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PUBLIC SECTOR PENSIONS--FUNDING THE BENEFITS, AND PROTECTING THE FUNDS

by Bruce Poyer

For the fifth straight year, a statewide conference on issues confronting California's public sector pension plans will be held in Sacramento, on February 16-17, at the Woodlake Resort and Convention Hotel (500 Leisure Lane, a few miles north east of downtown Sacramento). Conference co-sponsors are the Institute of Industrial Relations, U.C. Berkeley (Bruce Poyer, conference coordinator), and the Retirement Betterment Committee of Glendale, California (George Buck, President). The title of this year's conference is the title of this article, which describes the conference orientation and topics to be discussed by invited experts, legislators, and plan officials.

General Conference Orientation -- Public employees in California have pension coverage under more than 140 different plans, but only the 10 largest have 10,000 or more participants. The major public sector plans include (1) the Public Employees Retirement System (PERS), covering state and local agency and classified school district employees; with 559,350 active members, 190,000 retirees, and 22,500 survivors and beneficiaries, PERS is now one of the largest pension systems in the nation; (2) the 20 county plans which are governed by legislated provisions enacted in 1937; and (3) about 52 independent city or county or district plans, including "major" city plans in San Francisco, Los Angeles, Oakland, and San Diego, and "major" special district plans like that of the Metropolitan Water District of Southern California.

Estimates of the total assets of California's public sector pension plans, now invested all over the world, exceed \$90 billion. These assets are the pension fund savings of more than a million public employees in California.

Public sector pension plans in California have separate jurisdictions and constituencies. They differ in the organization of their governing boards and administrative systems and in the policies which they set for funding and investing. However, those noted above function under basic legislative provisions and concepts which do not differ greatly, and are also similar in their benefit structures. Of course they confront the same economic conditions when they set their contribution rates or fund their liabilities or manage their investments or seek to improve their benefits. Two other important California pension systems, the University of California's Retirement System and the State Teachers' Retirement System, are significantly different in structure and funding aspects; problems that are unique to these systems will not be considered in detail at the February conference.

In past years, representatives from all of these plans have attended the annual pension conferences in Sacramento. Public employee organizations, with significant representation on the boards of administration of these plans, have been especially well represented at the annual conference. Some management representatives who are concerned about the pension systems also attend. The conference is designed for basic education on generic issues that confront all major plans. These issues are explored by invited experts who present various points of view.

Agenda Issues for the February 16-17 conference --

Funding and Protecting the Funds: The first of three major issues to be developed at this year's conference concerns both the funding of the plans, and the protection of plan assets that are accrued to fund plan "liabilities" (i.e., the present and future benefits owed to covered employees as deferred wages). The opening conference session on Monday afternoon, Feb. 16, will focus on basic principles of funding any pension plan, and will trace important similarities and differences in the funding of public and private sector plans, Social

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Security, defined benefit and defined contribution plans. Questions about the level of funding and the actuarial time table for full funding will get special consideration.

Since considerable amounts of money are involved in the funding of future benefits, and since such amounts must be held and invested and reinvested over long periods of time, careful consideration will next be given to all existing legal requirements that protect the pension plan's assets. California law has been tightened in recent years to protect plan assets from unauthorized appropriation for non-plan uses, including the temptation to use plan assets to support the general budgets of public agencies. The key question to be considered is how to require adherence to existing legal protections that should be adequate, but are too often ignored or misunderstood or distorted in the trench warfare of public agency budget politics.

Corporate governance: Under this generic hearing, which is the second main conference topic this year, are grouped a variety of problems confronting pension plan trustees in carrying out their investment responsibilities. Policies are required for the voting of proxies, for divestment from South Africa, for handling other moral or ethical issues (like infant formulas, the war in Ireland, women's rights, health hazards, etc.) and for "social investment." The fiduciary obligations of trustees to invest pension funds only on the basis of maximizing returns has always been appealing in theory, but fraught with difficulties in practice. The California policy of divesting from South Africa, for example, has been justified both on moral and ethical grounds, and on the more limited basis of financial risk, which trustees are also obliged to consider.

The same combination of moral/ethical with financial risk factors now hangs over a broader range of pension fund investment policies and decisions, concerning the monitoring of questionable corporate behavior. A colorful new vocabulary has sprung up to describe some of this behavior, involving pension fund investment options which are generally not covered by careful investment policy guidelines. The vocabulary includes terms like junk bonds and activities like buy-outs and take-overs (including the leveraged varieties), down-sizing, poison pills, greenmail, golden parachutes, etc. Corporate raiders like T. Boone Pickens and Carl Ichan have popularized the new vocabulary. But what is involved in corporate behavior, like what is still involved in divesting from South Africa, requires better definition and understanding, not only in traditional economic and financial terms, but even more in terms of social goals and values. For the most part, appropriate monitoring guidelines are not in place to guide pension fund investments around these tangled thickets of the corporate jungle.

Retiree health benefits: The third major topic at this year's conference concerns the protection of retiree health care benefits, which have been under attack in many jurisdictions in California and in the nation--particularly in the private sector. The question of full health care protection for retirees has increasingly been subjected to the same kind of actuarial analysis used to insure the availability of future pension benefits for retirees, and the projections that are made from this kind of analysis are increasingly bleak. Many employee benefit plans have already been forced to consider whether pre-funding of retiree health benefits is now essential if current actives are to be guaranteed the same health benefits that current retirees have--even when current benefits are recognized as inadequate to meet the primary health care needs of current retirees. Invited experts will discuss both the projections based on present realities and trends, and the pros and cons of pre-funding, as it has been recommended for PERS in the Mercer study and report of 1984, and as it has been implemented in Santa Clara county.

Conclusion--The conference format designed to cover the above issues necessarily involves considerable discussion and analysis by recognized experts and specialists in employee benefit planning, some of whom do not always speak plain and simple English. Therefore, the format also includes a final session which is open to any and all questions from the floor, on any topic which was raised (or should have been raised) during the conference. Interpreters are available at this session, for the specific purpose of translating questions that may have been mystified rather than clarified in the development of the conference agenda, and giving plain answers to these questions, whenever possible.

A speakers' agenda and a conference registration form are enclosed with this mailing of LCR.

-- Bruce Poyer

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