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Union Pensions Could Fail Sooner Than Expected, Actuaries Say

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- Interest rates don't align with expected returns
- Plans may hedge existing assets in 10-20 years

Strict investment limits regulators have placed on financial assistance for failing multiemployer pension plans could result in lower returns, thrusting those plans back to the brink of insolvency sooner than expected.

The federal government's private-sector pension insurer last week issued long-awaited rules governing how it would administer President Joe Biden's $94 billion bailout for union-brokered pension plans. Millions of workers' retirement benefits have been threatened by more than 100 massively underfunded group plans that struggled to survive after a spate of economic downturns since 2001.

Special financial assistance was expected to forestall plan insolvency until at least 2051, but now some actuaries believe the federal Pension Benefit Guaranty Corp.'s investment limits are so conservative that plans could be in trouble much sooner.

"There's a real risk that 10 or 20 years from now, plans will be forced to take big risks to ensure this money doesn't run out," said Shivin Kwatra, head of liability-driven investment portfolio management at Insight Investment. "We've got a real challenge ahead of us in terms of not having enough assets."

While the PBGC didn't immediately respond to a request for comment about the actuarial concerns, the regulator is seeking stakeholder feedback on its investment limits.

'Math Doesn't Add Up'

The PBGC says it will calculate how much individual plans can expect to receive using interest rates that don't align with the kinds of modest returns special financial assistance is expected to generate in

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the market.

Those rates are clearly outlined in the law Congress passed, said Ted Goldman, PBGC's director of policy research and analysis. They must be the lesser of the plan's existing funding rate and IRS third-segment discount rates plus 2%. That sets a goal rate of return for plans investing the financial assistance they receive; they would need to generate at least 5.5% annually to ensure the money lasts until 2051, according to current PBGC variable rate premiums.

Under normal circumstances, that likely wouldn't be a problem, but the law also limited the way plans could invest the money, restricting investments to investment-grade bonds "or other investments as permitted by the corporation." The PBGC opted to keep plans' options limited only to fixed-income investments like highly rated corporate bonds or treasuries that usually return no more than 3.5% annually.

That would result in up to a 2% annual funding shortfall and leave most critical and declining plans cash-strapped by about 2040—11 years sooner than Congress intended.

"I think we're all for taxpayer dollars being invested conservatively, but the math doesn't add up," said Gene Kalwarski, CEO of Cheiron Inc., a leading multiemployer plan actuarial firm.

Not Over Yet

PBGC officials considered setting flexible investment limits that would require returns to match expected benefit payments, but opted not to put caps on variable investment returns. Still, the agency erred on the side of caution.

"I don't think the PBGC is asking everybody to play it conservatively. I think they're asking investors to play it smart," said Neil Gregorio, an attorney at Tucker Arensberg P.C. who represents many of the nation's largest multiemployer plans.

The details PBGC issued last week came in the form of an interim final rule, and the agency will be accepting comments to inform a final rule until Aug. 11. The preamble itself highlights the need for more information on investment limits and hybrid or fixed-income security replicates such as insurance contracts and stocks.

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"PBGC is providing a starting point for discussion on permissible investments of [special financial assistance] assets in this interim final rule," it reads. "With an eye toward finding a more appropriate balance between certainty and safety of investments on the one hand, and the opportunity for plans to have flexibility to decide appropriate overall investment policies on the other, PBGC seeks public input."

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