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Moody's: Public Pension Plans Lag Corporate Plans in Managing Credit Risk.

Credit risks related to pension liabilities will be a bigger problem for governments than for corporations for at least another decade, according to a new report from Moody's Investors Service.

The report is Moody's first look at the divergent pension risks of the public and private sectors, said Alfred Medioli, vice president and senior credit officer for public finance. "It's very illustrative to see how different disclosure regulation and exposure can be," he said in an interview.

While corporations have federal agencies, accounting rules and shareholders monitoring how well they fund their pension plans and manage the related credit risk, state and local governments do not. "It becomes an issue of governance," said Mr. Medioli, who added that more arcane accounting practices for government pension sponsors don't help control underfunding. "The problem began to build and nobody was able to grab a hold of it. That's why we began this study."

The report notes the 50 largest corporations have a median pension liability as a percentage of total debt (including pensions) of 24%, while the government median is 73% for states and 49% for large local governments. The state data are for fiscal year 2012 and the local government number is based on fiscal 2011 data.

The report also notes strategies used by the private sector to manage pension risk, including switching to defined contribution plans from defined benefit and the use of liability-driven investment strategies. "The question is, will (governments) have to follow the corporate route to derisk, or will they come up with something different? We think that they will find a solution to this," said Mr. Medioli.

The two sectors also differ on the degree of taxpayer backstops in place. While corporate sponsors are likely to place less strain on government pension guarantees as their risk of needing help from the Pension Benefit Guaranty Corp. diminishes as they derisk, state and local governments are facing a growing need for taxpayer funding, Moody's found.

Hank Kim, executive director and counsel of the National Conference on Public Employee Retirement Systems, Washington, cautioned that mimicking the corporate switch to defined contribution plans is not the answer for government workers. "Thirty years down the road, we're going to be a nation of seniors subsisting on social safety net programs paid for by middle-class taxpayers. In the larger scheme, (the switch to DC is) just deferring costs onto taxpayers," Mr. Kim said.

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