is a federal corporation created by Title IV of the Employee Retirement Income Security Act of 1974 (ERISA) and is subject to the provisions of the Government Corporation Control Act. Its activities are defined by ERISA, as that act has been amended over the years. The Corporation insures the pension benefits, within statutory limits, of participants in covered single-employer and multiemployer defined benefit pension plans.

ERISA requires that PBGC programs be self-financing. ERISA provides that the U.S. Government is not liable for any obligation or liability incurred by PBGC.

For financial statement purposes, PBGC divides its business activity into two broad areas – "Underwriting Activity" and "Financial Activity" – covering both single-employer and multiemployer program segments. PBGC's Underwriting Activity provides financial guaranty insurance in return for insurance premiums (whether actually paid or not). Actual and expected probable losses that result from the termination of underfunded pension plans are included in this category, as are actuarial adjustments based on changes in actuarial assumptions, such as mortality. Financial Activity consists of the performance of PBGC's assets and liabilities. PBGC's assets consist of premiums collected from defined benefit plan sponsors, assets from distress or involuntarily terminated plans that PBGC has insured, and recoveries from the former sponsors of those terminated plans. PBGC's future benefit liabilities consist of those future benefits, under statutory limits, that PBGC has assumed following distress or involuntary terminations. Gains and losses on PBGC's investments and changes in the value of PBGC's future benefit liabilities (e.g., actuarial charges such as changes in interest rates and expected interest) are included in this area.

As of September 30, 2012, the single-employer and multiemployer programs reported net positions of $(29.1) billion and $(5.2) billion, respectively. The single-employer program had assets of approximately $83.0 billion offset by total liabilities of $112.1 billion, which include a total present value of future benefits (PVFB) of approximately $105.6 billion. As of September 30, 2012, the multiemployer program had assets of $1.8 billion offset by approximately $7.0 billion in present value of nonrecoverable future financial assistance. Notwithstanding these deficits, the Corporation has sufficient liquidity to meet its obligations for a significant number of years; however, neither program at present has the resources to fully satisfy PBGC's long-term obligations to plan participants.

PBGC's $78.7 billion of total investments (including cash and investment income) represents the largest component of PBGC's Statements of Financial Condition combined assets of $84.8 billion at September 30, 2012. This amount of $78.7 billion (as compared to investments under management of $76.1 billion, as reported on page 35) reflects the fact that PBGC experiences a recurring inflow of trusteed plan assets that have not yet been incorporated into the PBGC investment program. For total investments (i.e., not the investment program), cash and fixed-income securities ($54.2 billion) represents 69 percent of the total investments, while equity securities ($22.6 billion) represents 29 percent of total investments. Private market assets ($1.3 billion), comprised largely of private equity, private debt, and real estate, represent 2 percent of the total investments.

Single-Employer and Multiemployer Program Exposure

PBGC's estimate of the total underfunding in single-employer plans sponsored by companies with credit ratings below investment grade, and which were classified by PBGC as reasonably possible of termination as of September 30, 2012, was $295 billion. The comparable estimates of the single-employer program's reasonably possible exposure for FY 2011 and FY 2010 were $227 billion and $170 billion, respectively. These estimates are measured as of December 31 of the previous year (see Note 9). For FY 2012, this exposure is concentrated in the following sectors: manufacturing (primarily automobile/auto parts, and primary and fabricated metals), transportation (primarily airlines), services, and wholesale and retail trade.

PBGC estimates that, as of September 30, 2012, it is reasonably possible that multiemployer plans may require future financial assistance in the amount of $27 billion. The comparable estimates of the multiemployer program's reasonable possible exposure for FY 2011 and FY 2010 were $23 billion and $20 billion, respectively. The increase in FY 2012 is primarily due to two large plans in the reasonably possible inventory. The sponsor of one plan, now with net liability of $20 billion, is in the "transportation, communication, and utilities" industry category; the other, now with net liability of $6 billion, is in the "agriculture, mining, and construction" industry category.

There is significant volatility in plan underfunding and sponsor credit quality over time, which makes long-term estimation of PBGC's expected claims difficult. This volatility, and the concentration of claims in a relatively small number of terminated plans, have characterized PBGC's experience to date and will likely continue. Among the factors that will influence PBGC's claims going forward are economic conditions affecting interest rates, financial markets, and the rate of business failures.

PBGC's sources of information on plan underfunding are the most recent Section 4010 and PBGC premium filings, and other submissions to the Corporation. PBGC publishes Table S-49, "Various Measures of Underfunding in PBGC-Insured Plans," in its *Pension Insurance Data Book* where the limitations of the estimates are fully and appropriately described.

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

Under the multiemployer program, if a plan becomes insolvent, it receives financial assistance from PBGC to allow the plan to continue to pay participants their guaranteed benefits. PBGC recognizes assistance as a loss to the extent that the plan is not expected to be able to repay these amounts from future plan contributions, employer withdrawal liability or investment earnings. Since multiemployer plans do not receive PBGC assistance until fully insolvent, financial assistance is almost never repaid; for this reason such assistance is fully reserved.

Note 2: Significant Accounting Policies

Basis of Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). The preparation of the financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates and assumptions may change over time as new information is obtained or subsequent developments occur. Actual results could differ from those estimates.

Recent Accounting Developments

During FY 2012, PBGC implemented FASB Accounting Standards update No. 2011-04, Fair Value Measurement (Topic 820), *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. This Update includes disclosure of the valuation techniques to price Level 3 fair value measurements, as well as disclosure of the sensitivity of different inputs into the valuation process. In addition, PBGC implemented FASB Accounting Standards Update No. 2011-03, Transfers and Servicing (Topic 860), *Reconsideration of Effective Control for Repurchase Agreements*. This Update addresses the rescission of financial reporting disclosure requirements effective in fiscal year 2011 to eliminate the collateral maintenance implementation guidance. See Note 3 for disclosures of Repurchase Agreements.

During FY 2011, PBGC implemented FASB Accounting Standards Update No. 2009-16, *Transfers and Servicing (Topic 860) – Accounting for Transfers of Financial Assets* and FASB Accounting Standards Update No. 2011-02, *Receivables (Topic 310) – A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring*. Accounting Standards Update 2009-16 improves the relevance, representations, and comparability of the information that PBGC provides in its financial reports regarding transfers of financial assets. See Note 3 for disclosures regarding Securities Lending and Repurchase Agreements. Accounting Standards Update 2011-02 requires disclosures for loan modifications that constitute troubled debt restructurings. See Note 7 for disclosures on multiemployer financial assistance notes receivable.

Valuation Method

A primary objective of PBGC's financial statements is to provide information that is useful in assessing PBGC's present and future ability to ensure that its plan beneficiaries receive benefits when due. Accordingly, PBGC values its financial assets at estimated fair value, consistent with the standards for pension plans contained in the FASB Accounting Standards Codification Section 960, *Defined Benefit Pension Plans*. PBGC values its liabilities for the present value of future benefits and present value of nonrecoverable future financial assistance using assumptions derived from annuity prices from insurance companies, as described in the Statement of Actuarial Opinion. As described in Section 960, the assumptions are "those assumptions that are inherent in the estimated cost at the (valuation) date to obtain a contract with an insurance company to provide participants with their accumulated plan benefits." Also, in accordance with Section 960, PBGC selects assumptions for expected retirement ages and the cost of administrative expenses in accordance with its best estimate of anticipated experience.

The FASB Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures*, defines fair value, establishes a framework for measuring fair value in U.S. GAAP, and expands disclosures about fair value measurements. Section 820 applies to accounting pronouncements that require or permit fair value measurements. Prior to Section 820, there were different definitions of fair value with limited guidance for applying those definitions in U.S. GAAP; additionally, the issuance for applying fair value was dispersed among many accounting pronouncements that require fair value measurement.

Revolving and Trust Funds

PBGC accounts for its single-employer and multiemployer programs' revolving and trust funds on an accrual basis. Each fund is charged its portion of the benefits paid each year. PBGC includes totals for both the revolving and trust funds for presentation purposes in the financial statements; however, the single-employer and multiemployer programs are separate programs by law and, therefore, PBGC also reports them separately.

ERISA provides for the establishment of the revolving fund where premiums are collected and held. The assets in the revolving fund are used to cover deficits incurred by plans trusteed and to provide funds for financial assistance. The Pension Protection Act of 1987 created a single-employer revolving fund (fund 7) that is credited with all premiums in excess of $8.50 per participant, including all penalties and interest charged on these amounts, and its share of earnings from investments. This fund may not be used to pay PBGC's administrative costs or the benefits of any plan terminated prior to October 1, 1988, unless no other amounts are available.

The trust funds include assets (e.g., pension plan investments) PBGC assumes (or expects to assume) once a terminated plan has been trusteed, and related investment income. These assets generally are held by custodian banks. The trust funds support the operational functions of PBGC.

The trust funds reflect accounting activity associated with:

1) trusteed plans – plans for which PBGC has legal responsibility – the assets and liabilities are reflected separately on PBGC's Statements of Financial Condition, the income and expenses are included in the Statements of Operations and Changes in Net Position and the cash flows from these plans are included in the Statements of Cash Flows.

2) plans pending termination and trusteeship – plans for which PBGC has begun the process for termination and trusteeship by fiscal year-end – the assets and liabilities for these plans are reported as a net amount on the liability side of the Statements of Financial Condition under "Present value of future benefits, net." For these plans, the income and expenses are included in the Statements of Operations and Changes in Net Position, but the cash flows are not included in the Statements of Cash Flows.

3) probable terminations – plans that PBGC determines are likely to terminate and be trusteed by PBGC – the assets and liabilities for these plans are reported as a net amount on the liability side of the Statements of Financial Condition under "Present value of future benefits, net." The accrued loss from these plans is included in the Statements of Operations and Changes in Net Position as part of "Losses from completed and probable terminations." The cash flows from these plans are not included in the Statements of Cash Flows. PBGC cannot exercise legal control over a plan's assets until it becomes trustee.

Allocation of Revolving and Trust Funds

PBGC allocates assets, liabilities, income and expenses to the single-employer and multiemployer programs' revolving and trust funds to the extent that such amounts are not directly attributable to a specific fund. Revolving fund investment income is allocated on the basis of each program's average cash and investments available during the year, while the expenses are allocated on the basis of each program's present value of future benefits and present value of nonrecoverable future financial assistance. Revolving fund assets and liabilities are allocated according to the year-end equity of each program's revolving funds. Plan assets acquired by PBGC and commingled at PBGC's custodian bank are credited directly to the appropriate fund, while the earnings and expenses on the commingled assets are allocated to each program's trust funds on the basis of each trust fund's value, relative to the total value of the commingled fund.

Cash and Cash Equivalents

Cash includes cash on hand and demand deposits. Cash equivalents are investments with original maturities of one business day and highly liquid investments that are readily convertible into cash within one business day.

Securities Lending Collateral

PBGC participates in a securities lending program administered by its custodian bank. The custodian bank requires collateral that equals 102 percent to 105 percent of the securities lent. The collateral is held by the custodian bank. The custodian bank either receives cash or non-cash as collateral or returns collateral to cover mark-to-market changes. Any cash collateral received is invested by PBGC's investment agent. In addition to the lending program managed by the custodian bank, some of PBGC's investment managers are authorized to invest in securities purchased under resale agreements (an agreement with a commitment by the seller to buy a security back from the purchaser at a specified price at a designated future date), and securities sold under repurchase agreements.

Investment Valuation and Income

PBGC bases market values on the last sale of a listed security, on the mean of the "bid-and-ask" for nonlisted securities, or on a valuation model in the case of fixed income securities that are not actively traded. These valuations are determined as of the end of each fiscal year. Purchases and sales of securities are recorded on the trade date. In addition, PBGC invests in and discloses its derivative investments in accordance with the guidance contained in the FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*. Investment income is accrued as earned. Dividend income is recorded on the ex-dividend date. Realized gains and losses on sales of investments are calculated using first-in, first-out for the revolving fund and average cost for the trust fund. PBGC marks the plan's assets to market and any increase or decrease in the market value of a plan's assets occurring after the date on which the plan is terminated must, by law, be credited to or suffered by PBGC.

Securities Purchased Under Resale Agreements

Securities purchased under resale agreements are agreements whereby the purchaser agrees to buy securities from the seller, and subsequently sell them back at a pre-agreed price and date. Those greater than one day are reported under "Fixed maturity securities" as "Securities purchased under resale agreements" in the Note 3 table entitled "Investments of Single-Employer Revolving Funds and Single-Employer Trusteed Plans," on page 61. Resale agreements that mature in one day are included in "Cash and cash equivalents" which are reported on the Statements of Financial Condition.

Sponsors of Terminated Plans

The amounts due from sponsors of terminated plans or members of their controlled group represent the settled, but uncollected, claims for employer liability (underfunding as of date of plan termination) and for contributions due their plan less an allowance for estimated uncollectible amounts. PBGC discounts any amounts expected to be received beyond one year for time and risk factors. Some agreements between PBGC and plan sponsors provide for contingent payments based on future profits of the sponsors. The Corporation will report any such future amounts in the period they are realizable. Income and expenses related to amounts due from sponsors are reported in the underwriting section of the Statements of Operations and Changes in Net Position. Interest earned on settled claims for employer liability and due and unpaid employer contributions (DUEC) is reported as "Income: Other." The change in the allowances for uncollectible employer liability and DUEC is reported as "Expenses: Other."

Premiums

Premiums receivable represent the estimated earned but unpaid portion of the premiums for plans that have a plan year commencing before the end of PBGC's fiscal year and past due premiums deemed collectible, including penalties and interest. The liability for unearned premiums represents an estimate of payments received during the fiscal year that cover the portion of a plan's year after PBGC's fiscal year-end. "Premium income, net" represents actual and estimated revenue generated from defined benefit pension plan premium filings as required by Title IV of ERISA less bad debt expense for premiums, interest, and penalties (see Note 11).

In accordance with the FASB Accounting Standards Codification Section 605-10-S99*, Revenue Recognition*, PBGC has strengthened the revenue recognition policy for termination premiums in bankruptcy and non-bankruptcy liquidations. The effect of this did not result in material change for our financial statements. We did not adjust any prior-period information. The effect of the change on income from operations and other items are immaterial, and there is no material effect on any other components of equity or net assets.

Capitalized Assets

Capitalized assets include furniture and fixtures, electronic processing equipment and internal-use software. This includes costs for internally developed software incurred during the application development stage (system design including software configuration and software interface, coding, testing including parallel processing phase). These costs are shown net of accumulated depreciation and amortization.

Present Value of Future Benefits (PVFB)

The PVFB is the estimated liability for future pension benefits that PBGC is or will be obligated to pay the participants of trusteed plans and the net liability for plans pending termination and trusteeship. The PVFB liability (including trusteed plans as well as plans pending termination and trusteeship) is stated as the actuarial present value of estimated future benefits less the present value of estimated recoveries from sponsors and members of their controlled group and the assets of plans pending termination and trusteeship as of the date of the financial statements. PBGC also includes the estimated liabilities attributable to plans classified as probable terminations as a separate line item in the PVFB (net of estimated recoveries and plan assets). PBGC uses assumptions to adjust the value of those future payments to reflect the time value of money (by discounting) and the probability of payment (by means of decrements, such as for death or retirement). PBGC also includes anticipated expenses to settle the benefit obligation in the determination of the PVFB. PBGC's benefit payments to participants reduce the PVFB liability.

The values of the PVFB are particularly sensitive to changes in underlying estimates and assumptions. These estimates and assumptions could change and the impact of these changes may be material to PBGC's financial statements (see Note 6).

(1) Trusteed Plans–represents the present value of future benefit payments less the present value of expected recoveries (for which a settlement agreement has not been reached with sponsors and members of their controlled group) for plans that have terminated and been trusteed by PBGC prior to fiscal year-end. Assets are shown separately from liabilities for trusteed plans.

(2) Pending Termination and Trusteeship–represents the present value of future benefit payments less the plans' net assets (at fair value) anticipated to be received and the present value of expected recoveries (for which a settlement agreement has not been reached with sponsors and members of their controlled group) for plans for which termination action has been initiated and/or completed prior to fiscal year-end. Unlike trusteed plans, the liability for plans pending termination and trusteeship is shown net of plan assets.

(3) Settlements and Judgments–represents estimated liabilities related to settled litigation.

(4) Net Claims for Probable Terminations–In accordance with the FASB Accounting Standards Codification Section 450, *Contingencies*, PBGC recognizes net claims for probable terminations which represent PBGC's best estimate of the losses, net of plan assets, and the present value of expected recoveries

(from sponsors and members of their controlled group) for plans that are likely to terminate in the future. The PBGC threshold for recognition of net claims for probable termination is $50 million or more of underfunding. These estimated losses are based on conditions that existed as of PBGC's fiscal year-end. Management believes it is likely that one or more events subsequent to PBGC's fiscal year-end will occur, confirming the loss.

Criteria used for classifying a specific single-employer plan as a probable termination include, but are not limited to, one or more of the following conditions: the plan sponsor is in liquidation or comparable state insolvency proceeding with no known solvent controlled group member; sponsor has filed or intends to file for distress plan termination and the criteria will likely be met; or PBGC is considering the plan for involuntary termination. In addition, management takes into account other economic events and factors in making judgments regarding the classification of a plan as a probable termination. These events and factors may include, but are not limited to: the plan sponsor is in bankruptcy or has indicated that a bankruptcy filing is imminent; the plan sponsor has stated that plan termination is likely; the plan sponsor has received a going concern opinion from its independent auditors; or the plan sponsor is in default under existing credit agreement(s).

In addition, a reserve for small unidentified probable losses and incurred but not reported (IBNR) claims is recorded based on an actuarial loss development methodology (ratio method) (see Note 6).

(5) PBGC identifies certain plans as high-risk if the plan sponsor is in Chapter 11 proceedings or the sponsor's senior unsecured debt is rated CCC+/Caa1 or lower by S&P or Moody's respectively. PBGC specifically reviews each plan identified as high-risk and classifies those plans as probable if, based on available evidence, PBGC concludes that plan termination is likely (based on criteria described in (4) above). Otherwise, high-risk plans are classified as reasonably possible.

(6) In accordance with Section 450, PBGC's exposure to losses from plans of companies that are classified as reasonably possible is disclosed in the footnotes. In order for a plan sponsor to be specifically classified as reasonably possible, it must first have $5 million or more of underfunding, as well as meet additional criteria. Criteria used for classifying a company as reasonably possible include, but are not limited to, one or more of the following conditions: the plan sponsor is in Chapter 11 reorganization; funding waiver pending or outstanding with the Internal Revenue Service; sponsor missed minimum funding contribution; sponsor's bond rating is below-investment-grade for Standard & Poor's (BB+) or Moody's (Ba1); or sponsor has no bond rating but the Dun & Bradstreet Financial Stress Score is below the threshold considered to be investment grade (see Note 9).

Present Value of Nonrecoverable Future Financial Assistance

In accordance with Title IV of ERISA, PBGC provides financial assistance to multiemployer plans, in the form of loans, to enable the plans to pay guaranteed benefits to participants and reasonable administrative expenses. These loans, issued in exchange for interest-bearing promissory notes, constitute an obligation of each plan.

The present value of nonrecoverable future financial assistance represents the estimated nonrecoverable payments to be provided by PBGC in the future to multiemployer plans that will not be able to meet their benefit obligations. The present value of nonrecoverable future financial assistance is based on the difference between the present value of future guaranteed benefits and expenses and the market value of plan assets, including the present value of future amounts expected to be paid by employers, for those plans that are expected to require future assistance. The amount reflects the rates at which, in the opinion of management, these liabilities (net of expenses) could be settled in the market for single-premium nonparticipating group annuities issued by private insurers (see Note 7).

A liability for a particular plan is included in the "Present Value of Nonrecoverable Future Financial Assistance" when it is determined that the plan is currently, or will likely become in the future, insolvent and will require assistance to pay the participants their guaranteed benefit. In accordance with the FASB Accounting Standards Codification Section 450, *Contingencies*, PBGC recognizes net claims for probable insolvencies for plans that are likely to become insolvent and require financial assistance in the future. Projecting a future insolvency requires considering several complex factors, such as an estimate of future cash flows, future mortality rates, and age of participants not in pay status.

Each year, PBGC analyzes insured multiemployer plans to identify those plans that are at risk of becoming claims on the insurance program. Regulatory filings with PBGC and the other ERISA agencies are important to this analysis and determination of risk. For example, a multiemployer plan that no longer has contributing employers files a notice of termination with PBGC. In general, if a terminated plan's assets are less than the present value of its liabilities, PBGC considers the plan a probable risk of requiring financial assistance in the future.

PBGC also analyzes ongoing multiemployer plans (i.e., plans that continue to have employers making regular contributions for covered work) to determine whether any such plans may be probable or possible claims on the insurance program. In conducting this analysis each year, PBGC examines plans that are chronically underfunded, have poor cash flow trends, a falling contribution base, and that may lack a sufficient asset cushion to weather income losses. A combination of these factors, or any one factor that is of sufficient concern, leads to a more detailed analysis of the plan's funding and the likelihood that the contributing employers will be willing and able to maintain the plan.

PBGC utilizes specific criteria for insolvent (PBGC's insurable event for multiemployer plans), probable, and reasonably possible classification of multiemployer plans. The criteria are as follows:

- Any multiemployer plans currently receiving financial assistance are classified as insolvent.
- Terminated, underfunded multiemployer plans (i.e., "wasting trusts") are classified as probable.
- Ongoing multiemployer plans projected to become insolvent:
  - within ten years are classified as probable,
  - from ten to twenty years are classified as reasonably possible.

In general, the date of insolvency is estimated by projecting plan cash flows using PBGC's actuarial assumptions for terminated plans, but also considered are projections based on other assumptions, such as those used by the plan actuary.

Note that PBGC has initiated a comprehensive review of accounting policies and processes addressing the classification and measurement of potential claims for financial assistance by multiemployer plans that may become insolvent in the future. This review will include (1) benchmarking the current accounting policy against other, similar contingent liability accounting policies, (2) identifying and analyzing alternative contingent liability processes, and (3) developing recommendations on possible modification to the current policies and processes. PBGC anticipates that any such modifications will be adopted and implemented by the end of fiscal year 2013. These steps are consistent with PBGC's ongoing efforts to review the efficacy of its accounting policies each year.

The present value of nonrecoverable future financial assistance is presented in the Liability section of the Statements of Financial Condition (see Note 7).

Securities Sold Under Repurchase Agreements

Securities sold under repurchase agreements are agreements with a commitment by the seller to buy a security back from the purchaser at a specified price and designated future date. These agreements represent collateralized short-term loans for which the collateral may be a treasury security, money market instrument, federal agency security, or mortgage-backed security. On the Statements of Financial Condition, securities sold under repurchase agreements are reported as a liability, "Securities sold under repurchase agreements" at the amounts at which the securities will be subsequently reacquired.

Administrative Expenses

These operating expenses (for either the single-employer or multiemployer insurance programs) are amounts paid and accrued for services rendered or while carrying out other activities that constitute PBGC's ongoing operations, e.g., payroll, contractual services, office space, material and supplies, etc. The expense allocation methodology fully captures the administrative expenses attributable to either the single-employer or multiemployer insurance programs.

Other Expenses

These expenses represent an estimate of the net amount of receivables deemed to be uncollectible during the period. The estimate is based on the most recent status of the debtor (e.g., sponsor), the age of the receivables and other factors that indicate the element of uncollectibility in the receivables outstanding.

Losses from Completed and Probable Terminations

Amounts reported as losses from completed and probable terminations represent the difference as of the actual or expected date of plan termination (DOPT) between the present value of future benefits (including amounts owed under Section 4022(c) of ERISA) assumed, or expected to be assumed, by PBGC, less related plan assets and the present value of expected recoveries from sponsors and members of their controlled group (see Note 12). When a plan terminates, the previously recorded probable net claim is reversed and newly estimated DOPT plan assets, recoveries and PVFB are netted and reported on the line "PVFB - Plans pending termination and trusteeship" (this value is usually different than the amount previously reported), with any change in the estimate being recorded in the Statements of Operations and Changes in Net Position. In addition, the plan's net income from date of plan termination to the beginning of PBGC's fiscal year is included as a component of losses from completed and probable terminations for plans with termination dates prior to the year in which they were added to PBGC's inventory of terminated plans.

Actuarial Adjustments and Charges (Credits)

PBGC classifies actuarial adjustments related to insurance based changes in method and the effect of experience as underwriting activity; actuarial adjustments are the result of the movement of plans from one valuation methodology to another, e.g., nonseriatim (calculating the liability for the group) to seriatim (calculating separate liability for each person), and of new data (e.g., deaths, revised participant data). Actuarial charges (credits) related to changes in interest rates and expected interest is classified as financial activity. These adjustments and charges (credits) represent the change in the PVFB that results from applying actuarial assumptions in the calculation of future benefit liabilities (see Note 6).

To ensure consistency and comparability of the information presented in PBGC's FY 2011 and FY 2012 financial statements and consistent with the presentation for the single-employer program, beginning FY 2012, losses from financial assistance in the multiemployer program have been reclassified to actuarial charges, credits, and adjustments. These categories provide improved transparency for those plans receiving and/or about to begin receiving financial assistance from the multiemployer program. In our FY 2011 Statements of Operations and Changes in Net Position, losses from financial assistance decreased $99 million and actuarial adjustments increased $37 million, resulting in a reclassification to the underwriting gain of $62 million. Furthermore, in the financial portion of the Statements of Operations and Changes in Net Position, due to expected interest increased by $52 million and due to change in interest rates increased by $10 million, resulting in a reclassification to the financial loss of $62 million. All such changes were reclassified within the FY 2011 Statements of Operations and Changes in Net Position, and have no impact on FY 2011 net position. Likewise, such FY 2012 Statements of Operations and Changes in Net Position reclassifications have no impact on FY 2012 net position.

Depreciation and Amortization

PBGC calculates depreciation on the straight-line basis over estimated useful lives of 5 years for equipment and 10 years for furniture and fixtures. PBGC calculates amortization for capitalized software, which includes certain costs incurred for purchasing and developing software for internal use, on the straight-line basis over estimated useful lives not to exceed 5 years, commencing on the date that the Corporation determines that the internal-use software is implemented. Routine maintenance and leasehold improvements (the amounts of which are not material) are charged to operations as incurred. Capitalization of software cost occurs during the development stage and costs incurred during the preliminary project and post-implementation stages are expensed as incurred.

Note 3: Investments

Premium receipts are invested through the revolving fund in U.S. Treasury securities. The trust funds include assets PBGC assumes or expects to assume with respect to terminated plans (e.g., recoveries from sponsors) and investment income thereon. These assets generally are held by custodian banks. The basis and market value of the investments by type are detailed below as well as related investment profile data. The basis indicated is cost of the asset if assumed after the date of plan termination or the market value at date of plan termination if the asset was assumed as a result of a plan's termination. PBGC marks the plan's assets to market and any increase or decrease in the market value of a plan's assets occurring after the date on which the plan is terminated must, by law, be credited to or suffered by PBGC. Investment securities denominated in foreign currency are translated into U.S. dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income, and expenses are translated into U.S. dollars at the prevailing exchange rates on the respective dates of the transactions. The portfolio does not isolate that portion of the results of operations resulting from changes in foreign exchange rates of investments from the fluctuations arising from changes in market prices of securities held. Such fluctuations are included with the net realized and unrealized gain or loss on investments. For PBGC's securities, unrealized holding gains and losses are both recognized by including them in earnings. Unrealized holding gains and losses measure the total change in fair value – consisting of unpaid interest income earned or unpaid accrued dividend and the remaining change in fair value from holding the security.

To Be Announced (TBA) and Bond Forward transactions are recorded as regular buys and sells of investments and not as derivatives. TBA is a contract for the purchase or sale of mortgage-backed securities to be delivered on a future date. The term TBA is derived from the fact that the actual mortgage-backed security that will be delivered to fulfill a TBA trade is not designated at the time the trade is made. The securities are to be announced 48 hours prior to the established trade settlement date. TBAs are issued by FHLMC, FNMA, and GNMA. In accordance with FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*, TBA and Bond Forward contracts are deemed regular way trades as they are completed within the time frame generally established by regulations and conventions in the market place or by the exchange on which they are executed. Thus, recording of TBA and Bond Forward contracts recognizes the acquisition or disposition of the securities at the full contract amounts on day one of the trade.

In prior years, foreign exchange forward contracts and swap contracts were recorded gross of receivables and payables. Beginning in FY 2010, foreign exchange forwards are included in "Fixed maturity securities" rather than "Receivables, net – Derivative contracts" or "Derivative contracts" (liabilities). Swaps are netted rather than recorded at gross levels for the individual contracts as "Receivables, net – Derivative contracts" and "Derivative contracts" (liabilities). Certain amounts shown as futures for receivables and payables were offset to reflect a net margin variation for one recently trusteed plan. Bond forwards and TBAs have been reclassified to "Receivables, net – Sale of securities" and "Due for purchases of securities" from derivative contracts receivables and payables.

As the following table illustrates, the market value of investments of the single-employer program increased significantly from September 30, 2011, to September 30, 2012.

INVESTMENTS OF SINGLE-EMPLOYER REVOLVING FUNDS AND SINGLE-EMPLOYER TRUSTEED PLANS

	September 30, 2012			September 30, 2011	
(Dollars in millions)	**Basis**	**Market Value**		Basis	Market Value
Fixed maturity securities:					
U.S. Government securities	**$21,122**	**$23,629**		$20,935	$23,775
Commercial paper/securities purchased under resale agreements	**442**	**442**		6	6
Asset backed securities	**3,350**	**3,509**		5,088	5,150
Pooled funds					
Domestic	**450**	**408**		374	393
International	**0**	**0**		0	0
Global/other	**0**	**0**		0	0
Corporate bonds and other	**9,798**	**11,073**		11,021	11,765
International securities	**8,443**	**9,115**		5,088	5,168
Subtotal	**43,605**	**48,176**		42,512	46,257
Equity securities:					
Domestic	**2,047**	**2,417**		1,678	1,681
International	**575**	**670**		1,067	1,015
Pooled funds					
Domestic	**8,128**	**10,798**		6,377	7,990
International	**5,805**	**8,733**		5,373	7,308
Global/other	**1**	**1**		3	3
Subtotal	**16,556**	**22,619**		14,498	17,997
Private equity	**1,398**	**1,339**		1,452	1,459
Real estate and real estate investment trusts	**445**	**511**		447	536
Insurance contracts and other investments	**84**	**77**		23	22
Total*	**$62,088**	**$72,722**	**	$58,932	$66,271

*Total includes securities on loan at September 30, 2012, and September 30, 2011, with a market value of $4.298 billion and $6.125 billion, respectively.

**This total of $72.72 billion of investments at market value represents the single-employer assets only. It differs from the total investments of $78.74 billion shown on page 35 of this report which includes investments of the multiemployer program, cash and cash equivalents and accrued investment income.

INVESTMENTS OF MULTIEMPLOYER REVOLVING FUNDS AND MULTIEMPLOYER TRUSTEED PLANS

	September 30, 2012		September 30, 2011	
(Dollars in millions)	**Basis**	**Market Value**	Basis	Market Value
Fixed maturity securities:				
U.S. Government securities	**$1,568**	**$1,767**	$1,533	$1,720
Equity securities	**0**	**0**	0	0
Total	**$1,568**	**$1,767**	$1,533	$1,720

INVESTMENT PROFILE

	September 30, 2012	September 30, 2011
Fixed Income Assets		
Average Quality	**AA**	AA
Average Maturity (years)	**14.0**	14.9
Duration (years)	**9.3**	9.6
Yield to Maturity (%)	**2.7**	3.3
Equity Assets		
Average Price/Earnings Ratio	**15.6**	12.9
Dividend Yield (%)	**2.6**	2.9
Beta	**1.03**	1.03

Derivative Instruments

PBGC assigns investment discretion and grants specific authority to all of its investment managers to invest according to specific portfolio investment guidelines established by PBGC. PBGC further limits the use of derivatives by investment managers through tailored provisions in the investment guidelines with investment managers consistent with PBGC's investment policy statement and overall risk tolerance. These investment managers, who act as fiduciaries to PBGC, determine when it may or may not be appropriate to utilize derivatives in the portfolio(s) for which they are responsible. Investments in derivatives carry many of the same risks of the underlying instruments and carry additional risks that are not associated with direct investments in the securities underlying the derivatives. Furthermore, risks may arise from the potential inability to terminate or sell derivative positions, although derivative instruments are generally more liquid than physical market instruments. A liquid secondary market may not always exist for certain derivative positions at any time. Over-the-counter derivative instruments also involve counterparty risk that the other party to the derivative instrument will not meet its obligations.

The use of derivatives by PBGC investment managers is restricted in-so-far as portfolios cannot utilize derivatives to create leverage in the portfolios for which they are responsible. That is, the portfolios shall not utilize derivatives to leverage the portfolio beyond the maximum risk level associated with a fully invested portfolio of physical securities.

Derivative instruments are used (1) to mitigate risk (e.g., adjust duration or currency exposures), (2) to enhance investment returns, and/or (3) as liquid and cost-efficient substitutes for positions in physical securities. These derivative instruments are not designated as accounting hedges consistent with FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*, which requires an active designation as a prerequisite for any hedge accounting. PBGC utilizes a no hedging designation which results in the gain or loss on a derivative instrument to be recognized currently in earnings. Derivatives are accounted for at fair market value in accordance with the FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*. Derivatives are marked to market with changes in value reported as a component of financial income on the Statements of Operations and Changes in Net Position. PBGC presents all derivatives at fair value on the Statements of Financial Condition.

During fiscal years 2012 and 2011, PBGC, through its investment managers, invested in investment products that used various U.S. and non-U.S. derivative instruments including but not limited to: S&P 500 index futures, options, money market futures, government bond futures, interest rate, credit default and total return swaps and swaption contracts, stock warrants and rights, debt option contracts, and foreign currency forward and option contracts. Some of these derivatives are traded on organized exchanges and thus bear minimal counterparty risk. The counterparties to PBGC's non-exchange-traded derivative contracts are major financial institutions subject to ISDA (International Swaps and Derivatives Association, Inc.) master agreements. PBGC monitors its counterparty risk and exchanges collateral under most contracts to further support performance by its counterparties.

A futures contract is an agreement between a buyer or seller and an established futures exchange clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date) in the future. The futures exchanges and clearinghouses clear, settle, and guarantee transactions occurring through their facilities. Upon entering into a futures contract, an "initial margin" amount (in cash or liquid securities) of generally one to six percent of the face value indicated in the futures contract is required to be deposited with the broker. Open futures positions are marked to market daily. Subsequent payments known as "variation margin" are made or received by the portfolio dependent upon the daily fluctuations in value of the underlying contract. PBGC maintains adequate liquidity in its portfolio to meet these margin calls.

PBGC also invests in forward contracts. A forward foreign currency contract is a commitment to purchase or sell a foreign currency at the settlement date (in the future) at a negotiated rate. Foreign currency forward, futures, and option contracts may be used as a substitute for cash currency holdings, in order to minimize currency risk exposure to changes in foreign currency exchange rates and to adjust overall currency exposure to reflect the investment views of the fixed income and equity portfolio managers regarding relationships between currencies.

A swap is an agreement between two parties to exchange different financial returns on a notional investment amount. The major forms of swaps traded are interest rate swaps, credit default swaps, and total return swaps. PBGC uses swap and swaption (an option on a swap) contracts to adjust exposure to interest rates, fixed income securities exposure, credit exposure, and equity exposure, and to generate income based on the investment views of the portfolio managers regarding interest rates, indices and individual issues.

Interest rate swaps involve exchanges of fixed rate and floating rate interest. Interest rate swaps are often used to alter exposure to interest rate fluctuations, by swapping fixed rate obligations for floating rate obligations, or vice versa. The counterparties to the swap agree to exchange interest payments on specific dates, according to a predetermined formula. The payment flows are usually netted against each other, with one party paying the difference to the other.

A credit default swap is a contract between a buyer and seller of protection against pre-defined credit events. PBGC may buy or sell credit default swap contracts to seek to increase the portfolio's income or to mitigate the risk of default on portfolio securities.

A total return swap is a contract between a buyer and seller of exposures to certain asset classes such as equities. PBGC may buy or sell total return contracts to seek to increase or reduce the portfolio's exposure to certain asset classes.

An option contract is a contract in which the writer of the option grants the buyer of the option the right to purchase from (call option) or sell to (put option) the writer a designated instrument at a specified price within a specified period of time.

Stock warrants and rights allow PBGC to purchase securities at a stipulated price within a specified time limit.

For the fiscal years ended September 30, 2012 and 2011, gains and losses from settled margin calls are reported in Investment income on the Statements of Operations and Changes in Net Position. Securities and cash are pledged as collateral for derivative contracts (e.g., futures and swaps) are recorded as a receivable or payable.

Effective January 1, 2009, PBGC adopted the provisions of the FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*. This standard requires the disclosure of fair values of derivative instruments and their gains and losses in its financial statements of both the derivative positions existing at period end and the effect of using derivatives during the reporting period. The first table below identifies the location of derivative fair market values (FMV) on the Statements of Financial Condition, as well as the notional amounts, while the second table identifies the location of derivative gains and losses on the Statements of Operations and Changes in Net Position as of September 30, 2012, and September 30, 2011.

FAIR VALUES OF DERIVATIVE INSTRUMENTS

	Asset Derivative					
	September 30, 2012			September 30, 2011		
(Dollars in millions)	Statements of Financial Condition Location	**Notional**	**FMV**	Statements of Financial Condition Location	Notional	FMV
Futures	Derivative Contracts	**$1,323**	**$4**	Derivative Contracts	$3,586	$90
Swap agreements						
Interest rate swaps	Investments-Fixed	**1,904**	**12**	Investments-Fixed	1,330	(15)
Credit default swaps	Investments-Fixed	**2,180**	**14**	Investments-Fixed	2,150	6
Option contracts	Investments-Fixed	**146**	**2**	Investments-Fixed	121	1
Forwards - foreign exchange	Investments-Fixed	**4,650**	**(27)**	Investments-Fixed	3,021	26
	Investments-Equity	**0**	**0**	Investments-Equity	45	1

	Liability Derivative					
	September 30, 2012			September 30, 2011		
(Dollars in millions)	Statements of Financial Condition Location	**Notional**	**FMV**	Statements of Financial Condition Location	Notional	FMV
Futures	Derivative Contracts	**$2,283**	**$ (9)**	Derivative Contracts	$2,148	$ (2)
Option contracts	Derivative Contracts	**1,042**	**(11)**	Derivative Contracts	1,202	(4)

Additional information specific to derivative instruments is disclosed in Note 4 – Derivative Contracts, and Note 5 – Fair Value Measurements.

EFFECT OF DERIVATIVE CONTRACTS ON THE STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION

(Dollars in millions)	Location of Gain or (Loss) Recognized in Income on Derivatives	Amount of Gain or (Loss) Recognized in Income on Derivatives	
		Sept. 30, 2012	Sept. 30, 2011
Futures			
Contracts in a receivable position	Investment Income-Fixed	**$9**	($38)
Contracts in a receivable position	Investment Income-Equity	**0**	0
Contracts in a payable position	Investment Income-Fixed	**69**	177
Contracts in a payable position	Investment Income-Equity	**0**	0
Swap agreements			
Interest rate swaps	Investment Income-Fixed	**14**	0
Credit default swaps	Investment Income-Fixed	**38**	12
Option contracts			
Options purchased (long)	Investment Income-Fixed	**(14)**	3
Options purchased (long)	Investment Income-Equity	**0**	0
Options written (sold short)	Investment Income-Fixed	**4**	2
Options written (sold short)	Investment Income-Equity	**0**	0
Forward contracts			
Forwards - foreign exchange	Investment Income-Fixed	**14**	(42)
	Investment Income-Equity	**0**	1

Additional information specific to derivative instruments is disclosed in Note 4 - Derivative Contracts and Note 5 - Fair Value Measurements.

Securities Lending

PBGC participates in a securities lending program administered by its custodian bank whereby the custodian bank lends PBGC's securities to third parties. The custodian bank requires initial collateral from the borrower that equals 102 percent to 105 percent of the securities lent. Collateral consisting of cash and non-cash instruments is held by the custodian bank. The custodian bank either requires additional collateral or returns collateral to cover daily market value changes. The margin call for additional collateral occurs when levels fall below the initial collateral requirement, except for U.S. Government securities and sovereign debt issued by non-U.S. Governments where the margin call may not occur until collateral held falls below certain levels depending upon the composition of collateral but never lower than 100 percent of the securities lent. Any cash collateral received is invested.

The total value of securities on loan at September 30, 2012, and September 30, 2011, was $4.298 billion and $6.125 billion, respectively. The decrease in loan balances was mainly attributable to decreased utilization of PBGC's U.S. Government Securities due to lower demand. In addition, low yields made lending U.S. Government securities less attractive.

U.S. Government securities continue to represent PBGC's largest amount of assets on loan. The FY 2012 year-end lendable balance for U.S. Government securities was approximately $7.0 billion or 54 percent of PBGC's overall lendable securities balance; while the September 30, 2011 balance for U.S. Government securities was approximately $8.2 billion or 33 percent of PBGC's overall lendable security balance. Of the $4.298 billion market value of securities on loan at September 30, 2012, approximately 54 percent are lent U.S. Government securities. Utilization levels of U.S. Government securities, U.S. corporate bonds and U.S. equities on September 30, 2012 were lower than a year earlier, but was partially offset by the increased loan balances of U.S. corporate bonds and U.S. equities.

The amount of cash collateral received for these loaned securities was $3.425 billion at September 30, 2012, and $4.587 billion at September 30, 2011. These amounts are recorded as assets and are offset with a corresponding liability. For lending agreements collateralized by securities, no accompanying asset or liability is recorded, as PBGC does not sell or re-pledge the associated collateral. For those securities lending activities that PBGC directs through its custodian manager, the corporation chooses to invest proceeds from securities lending in the Quality A cash collateral pool.

PBGC earned $19.1 million from its securities lending programs as of September 30, 2012. Also contributing to PBGC's securities lending income is its participation in certain pooled index funds. Net income from securities lending is included in "Investment income – Fixed" on the Statements of Operations and Changes in Net Position. As of September 30, 2012, PBGC loaned out $4.298 billion in securities of approximately $26.959 billion of securities available for securities lending.

PBGC does not have the right by contract or custom to sell or re-pledge non-cash collateral; it is no longer reported on the Statements of Financial Condition. Non-cash collateral, which consists primarily of U.S. Treasuries, has recently increased to material levels.

Repurchase Agreements

PBGC's repurchase agreements entitle and obligate PBGC to repurchase or redeem the same or substantially the same securities that were previously transferred as collateralized securities. In addition, its repurchase agreements require PBGC to redeem the collateralized securities, before maturity at a fixed determinable price.

As of September 30, 2012, PBGC had $36 million in Repurchase Agreements. This amount represents maturities of one day and is reported as an asset and included in the "Cash and cash equivalents" balance. There was no associated liability for these secured borrowings reported as "Securities sold under repurchase agreements." PBGC has no restrictions placed on the cash received for all of its outstanding repurchase agreements as of September 30, 2012.

Note 4: Derivative Contracts

PBGC's derivative financial instruments are recorded at fair value and are included on the Statements of Financial Condition as investments and derivative contracts. Foreign exchange forwards are included in "Fixed maturity securities". Swaps are netted for the individual contracts as "Receivables, net – Derivative contracts" and "Derivative contracts" (liabilities). Bond forwards and TBAs are reclassified as "Receivables, net – Sale of securities" and "Due for purchases of securities" from derivative contracts receivables and payables.

Amounts in the table below represent the derivative contracts in a receivable position at financial statement date. Collateral deposits of $79 million, which represent cash paid as collateral on certain derivative contracts, are shown.

DERIVATIVE CONTRACTS

(Dollars in millions)	**September 30, 2012**	September 30, 2011
Open receivable trades on derivatives:		
Collateral deposits	**$79**	$81
Futures contracts	**4**	90
Interest rate swaps	**0**	0
Credit default swaps	**0**	7
Total	**$83**	$178

Amounts in the Derivative Contracts table below represent derivative contracts in a payable position at financial statement date which PBGC reflects as a liability. Collateral deposits of $72 million, which represent cash received as collateral on certain derivative contracts, are included.

DERIVATIVE CONTRACTS

(Dollars in millions)	**September 30, 2012**	September 30, 2011
Open payable trades on derivatives:		
Collateral deposits	**$72**	$167
Futures contracts	**9**	2
Interest rate swaps	**0**	0
Credit default swaps	**2**	0
Options-fixed income	**11**	4
Total	**$94**	$173

Note 5: Fair Value Measurements

Effective January 1, 2009, PBGC adopted the provisions of the FASB Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures*. The standard does not require the measurement of financial assets and liabilities at fair value, but provides a consistent definition of fair value and establishes a framework for measuring fair value in accordance with U.S. GAAP. The standard is intended to increase consistency and comparability in, and disclosures about, fair value measurements, by providing users with better information about the extent to which fair value is used to measure financial assets and liabilities, the inputs used to develop those measurements and the effect of the measurements, if any, on financial condition, results of operations, liquidity and capital.

Section 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an "exit price") in the principal or most advantageous market for an asset or liability in an orderly transaction between market participants on the measurement date. When PBGC measures fair value for its financial assets and liabilities, PBGC considers the principal or most advantageous market in which PBGC would transact, and PBGC considers assumptions that market participants would use when pricing the asset or liability. When possible, PBGC looks to active and observable markets to measure the fair value of identical, or similar, financial assets or liabilities. When identical financial assets and liabilities are not traded in active markets, PBGC looks to market observable data for similar assets and liabilities. In some instances, certain assets and liabilities are not actively traded in observable markets, and as a result PBGC uses alternative valuation techniques to measure their fair value.

In addition, Section 820 establishes a hierarchy for measuring fair value. The fair value hierarchy is based on the observability of inputs to the valuation of a financial asset or liability as of the measurement date. The standard requires the recognition of trading gains or losses related to certain derivative transactions whose fair value has been determined using unobservable market inputs.

PBGC believes that its valuation techniques and underlying assumptions used to measure fair value conform to the provisions of Section 820. PBGC has categorized the financial assets and liabilities that it carries at fair value in the Statements of Financial Condition based upon the standard's valuation hierarchy. The hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1); next highest priority to pricing methods with significant observable market inputs (Level 2); and the lowest priority to significant unobservable valuation inputs (Level 3).

If the inputs used to measure a financial asset or liability cross different levels of the hierarchy, categorization is based on the lowest level input that is significant to the fair value measurement. Management's assessment of the significance of a particular input to the overall fair value measurement of a financial asset or liability requires judgment, and considers factors specific to that asset or liability.

The three levels are described below:

Level 1 - Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market. PBGC's Level 1 investments primarily included are exchange-traded equity securities and certain U.S. Government securities.

Level 2 - Financial assets and liabilities whose values are based on quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability. Level 2 inputs to the valuation methodology include the following:

a. Quoted prices for similar assets or liabilities in active markets – included are cash equivalents, securities lending collateral, U.S. Government securities, asset backed securities, fixed foreign investments, corporate bonds, repos, bond forwards, and swaps;

b. Quoted prices for identical or similar assets or liabilities in non-active markets – included are corporate stock, pooled funds fixed income, pooled funds equity, and foreign investments equity;

c. Pricing models whose inputs are observable for substantially the full term of the asset or liability – included are insurance contracts and bank loans; and

d. Pricing models whose inputs are derived principally from or corroborated by observable market information through correlation or other means for substantially the full term of the asset or liability.

Level 3 - Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable in the market and significant to the overall fair value measurement. These inputs reflect management's judgment about the assumptions that a market participant would use in pricing the asset or liability, and based on the best available information. The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. We include instruments whose values are based on a single source such as a broker, pricing service, or dealer which cannot be corroborated by recent market transactions. These include fixed maturity securities such as corporate bonds that are comprised of securities that are no longer traded on the active market and/or not managed by any asset manager. Equity securities such as corporate stocks are also included in this level, and are comprised of securities that are no longer traded on the active market and/or not managed by any asset manager. Private equity, real estate funds, and separate accounts that invest primarily in U.S. commercial real estate, are valued based on each underlying investment within the fund/account incorporating valuations that consider the evaluation of financing and sale transactions with third parties, expected cash flows and market-based information, including comparable transactions, and performance multiples, among other factors.

The assets and liabilities that PBGC carries at fair value are summarized by the three levels required by Section 820 in the following table. The fair value of the asset or liability represents the price that would be received to sell the asset or paid to transfer the liability (an exit price).

FAIR VALUE MEASUREMENTS ON A RECURRING BASIS AS OF SEPTEMBER 30, 2012

(Dollars in millions)	Quoted Market Prices in Active Markets (Level 1)	Pricing Methods with Significant Observable Market Inputs (Level 2)	Pricing Methods with Significant Unobservable Market Inputs (Level 3)	Total Net Carrying Value in Statements of Financial Condition
Assets				
Cash and cash equivalents	$ 425	$ 3,367		$ 3,792
Securities lending collateral		3,425		3,425
Investments:				
Fixed maturity securities				
U.S. Government securities		25,396		
Commercial paper/securities purchased under resale agreements		442		
Asset backed/Mortgage backed securities		3,509		
Pooled funds				
Domestic		131	277	
International				
Global/other				
Corporate bonds and other	2	11,071		
International securities	(12)	9,127		
Total fixed maturity securities	(10)	49,676	277	49,943
Equity securities:				
Domestic	2,240	170	7	
International	668	2		
Pooled funds				
Domestic	7	10,791		
International	2	8,731		
Global/other	1	-	0 ***	
Total equity securities	2,918	19,694	7	22,619
Private equity			1,339	1,339
Real estate and real estate investment trusts	2	1	508	511
Insurance contracts and other Investments		75	2	77
Receivables:				
Derivative contracts*	4	79		83
Liabilities				
Payables:				
Derivative contracts**	20	74		94

* Derivative contracts receivables are comprised of open receivable trades on futures, swaps, and collateral deposits. See the Derivative Contracts table under Note 4.

** Derivative contracts payables are comprised of open payable trades on futures, swaps, options, and collateral deposits. See the Derivative Contracts table under Note 4.

*** Less than $500,000.

As of September 30, 2012, there were no significant transfers between Level 1 and Level 2. The end of the reporting period is the date used to recognize transfers between levels.

CHANGES IN LEVEL 3 ASSETS AND LIABILITIES MEASURED AT FAIR VALUE ON A RECURRING BASIS FOR THE YEAR ENDED SEPTEMBER 30, 2012

(Dollars in millions)	Fair Value at September 30, 2011	Total Realized and Unrealized Gains (Losses) included in Income	Purchases	Sales	Transfers Into Level 3	Transfers Out of Level 3	Fair Value at September 30, 2012	Change in Unrealized Gains (Losses) Related to Financial Instruments held at September 30, 2012 **
Assets:								
Pooled funds (fixed)	$ 343	$(66)					$ 277	$ (66)
Corporate bonds and other *	0***	0***	0***	0***			0***	0***
Domestic/Int'l equity *	9	0***	1	(3)			7	0***
Private equity	1,459	(66)	12	(66)			1,339	(66)
Real estate & real estate investment trusts	523	(24)	9	0***			508	(24)
Other *	0				2		2	

*Assets which are not actively traded in the market place.

** Amounts included in this column solely represent unrealized gains and losses and cannot be derived from other columns in this table.

*** Less than $500,000.

Pursuant to FASB Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures – Investments in Certain Entities That Calculate Net Asset Value per Share;* additional disclosures for Investments priced at Net Asset Value are discussed below.

INVESTMENTS IN CERTAIN ENTITIES THAT CALCULATE NET ASSET VALUE PER SHARE (OR ITS EQUIVALENT) FOR THE YEAR ENDED SEPTEMBER 30, 2012

	Fair Value (in millions)	Unfunded Commitments [1]	Redemption Frequency (If Currently Eligible)	Redemption Notice Period
Real estate (a)	$ 511	$118	n/a	n/a
Private equity (b)	1,339	304	n/a	n/a
Pooled funds (c)	11,206	0	n/a	n/a
Total	$ 13,056	$422		

[1] Unfunded amounts include recallable distributions. A substantial portion of the unfunded commitments is unlikely to be called.

a. This class includes 157 real estate investments that invest primarily in U.S. commercial real estate, and to a lesser extent, U.S. residential real estate. The fair value of each individual investment in this class has been estimated using the net asset value of the PBGC's ownership interest in partners' capital. Generally, these investments do not have redemption provisions. Distributions from each fund will be received as the underlying assets of the fund will be liquidated over the next ten years or so. In addition, distributions will also include any periodic income distributions received. No fund investments in this class are planned to be sold. Individual portfolio investments will be sold over time, however, those have not yet been determined.

b. This class includes 617 private market investments that invest primarily in U.S. buyout and U.S. venture capital funds. A small number of those focus on natural resources. These investments do not have redemption provisions. Instead, the nature of the investments in this class is that distributions are received through the liquidation of the underlying assets of the funds. If these investments were held, it is estimated that the underlying assets of the fund would be liquidated over the next twelve years. However, the individual investments that will be sold have not yet been determined. The fair value of each individual investment has been estimated using the net asset value of the PBGC's ownership interest in partners' capital.

c. This class includes investments in unit trusts that are intended to match returns of domestic and international indices. Units reflect a pro-rata share of the fund's investments. The per unit net asset value is determined each business day based on the fair value of the fund's investments. Issuances and redemptions are possible daily when a per unit value is determined and are based upon the closing per unit net asset value.

PBGC uses recent prices of group annuities to derive the interest factors used to calculate the present value of future benefit-payment obligations. PBGC determines the interest-factor set that, when combined with a specified mortality table, produces present values that approximate the prices private insurers would charge to annuitize the same benefit-payment obligations. Based on this valuation and in accordance with the provisions of the FASB Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures*, the significant unobservable inputs for the liability is the interest rate risk for Level 3 fair value measurements. A change in interest factors has an impact to the calculation of PBGC's present value of future benefits (PVFB). The table below summarizes the hypothetical results of using a 100 basis point difference causing the PVFB liability to increase (decrease) with a corresponding decrease (increase) in the interest rates.

Hypothetical and Actual Interest Rate Sensitivity Calculations of PVFB
Single-Employer Trusteed Plans and the Multiemployer Program*

September 30, 2012 *(Dollars in millions)*	**Hypothetical Rates 2.28% for 25 years, 1.97% thereafter**	**Actual Rates** 3.28% for 25 years, 2.97% thereafter**	**Hypothetical Rates 4.28% for 25 years, 3.97% thereafter**
Single-Employer Program	$115,759	**$103,126**	$92,712
Multiemployer Program	8,063	**7,010**	6,126
Total	$123,822	**$110,136**	$98,838

*Level 3 Fair Value Measurements
**Actual rates and PVFB amounts calculated for September 30, 2012 quarterly financial statements.

Note 6: Present Value of Future Benefits

The following table summarizes the actuarial adjustments, charges and credits that explain how the Corporation's single-employer program liability for the present value of future benefits changed for the years ended September 30, 2012 and for the fiscal year ended September 30, 2011.

For FY 2012, PBGC used a 25 year select interest factor of 3.28% followed by an ultimate factor of 2.97% for the remaining years. In FY 2011, PBGC used a 20-year select interest factor of 4.31% followed by an ultimate factor of 4.26% for the remaining years. These factors were determined to be those needed, given the mortality assumptions, to continue to match the survey of annuity prices provided by the American Council of Life Insurers (ACLI). Both the interest factor and the length of the select period may vary to produce the best fit with these prices. The prices reflect rates at which, in the opinion of management, the liabilities (net of administrative expenses) could be settled in the market at September 30, for the respective year, for single-premium nonparticipating group annuities issued by private insurers. Many factors, including Federal Reserve policy, changing expectations about longevity risk, and competitive market conditions may affect these rates.

For FY 2012, PBGC used the Retirement Plan-2000 Combined Healthy (RP-2000 CH) Male and Female Tables, each set back one year and projected 22 years to 2022 using Scale AA. For September 30, 2011, PBGC used the same table, set back one year and projected 21 years to 2021 using Scale AA. The number of years that PBGC projects the mortality table reflects the number of years from the 2000 base year of the table to the end of the fiscal year (12 years in FY 2012, 11 years in FY 2011) plus PBGC's calculated duration of its liabilities (10 years in FY 2012 and FY 2011).

PBGC continues to utilize the results of its 2011 mortality study. The study showed that the mortality assumptions used in FY 2010 reflected higher mortality than was realized in PBGC's seriatim population. Therefore, PBGC adopted a base mortality table (i.e. RP-2000 CH set back one year instead of GAM94 set forward one year) that better reflects past mortality experience. The study also recommended changes in the mortality assumptions for disabled lives that PBGC implemented in the June 30, 2011 and subsequent valuations. The ACLI survey of annuity prices, when combined with the mortality table, provides the basis for determining the interest factors used in calculating the PVFB. The insurance company prices, when combined with the stronger mortality table, results in a higher interest factor.

The expense reserve factor for administrative expenses beginning with the FY 2007 valuation is 1.37 percent plus additional reserves for cases in which plan asset determinations, participant database audits and actuarial valuations were not yet complete. In addition to the completion of these milestones, PBGC continues to base the reserve on case size, number of participants and time since trusteeship.

The present values of future benefits for trusteed multiemployer plans for FY 2012 and FY 2011 reflect the payment of benefits and the changes in interest and mortality assumptions, expected interest and the effect of experience.

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

RECONCILIATION OF THE PRESENT VALUE OF FUTURE BENEFITS FOR THE YEARS ENDED SEPTEMBER 30, 2012 AND 2011

	September 30,			
(Dollars in millions)		**2012**		2011
Present value of future benefits, at beginning of year -- Single-Employer, net		**$ 92,953**		$90,022
Estimated recoveries, prior year		**205**		107
Assets of terminated plans pending trusteeship, net, prior year		**280**		542
Present value of future benefits at beginning of year, gross		**93,438**		90,671
Settlements and judgments, prior year		**(56)**		(55)
Net claims for probable terminations, prior year		**(833)**		(1,445)
Actuarial adjustments -- underwriting:				
Changes in method and assumptions	**$ 76**		$1,881	
Effect of experience	**153**		(209)	
Total actuarial adjustments -- underwriting	**229**		1,672	
Actuarial charges -- financial:				
Expected interest	**3,927**		3,880	
Change in interest rates	**10,718**		1,009	
Total actuarial charges -- financial	**14,645**		4,889	
Total actuarial charges, current year		**14,874**		6,561
Terminations:				
Current year	**2,035**		2,363	
Changes in prior year	**(16)**		(206)	
Total terminations		**2,019**		2,157
Benefit payments, current year*		**(5,384)**		(5,340)
Estimated recoveries, current year**		**(243)**		(205)
Assets of terminated plans pending trusteeship, net, current year		**(271)**		(280)
Settlements and judgments, current year		**56**		56
Net claims for probable terminations:				
Future benefits***	**7,686**		1,379	
Estimated plan assets and recoveries from sponsors	**(5,651)**		(546)	
Total net claims, current year		**2,035**		833
Present value of future benefits, at end of year -- Single-Employer, net		**105,635**		92,953
Present value of future benefits, at end of year -- Multiemployer		**1**		1
Total present value of future benefits, at end of year, net		**$105,636**		$92,954

* The benefit payments of $5,384 million and $5,340 million include $51 million in FY 2012 and $(42) million in FY 2011 for benefits paid from plan assets by plans prior to trusteeship.

**United Continental Holdings, Inc. (UAL) is obligated under an indenture to issue to PBGC up to $500 million aggregate principal amount of 8% Contingent Senior Notes (8% Notes) in up to eight equal tranches of $62.5 million if certain UAL earnings related triggering events occur. As of September 30, 2012, UAL issued two tranches of $62.5 million of the 8% Notes.

*** The future benefits for probable terminations of $7,686 million and $1,379 million for fiscal years 2012 and 2011, respectively, include $299 million and $288 million, respectively, for probable terminations not specifically identified and $7,387 million and $1,091 million, respectively, for specifically identified probables.

The following table details the assets that make up single-employer terminated plans pending termination and trusteeship:

ASSETS OF SINGLE-EMPLOYER PLANS PENDING TERMINATION AND TRUSTEESHIP, NET

	September 30, 2012		September 30, 2011	
(Dollars in millions)	**Basis**	**Market Value**	Basis	Market Value
U.S. Government securities	**$ 0**	**$ 0**	$ 0	$ 0
Corporate and other bonds	**108**	**109**	148	148
Equity securities	**164**	**170**	137	139
Private equity	**0**	**0**	0	0
Insurance contracts	**0** *	**0** *	7	7
Other	**(8)**	**(8)**	(19)	(14)
Total, net	**$264**	**$271**	$273	$280

* less than $500,000

Net Claims for Probable Terminations

Factors that are presently not fully determinable may be responsible for these claim estimates differing from actual experience. Included in net claims for probable terminations is a provision for future benefit liabilities for plans not specifically identified.

The values recorded in the following reconciliation table have been adjusted to the expected dates of termination.

RECONCILIATION OF NET CLAIMS FOR PROBABLE TERMINATIONS

	September 30,			
(Dollars in millions)	**2012**		2011	
Net claims for probable terminations, at beginning of year		**$ 833**		$1,445
New claims	**$ 1,736**		$ 545	
Actual terminations	**(150)**		(474)	
Deleted probables	**(394)**		(718)	
Change in benefit liabilities	**10**		35	
Change in plan assets	**0**		0	
Loss (credit) on probables		**1,202**		(612)
Net claims for probable terminations, at end of year		**$ 2,035**		$ 833

The following table itemizes the single-employer probable exposure by industry:

PROBABLES EXPOSURE BY INDUSTRY (PRINCIPAL CATEGORIES)

(Dollars in millions)	**FY 2012**	FY 2011
Manufacturing	**$ 1,900**	$ -
Health Care	**135**	231
Wholesale and Retail Services	**-**	602
Services	**-**	-
Total	**$ 2,035**	$833

For further detail, see Note 2 subpoint (4).

The following table shows what has happened to plans classified as probables. This table does not capture or include those plans that were not previously classified as probable before they terminated.

ACTUAL PROBABLES EXPERIENCE

As Initially Recorded Beginning in 1987

(Dollars in millions)	Status of Probables from 1987-2011 at September 30, 2012			
Beginning in 1987, number of plans reported as Probable:	Number of Plans	Percent of Plans	Net Claim	Percent of Net Claim
Probables terminated	364	79%	$28,622	73%
Probables not yet terminated or deleted	0	0	0	0
Probables deleted	98	21	10,729	27
Total	462	100%	$39,351	100%

Note 7: Multiemployer Financial Assistance

PBGC provides financial assistance to multiemployer defined benefit pension plans in the form of loans. Since these loans are not generally repaid, an allowance is set up to the extent that repayment of these loans is not expected.

NOTES RECEIVABLE MULTIEMPLOYER FINANCIAL ASSISTANCE

(Dollars in millions)	**September 30, 2012**	September 30, 2011
Gross balance at beginning of year	**$599**	$484
Financial assistance payments - current year	**95**	115
Write-offs related to settlement agreements	**0**	0
Subtotal	**694**	599
Allowance for uncollectible amounts	**(694)**	(599)
Net balance at end of year	**$ 0**	$ 0

The losses from financial assistance and probable financial assistance are reflected in the Statements of Operations and Changes in Net Position include period changes in the estimated present value of nonrecoverable future financial assistance. The losses from financial assistance are presented as actuarial charges, credits, and adjustments for plans that are known to be insolvent as of the valuation date and/or have or about to begin receiving financial assistance. In addition, a change in the valuation of the liability due to new data received (e.g., new plan expenses, more recent valuation liabilities, and new withdrawal payment schedules) is included as financial assistance from insolvent and probable plans on the Statements of Operations and Changes in Net Position. This valuation data change is a separate line item from actuarial adjustments and actuarial charges.

As of September 30, 2012, the corporation expects 148 multiemployer plans will exhaust plan assets and need financial assistance from PBGC to pay guaranteed benefits and plan administrative expenses. The present value of nonrecoverable future financial assistance for these 148 plans is $7.010 billion. The 148 plans fall into three categories: (1) plans currently receiving financial assistance; (2) plans that have terminated but have not yet started receiving financial assistance from PBGC; and (3) ongoing plans (not terminated) that the corporation expects will require financial assistance in the future. The latter two categories are comprised of multiemployer probables as defined by the following classification criteria:

- Probable insolvent plan-terminated future probables – A plan that may still have assets but the combination of plan assets and collectible payments of withdrawal liability are projected to be insufficient to cover plan benefits plus expenses.
- Probable insolvent plan-ongoing future probables – An ongoing plan with a projected date of insolvency within 10 years.

MULTIEMPLOYER FINANCIAL ASSISTANCE

(Dollars in millions)	**September 30, 2012** Number of Plans	**September 30, 2012** Net Liability	September 30, 2011 Number of Plans	September 30, 2011 Net Liability
Plans currently receiving financial assistance	**41**	**$1,388**	41	$1,232
Plans that have terminated but have not yet started receiving financial assistance	**61**	**1,725**	60	1,487
Ongoing plans (not terminated) that the corporation expects will require financial assistance in the future	**46**	**3,897**	34	1,756
Total	**148**	**$7,010**	135	$4,475

Of the 148 plans:

1) 41 have exhausted plan assets and are currently receiving financial assistance payments from PBGC. The present value of future financial assistance payments for these insolvent 41 plans is $1.388 billion.

2) 61 plans have terminated but have not yet started receiving financial assistance payments from PBGC. Terminated multiemployer plans no longer have employers making regular contributions for covered work, though some plans continue to receive withdrawal liability payments from withdrawn employers. In general, PBGC records a loss for future financial assistance for any underfunded multiemployer plan that has terminated. The present value of future financial assistance payments to these 61 terminated plans is $1.725 billion.

3) 46 plans are ongoing (i.e., have not terminated), but PBGC expects these plans will exhaust plan assets and need financial assistance within 10 years. In this analysis, PBGC takes into account the current plan assets, future income to the plan, the statutory funding rules, and the possibility for future increases in contributions. The present value of future financial assistance payments for these 46 ongoing plans is $3.897 billion.

PRESENT VALUE OF NONRECOVERABLE FUTURE FINANCIAL ASSISTANCE AND LOSSES FROM FINANCIAL ASSISTANCE

(Dollars in millions)	**September 30, 2012**	September 30, 2011
Balance at beginning of year	**$4,475**	$3,030
Changes in allowance:		
Losses from insolvent and probable plans - financial assistance	**2,466**	1,461
Actuarial adjustments	**(6)**	37
Actuarial charges (credits):		
Due to expected interest	**54**	52
Due to change in interest rates	**116**	10
Financial assistance granted (previously accrued)	**(95)**	(115)
Balance at end of period	**$7,010**	$4,475

In the table above, actuarial charges are reported separately from Losses from insolvent and probable plans-financial assistance. As a result, the table includes the following new lines: Actuarial adjustments, Due to expected interest, and Due to change in interest rates. Insolvent plans are presented within these three new actuarial charges (credits) lines. Losses from insolvent and probable plans-financial assistance include plans that terminated but have not yet received financial assistance, ongoing plans that PBGC expects will require financial assistance in the future, and those insolvent plans that have a change in liability due to new plan data included in the valuation.

Note 8: Accounts Payable and Accrued Expenses

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

ACCOUNTS PAYABLE AND ACCRUED EXPENSES

(Dollars in millions)	**September 30, 2012**	September 30, 2011
Annual leave	**$ 9**	$ 8
Other payables and accrued expenses	**70**	62
Accounts payable and accrued expenses	**$ 79**	$ 70

Note 9: Reasonably Possible Contingencies

Single-Employer Plans

Single-employer plans sponsored by companies whose credit quality is below investment grade pose a greater risk of being terminated. The estimated unfunded vested benefits exposure amounts disclosed below represent the Corporation's estimates of the reasonably possible exposure to loss given the inherent uncertainties about these plans. In rare circumstances for certain large companies, the reasonably possible exposure calculation reflects the estimated unfunded guaranteed benefit determination rather than the estimated unfunded vested benefit determination.

In accordance with the FASB Accounting Standards Codification Section 450, *Contingencies*, PBGC classified a number of these companies as reasonably possible rather than probable terminations as the sponsors' financial condition and other factors did not indicate that termination of their plans was likely. This classification was done based upon information about the companies as of September 30, 2012. The following standard criteria for a single-employer plan sponsor to be classified as Reasonably Possible are as follows:

a. The sponsor(s) or significant member(s) of its controlled group (e.g., a parent or major subsidiary) is in reorganization under Title 11 of the United States code.

b. An application for a funding waiver is pending or outstanding with the IRS.

c. A minimum funding contribution has been missed.

d. The sponsor(s) has an S&P senior unsecured credit rating or an issuer credit rating less two notches of BB+ or below, or a Moody's senior unsecured credit rating or a corporate family rating less one notch of Ba1 or below. If the controlled group is not rated by Moody's and S&P, PBGC will use the Dun & Bradstreet Financial Stress Score (if available) to classify the controlled group as Reasonably Possible or Remote.

e. The sponsor(s) has no bond rating, but analysis indicates that its unsecured debt would be below investment grade.

f. The sponsor(s) meet at least one of the PBGC "high risk" criteria.

g. Other (detailed explanation must be provided and be approved by PBGC's Contingency Working Group).

The estimate of unfunded vested benefits exposure to loss for the single-employer plans of these companies was measured as of December 31, 2011. The reasonably possible exposure to loss in these plans was $295 billion for FY 2012. This is an increase of $68 billion from the reasonably possible exposure of $227 billion in FY 2011. This reasonably possible exposure increased primarily due to the decrease in the interest rate used for valuing liabilities and low asset returns for calendar year 2011.

Except in rare circumstances as indicated earlier in this footnote, the estimate of unfunded vested benefits exposure to loss is not generally based on PBGC-guaranteed benefit levels, since data is not available to determine an estimate at this level of precision. PBGC calculated this estimate, as in previous years, by using the most recent data available from filings and submissions to the Corporation for plan years ended on or after December 31, 2010. The Corporation adjusted the value reported for liabilities to December 31, 2011, using a select rate of 3.08% for the first 20 years and 3.37% thereafter and applying the expense load as defined in 29 CFR Part 4044, Appendix C. The rates were derived in conjunction with the 1994 Group Annuity Mortality Static Table (with margins) projected to 2021 using Scale AA to approximate annuity prices as of December 31, 2011. The underfunding associated with these plans could be substantially different at September 30, 2012, because of the economic conditions that changed between December 31, 2011 and September 30, 2012. The Corporation did not adjust the estimate for events that occurred between December 31, 2011, and September 30, 2012.

The following table by industry itemizes the single-employer reasonably possible exposure to loss:

REASONABLY POSSIBLE EXPOSURE TO LOSS BY INDUSTRY (PRINCIPAL CATEGORIES)

(Dollars in millions)	**FY 2012**	FY 2011
Manufacturing *	**$155,857**	$120,690
Transportation, Communication and Utilities **	**67,355**	50,133
Services	**29,795**	25,879
Wholesale and Retail Trade	**17,199**	12,218
Health Care	**12,089**	8,818
Finance, Insurance, and Real Estate	**8,463**	5,953
Agriculture, Mining, and Construction	**4,205**	3,426
Total	**$294,963**	$227,117

* Primarily automobile/auto parts and primary and fabricated metals

** Primarily airline

Multiemployer Plans

There are some multiemployer plans that may require future financial assistance. PBGC included amounts in the liability for the present value of nonrecoverable future financial assistance (See Note 7) for multiemployer plans that PBGC estimated may require future financial assistance. In addition, PBGC estimated as of September 30, 2012, that it is reasonably possible that other multiemployer plans may require future financial assistance in the amount of $27 billion.

The Corporation calculated the future financial assistance liability for each multiemployer plan identified as probable (see Note 7), or reasonably possible as the present value of guaranteed future benefit and expense payments net of any future contributions or withdrawal liability payments as of the later of September 30, 2012, or the projected (or actual, if known) date of plan insolvency, discounted back to September 30, 2012. The Corporation's identification of plans that are likely to require such assistance and estimation of related amounts required consideration of many complex factors, such as an estimate of future cash flows, future mortality rates, and age of participants not in pay status. These factors are affected by future events, including actions by plans and their sponsors, most of which are beyond the Corporation's control. Reasonably possible multiemployer classification is defined as an ongoing plan with a projected insolvency date between 10 and 20 years from the valuation date.

Note 10: Commitments

PBGC leases its office facility under a commitment that began on January 1, 2005, and expires December 10, 2018. This lease provides for periodic rate increases based on increases in operating costs and real estate taxes over a base amount. In addition, PBGC is leasing space for field benefit administrators. These leases began in 1996 and expire in 2017. The minimum future lease payments for office facilities having noncancellable terms in excess of one year as of September 30, 2012, are as follows:

COMMITMENTS: FUTURE LEASE PAYMENTS

(Dollars in millions)	
Years Ending September 30,	Operating Leases
2013	$ 18.9
2014	18.5
2015	18.3
2016	18.0
2017	17.9
Thereafter	39.8
Minimum lease payments	$131.4

Lease expenses were $17.6 million in FY 2012 and $18.3 million in FY 2011.

Note 11: Premiums

For both the single-employer and multiemployer programs, ERISA provides that PBGC shall continue to guarantee basic benefits despite the failure of a plan administrator to pay premiums when due. PBGC assesses interest and penalties on the unpaid portion of or underpayment of premiums. Interest continues to accrue until the premium and the interest due are paid. For plan years 2012 and 2011, the flat-rate premiums for single-employer pension plans were $35 per participant and for multiemployer plans, $9 per participant. PBGC recorded net premium income of $2.734 billion that consisted primarily of $1.215 billion in flat-rate premiums, $1.495 billion in variable-rate premiums, and $0.033 billion in termination premiums, offset by a bad debt expense of $0.014 billion. Bad debt expenses include a reserve for uncollectible premium receivables (including flat, variable, and termination premiums), interest, and penalties. Net premium income for FY 2011 was $2.164 billion and consisted primarily of approximately $1.235 billion in flat-rate premiums, $0.929 billion in variable-rate premiums, and $0.202 billion in termination premiums, offset by a bad debt expense of $0.207 billion. The termination premium applies to certain plan terminations occurring after 2005. If a pension plan terminates in a distress termination pursuant to ERISA section 4041(c)(2)(B)(ii) or (iii), or in a PBGC-initiated termination under ERISA section 4042, the plan sponsor and its controlled group are liable to PBGC for a termination premium at the rate of $1,250 per plan participant per year for three years.

The following table presents a year-to-year comparison of key premium information.

PREMIUMS

(Dollars in millions)	September 30, 2012	September 30, 2011
Flat Rate Premium:		
Single-Employer	**$1,123**	$1,143
Multiemployer	**92**	92
Total Flat Rate Premium	**1,215**	1,235
Variable Rate Premium	**1,495**	929
Interest and Penalty Income	**5**	5
Termination Premium	**33**	202
Less Changes in the Allowance Reserve for Bad Debts for Interest, Penalties, and Premiums	**(14)**	(207)
Total	**$2,734**	$2,164
Single-Employer	**$2,623**	$2,077
Termination Premium	**33**	202
Less Changes in the Allowance Reserve for Bad Debts for Interest, Penalties, and Premiums	**(14)**	(207)
Total Single-Employer	**2,642**	2,072
Multiemployer	**92**	92
Less Changes in the Allowance Reserve for Bad Debts for Interest and Penalties	**0***	0*
Total Multiemployer	**92**	92
Total	**$2,734**	$2,164

* less than $500,000

Note 12: Losses from Completed and Probable Terminations

Amounts reported as losses are the present value of future benefits less related plan assets and the present value of expected recoveries from sponsors. The following table details the components that make up the losses:

LOSSES FROM COMPLETED AND PROBABLE TERMINATIONS
SINGLE-EMPLOYER PROGRAM

	For the Years Ended September 30,					
	2012			2011		
(Dollars in millions)	**New Terminations**	**Changes in Prior Year Terminations**	**Total**	New Terminations	Changes in Prior Year Terminations	Total
Present value of future benefits	**$2,035**	**$ (16)**	**$2,019**	$ 2,363	$ (206)	$2,157
Less plan assets	**1,027**	**228**	**1,255**	1,173	175	1,348
Plan asset insufficiency	**1,008**	**(244)**	**764**	1,190	(381)	809
Less estimated recoveries	**0**	**(39)**	**(39)**	0	(3)	(3)
Subtotal	**1,008[1]**	**(205)**	**803**	1,190[1]	(378)	812
Settlements and judgments		**1**	**1**		1	1
Loss (credit) on probables	**(150)[2]**	**1,352[3]**	**1,202[4]**	(474)[2]	(138)[3]	(612)[4]
Total	**$ 858**	**$1,148**	**$2,006**	$ 716	$(515)	$ 201

[1] Gross amounts for plans terminated during the period, including plans previously recorded as probables.
[2] Net claims for plans previously recorded as probables that terminated.
[3] Includes changes to old and new probables.
[4] See Note 6 - includes $150 million at September 30, 2012, and $474 million at September 30, 2011, previously recorded relating to plans that terminated during the period ("Actual terminations").

Note 13: Financial Income

The following table details the combined financial income by type of investment for both the single-employer and multiemployer programs:

INVESTMENT INCOME SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS

(Dollars in millions)	**Single-Employer Program Sept. 30, 2012**	**Multiemployer Program Sept. 30, 2012**	**Memorandum Total Sept. 30, 2012**	Single-Employer Program Sept. 30, 2011	Multiemployer Program Sept. 30, 2011	Memorandum Total Sept. 30, 2011
Fixed maturity securities:						
Interest earned	**$1,800**	**$44**	**$1,844**	$1,796	$57	$1,853
Realized gain	**2,005**	**36**	**2,041**	973	31	1,004
Unrealized gain	**894**	**11**	**905**	733	60	793
Total fixed maturity securities	**4,699**	**91**	**4,790**	3,502	148	3,650
Equity securities:						
Dividends earned	**66**	**0**	**66**	67	0	67
Realized gain	**1,385**	**0**	**1,385**	2,857	0	2,857
Unrealized gain (loss)	**2,622**	**0**	**2,622**	(3,200)	0	(3,200)
Total equity securities	**4,073**	**0**	**4,073**	(276)	0	(276)
Private equity:						
Distributions earned	**27**	**0**	**27**	27	0	27
Realized gain (loss)	**81**	**0**	**81**	(9)	0	(9)
Unrealized gain	**(66)**	**0**	**(66)**	126	0	126
Total private equity	**42**	**0**	**42**	144	0	144
Other income (loss)	**(22)**	**0**	**(22)**	76	0	76
Total investment income	**$8,792**	**$91**	**$8,883**	$3,446	$148	$3,594

Note 14: Employee Benefit Plans

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

The Corporation's contribution to the CSRS plan for both FY 2012 and FY 2011 was 7.0 percent of base pay for those employees covered by that system. For those employees covered by FERS, the Corporation's contribution was 11.7 percent of base pay for FY 2012, increased from 11.2 percent for FY 2011. In addition, for FERS-covered employees, PBGC automatically contributes one percent of base pay to the employee's Thrift Savings account, matches the first three percent contributed by the employee and matches one-half of the next two percent contributed by the employee. Total retirement plan expenses amounted to $20 million in FY 2012 and $19 million in FY 2011.

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

Note 15: Cash Flows

The following table consists of detailed cash flows from the sales and purchases of investment activity. Sales and purchases of investments are driven by the level of newly trusteed plans, the unique investment strategies implemented by PBGC's investment managers, and the varying capital market conditions in which they invest during the year. These cash flow numbers can vary significantly from year to year based on the fluctuation in these three variables.

INVESTING ACTIVITIES (SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS COMBINED)

	September 30,	
(Dollars in millions)	**2012**	2011
Proceeds from sales of investments:		
Fixed maturity securities	**$70,055**	$73,641
Equity securities	**6,120**	9,113
Other/uncategorized	**1,874**	3,704
Memorandum total	**$78,049**	$86,458
Payments for purchases of investments:		
Fixed maturity securities	**$(69,841)**	$(77,935)
Equity securities	**(6,681)**	(4,144)
Other/uncategorized	**(1,262)**	(2,248)
Memorandum total	**$(77,784)**	$(84,327)

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

RECONCILIATION OF NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	September 30,		September 30,		September 30,	
(Dollars in millions)	**2012**	2011	**2012**	2011	**2012**	2011
Net income (loss)	**$(5,876)**	$ (1,672)	**$(2,467)**	$(1,334)	**$(8,343)**	$(3,006)
Adjustments to reconcile net income to net cash provided by operating activities:						
Net (appreciation) decline in fair value of investments	**(6,958)**	(1,634)	**(46)**	(91)	**(7,004)**	(1,725)
Net gain (loss) of plans pending termination and trusteeship	**(27)**	23	**0**	0	**(27)**	23
Losses (credits) on completed and probable terminations	**2,006**	201	**0**	0	**2,006**	201
Actuarial charges (credits)	**14,874**	6,561	**0**	0	**14,874**	6,561
Benefit payments - trusteed plans	**(5,333)**	(5,382)	**0**	0	**(5,333)**	(5,382)
Settlements and judgments	**0**	0	**0**	0	**0**	0
Cash received from plans upon trusteeship	**126**	36	**0**	0	**126**	36
Receipts from sponsors/non-sponsors	**114**	70	**0**	0	**114**	70
Amortization of discounts/premiums	**99**	100	**10**	10	**109**	110
Changes in assets and liabilities, net of effects of trusteed and pending plans:						
(Increase) decrease in receivables	**(510)**	144	**0**	1	**(510)**	145
Increase in present value of nonrecoverable future financial assistance			**2,535**	1,445	**2,535**	1,445
Increase in unearned premiums	**(38)**	2	**(1)**	0	**(39)**	2
Increase (decrease) in accounts payable	**(8)**	(33)	**1**	0	**(7)**	(33)
Net cash provided (used) by operating activities	**$(1,531)**	$(1,584)	**$ 32**	$ 31	**$(1,499)**	$(1,553)

Note 16: Litigation

Legal challenges to PBGC's policies and positions continued in FY 2012. At the end of the fiscal year, PBGC had 47 active cases in state and federal courts and 473 bankruptcy and state receivership cases.

PBGC records as a liability on its financial statements an estimated cost for unresolved litigation to the extent that losses in such cases are probable and estimable in amount. In addition to such recorded costs, PBGC estimates with a degree of certainty that possible losses of up to $68 million could be incurred in the event that PBGC does not prevail in these matters.

Note 17: Subsequent Events

Management evaluated subsequent events through publication on November 14, 2012, the date the financial statements were available to be issued. Events or transactions for either the single-employer or multiemployer program, occurring after September 30, 2012 and before the financial statements were available to be issued, that provided additional evidence about conditions that existed at September 30, 2012 have been recognized in the financial statements.

For the single-employer program, there was one nonrecognized subsequent event. Subsequent to September 30, 2012, business and financial conditions significantly declined for one controlled group that sponsors two single-employer plans (unfunded guaranteed liabilities of $0.063 billion). Had these events occurred on or prior to September 30, 2012, PBGC's financial statements would have reflected an additional loss of $0.063 billion resulting in an FY 2012 single-employer net loss of $5.939 billion and an FY 2012 single-employer net position of $(29.205) billion.

For the multiemployer program, there was one nonrecognized subsequent event. On November 5, 2012, PBGC received a formal notice of a mass withdrawal termination from a multiemployer plan, resulting in the present value of financial assistance of approximately $0.127 billion as of September 30, 2012. Had this event occurred on or prior to September 30, 2012, PBGC's financial statements would have reflected an additional loss of $0.127 billion, resulting in a FY 2012 multiemployer program net loss of $2.59 billion and a FY 2012 multiemployer program net position of $(5.36) billion.

Audit of the Pension Benefit Guaranty Corporation's
Fiscal Year 2012 and 2011 Financial Statements

Audit Report AUD-2013-1 / FA-12-88-1

Section III

Management Comments

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PBGC
Protecting America's Pensions
Pension Benefit Guaranty Corporation
1200 K Street, N.W., Washington, D.C. 20005-4026

Office of the Director

MEMORANDUM

November 14, 2012

To: Rebecca Anne Batts
Inspector General

From: Josh Gotbaum Josh Gotbaum
Director

Subject: Response to the Independent Auditor's Combined Audit Report on the FY 2012 Financial Statement Audit

Thank you for the opportunity to comment on the Office of Inspector General's FY 2012 combined audit report, including the opinions on PBGC's financial statements, internal controls, and compliance with laws and regulations.

Management appreciates the work your office performs in your oversight of this audit. As PBGC's work involves billions of dollars and affects millions of Americans, it is especially noteworthy that the Corporation has once again received an unqualified opinion on our financial statements for FY 2012.

We also recognize and concur with your opinion on internal controls. Management has already set the foundation and continues its work for addressing the three material weaknesses (benefits administration and payment department management and oversight, entity-wide security program planning and management, and access controls and configuration management) and the significant deficiency (integrated financial management systems) that were recognized as a result of prior audit work.

We are committed to addressing the findings in our corrective action plans and will keep you informed of our progress.

cc: Laricke Blanchard
Patricia Kelly
Alice Maroni
Ann Orr
Michael Rae
Srividhya Shyamsunder
Judith Starr
Martin Boehm
Theodore Winter

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