BNA, INC.

PENSION & BENEFITS

BNA Employee-Owned Since 1947

DAILY

Public Plans

Public Pension Plans Getting It Right, Speakers Tell Senate Committee Hearing

Public pension plans are ''getting it right,'' so the federal government does not need to get involved, speakers told a hearing of the Joint Economic Committee July 10. In addition, they suggested, public plans should be used as a model for the private sector.

Sen. Robert Casey (D-Pa.) said he convened the hearing to get specific recommendations on what to do about the future of defined benefit plans, and whether any Congressional action was needed in the area of public pension plans. ''At a minimum, we should ensure that the circumstances that led to the decline of defined benefit plans in the corporate world are not repeated in the public or Taft-Hartley [multiemployer plan] sectors,'' Casey said.

Stability of Public Plans. Nearly 20 million active employees and 7 million retirees and dependents participate in public pension plans, according to Barbara D. Bovbjerg, Director, Education, Workforce, and Income Security, U.S. Government Accountability Office.

Most public plans have enough money to pay for promises for several years to come, Bovbjerg said. However, funding levels have fallen steadily since 2000, she said. Many governments have not put in enough contributions needed to maintain funded ratios, which could lead to questions about the ability to sustain the funds, she added.

In addition, ''states have about a decade before health care costs eat them alive,'' she said.

Benefits of Public Defined Benefit Plans. According to Christian E. Weller, associate professor at the Department of Public Policy and Public Affairs, University of Massachusetts, public pension plans usually meet all the criteria for an ideal pension plan, including broad-based coverage, portability, professionally managed assets, and adequate lifetime benefits.

In addition, Weller said, the benefits of defined benefit plans include:

- *Mortality risk-pooling*. By pooling the mortality risks of large groups of people, defined benefit plans only need to accumulate assets to fund retirement benefits over the average life expectancy. Individual investors have to plan for their maximum possible lifetime, requiring more assets.
- *Economies of scale*. Pooled assets allow plans to reduce their costs.
- *Diversification*. The ability to diversify adds to improved rates of return.

Another benefit of public pension plans is that they provide investment opportunities that are not available to participants in individually managed defined contribution plans, including private equity and real estate, both of which require investing large amounts on a long-term basis, said William Pryor, chairman of the board of investments at the Los Angeles County Employees Retirement Association. In addition, public plans have a huge impact on a state's economy, and mean significant community improvements, he said. Finally, defined benefit plans play an important role in the U.S. economy by providing long-term, patient investors, he added.

Responding to the question of whether public pensions are an efficient allocation of taxpayer money, Weller said taxpayers want to have good teachers, police, and firefighters, so governments need good defined benefit plans offering a solid retirement, survivorship benefits, and disability benefits in order to recruit and retain these workers.

The increased investment in venture capital is another benefit of public defined benefit plans, according to Sherrill Neff, a partner in the venture capital firm Quaker BioVentures, in Philadelphia. Most public pension plans invest a small percentage of their assets in venture capital, he said. Venture capital— a subsector of alternative investments—is invested in start-up companies, and has an investment horizon of five to 10 years, Neff said. The typical start-up company employs highly skilled, highly paid professionals that spend in the economy, Neff said.

Impact on Oil Prices. Rep. Kevin P. Brady (R-Tex.) asked Weller whether public pension plans are to blame for higher oil prices, and what would be the effect of legislation that would limit the ability of these large plans to invest in oil futures.

Weller responded that legislators should be careful in regulating markets. ''If you shut out large investors that bring liquidity, it could cause more volatility,'' Weller said. The problem is the big price swings in commodities, Weller said. It would increase volatility to take out the investors that have a long-term interest, he added.

Recommendations on Congressional Action. ''Public sector plans are getting it right,'' and should be used as a model to improve income security in the private sector, Weller said. There is no role for the federal government in public sector plans, he said. However, Congress should look at why single-employer defined benefit plans have disappeared while multiemployer plans have remained stable, he said.

Bovjberg said public pension plans are stable, so there is not much to be done by the government. GAO will release a report soon on the dynamics of frozen plans and is starting work on what would be a good hybrid plan, she said.

Neff said the government should not do anything that would further encourage public funds to move from defined benefit to defined contribution designs.

BY ANDREA L. BEN-YOSEF

