Opinions

David H. Webber: Protecting public pension investments

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Public pension funds should invest the retirement savings of government workers to secure their financial future, not undermine it. Yet across the country, these funds are financing companies that privatize their own workers' jobs. And because many of these investments are funneled through private-equity companies, the problem is still largely hidden from public view.

Pension trustees who are rightly concerned about these investments too often find themselves silenced by a subtle legalistic maneuver that took place six years ago last month and that could be stopped with the help of President Obama's Labor Department.

Consider the public school system in Chelmsford, Mass. The schools employed custodians who were once paid $25 an hour and were promised a modest pension. For decades, the jobs had been reasonably stable. But as Bloomberg News reported, these custodians learned in 2012 that their jobs had been privatized and they were being fired. They were then offered the same job, at a 50 percent pay cut, by Aramark, a private firm that had been funded by their own pension funds. In other words, the pension plan was invested in a company that made money by slashing the future pensioners' wages.

This pattern is surprisingly pervasive: The retirement funds of firefighters, teachers, prison guards and others are invested in private firefighting companies, private public-school-service companies and private prisons. These companies may offer the promise of high investment returns, but they may achieve those returns at the expense of the public employees themselves. The Florida Retirement System, with half its assets belonging to teachers and other school employees, bought Edison Schools, a company that ran public schools. Pension funds have financed the privatization of school bus companies, water utilities and libraries. Displaced workers not only stop contributing to the funds, losses that can harm other workers and retirees, but also often must turn to public assistance to survive, undermining the argument that taxpayers benefit from these transactions.

In theory, legal protections exist to ensure that employee benefit plans invest in the economic interest of employees. The duty of loyalty that is enshrined in state pension codes requires that such investments be made "solely in the interests of participants and beneficiaries." Thus, one might think that pension trustees would be required to assess whether investments in companies that compete for jobs with a fund's beneficiaries are actually in the economic interest of their members. But things are not as simple as they should be.

Pension trustees justify these investments by pointing to an "interpretive bulletin" issued by the Labor Department in the waning days of George W. Bush's presidency, on Oct. 17, 2008. It does not technically apply to state and local pension funds, but it is widely relied upon to guide the interpretation of their trustees' fiduciary duties.

According to this bulletin, the statutory command that trustees act "solely in the interests of participants and beneficiaries" really means that they should act solely in the interest of "the plan." Under this plan-centric view of loyalty, trustees can invest in companies that seek to privatize their own members' jobs, focusing exclusively on the investment return to the plan.

This subtle shift has stark consequences for public employees. It transforms an investment's impact on jobs — which is of vital interest to workers and beneficiaries — into an "extraneous" consideration. By asking whether an investment that harms participant jobs is really in the interests of the plan's participants and beneficiaries, a fund trustee potentially risks violating his or her duty of loyalty to the plan. This perverts the duty's original purpose.

The toxic combination of this flawed view of the law and the rise of politicians who are committed to undercutting public employees and their unions creates a potent weapon to use against workers. Governors, state treasurers and mayors can encourage, or at least tolerate, the use of these (collectively enormous) retirement funds against the employees and pensioners themselves. How loyal is that?

Proper understanding of the duty of loyalty should empower trustees to weigh the impact of investments on jobs. That doesn't mean abandoning a core focus on investment returns, and it doesn't mean blindly boycotting privatizing investments. It means asking whether exiting would work or whether it would simply lead to replacement by another, indifferent investor. It means asking whether engaging the investee to reduce the jobs impact could advance the economic interest of members.

In restoring this proper understanding of a trustee's role, a few well-placed lawsuits might help. Indeed, some helpful legal precedents already exist. Favorable pronouncements from state attorneys general or legislatures could also move things in the right direction.

Best of all would be a new interpretive bulletin from Obama's Labor Department, with its national voice and its powerful, if informal, influence over state and local pensions, clarifying that when the duty of loyalty says that trustees should invest "solely in the interests of participants and beneficiaries" it means just that — not in the interests of "the plan," or anyone else.

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