Transparency in Public Pension Plans

NCSL Legislative Summit

August 10, 2016

Susan Banta, Director of Research
Public Sector Retirement Systems Project
The Pew Charitable Trusts

• More than 40 active, evidence-based research projects

• Projects include public safety, immigration, elections, transportation, pensions, and state tax incentives

• All follow a common approach: data-driven, inclusive, and transparent

Pew’s Public Sector Retirement Systems Project

• Research since 2007 includes 50-state trends on public pensions and retiree benefits relating to funding, investments, governance, and employee preferences

• Technical assistance for states and cities since 2011
  – No one-size-fits-all approach
  – Key principles for reform: fiscal sustainability for states and retirement security for workers
Investments – Key Trends:
Bond Yields Decrease

Figure 2
Public Pension Plan Median Assumed Rate of Return Versus U.S. Treasury Bond Yields in 1992 and 2012
Plans’ anticipated risk premium has grown by 4.5 percentage points

Between 1992 and 2012, the difference between the median pension fund’s assumed rate of return and the yield on risk free 30-year Treasury bonds has increased from .33 percentage points to 4.83 percentage points.

Source: U.S. Treasury and Analysis by the Pew Charitable Trusts of Comprehensive Annual Financial Reports, actuarial valuations and related reports from states
© 2014 The Pew Charitable Trusts
Investments – Key Trends: 
Increased Risk Premium

US Public Fund Average Increasing Risk Premium
Plan’s assumed rate of return remains relatively stable, while bond yields have declined

State Pension Fund Expected Rates of Return

Most public pensions target a long-term rate of return between 7 and 8 percent.

Source: Analysis by the Pew Charitable Trusts of state Comprehensive Annual Financial Reports.
©2016 The Pew Charitable Trusts
Investments – Key Trends: More in Stocks and Less in Bonds

Public Pension Investments, 1954-2014

Allocations to equities and alternative investments have increased, while those to fixed-income investments have declined

Investments – Key Trends: Increased Use of Alternatives

Public Pensions Include More Alternative Investments
Share of pension assets in alternatives has more than doubled

Impact of Trends on Performance, Cost, and Risk
Volatility in Returns – S&P 500 and Pension Plan Returns
FY 2005-2015

Source: Wilshire®, Trust Universe Comparison Service®
External Management Fees as a Percent of Assets

Reported Fees increased by 30% as a percentage of assets from 2006 to 2014

Source: Analysis by the Pew Charitable Trusts of state Comprehensive Annual Financial Reports.
©2016 The Pew Charitable Trusts
Reporting Standards Must Keep Pace with Changes in Investment Practices

• Make investment policy statements transparent and accessible
• Disclose bottom-line performance, both net and gross of fees
• Expand performance reporting to include 20-year results by investment type
• Include performance results by asset class – both net and gross of fees
• Adopt comprehensive fee reporting standards (ILPA)
Transparency and Bottom Line Performance
Performance Reporting Practices Vary Across the States

Thirty-seven percent of funds report returns “gross of fees”

Note: South Dakota discloses performance as both net and gross of fees. The states marked as having multiple reporting methods have two funds included in our list of 73 that report performance differently from each other.

Source: Comprehensive Annual Financial Reports (CAFRs), state treasury reports, quarterly investment reports, and state responses to data inquiries.
Alternative Investments and Comprehensive Fee Disclosure
Reported Private Equity Fees by State Pension Fund
Performance fees substantially higher than invoiced management fees

Source: Analysis by the Pew Charitable Trusts of SCRS and MOSERS Plan CAFRs and CEM Benchmarking
©2016 The Pew Charitable Trusts

CalPERS’ recent supplemental disclosure of PE performance fees also equaled over 2% of assets
Just How Much in Private Equity Fees Go Unreported?

• In 2014, state-sponsored plans held more than $250 billion in private equity (nearly 9 percent of assets).

• Estimated $4+ Billion in undisclosed fees
Looking Forward: Measuring and Disclosing Risk
State-Sponsored Fund 10-Year Returns, 2014
Performance varies widely, from less than 6 percent to 9 percent

Average 10 Year Return = 7.2%

Source: Analysis by the Pew Charitable Trusts of state Comprehensive Annual Financial Reports.
©2016 The Pew Charitable Trusts
Funding Projections Through 2060
(Under Current Investment Return Assumption of 8%)

All dollar figures in millions
Sources: The Terry Group
Funding Projections Through 2060
(Under Lower Investment Return Scenario of 6%)

All dollar figures in millions
Sources: The Terry Group
Public Sector Retirement Systems Project

Susan Banta
sbanta@pewtrusts.org

www.pewtrusts.org/publicpensions