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Billionaire Arnold's Pension Push Makes Him Workers' Bane.

When Kentucky, with the country's second-lowest funded pension system, set out to bolster the plan last year, it sought recommendations from Pew Charitable Trusts, funded in part by Houston billionaire John Arnold.

Kentucky's worker retirement plan, squeezed by investment losses and shortchanged for years by the state, had just 30 percent of what it would need to pay the benefits due as employees retire in the years ahead. So the state's lawmakers decided to cut long-term retirement benefits for newly hired workers, just as the Philadelphia-based Pew suggested.

Arnold, 40, a former hedge-fund manager and Enron Corp. commodities trader, has inserted the Houston-based Laura and John Arnold Foundation into political fights over how to deal with the rising cost of state and local government pensions. A Democrat who says he has raised money for President Barack Obama, Arnold sees such benefits as unsustainable.

"Many public pensions are poorly designed, allowing elected officials to underfund benefits and shift massive market risk onto state and local governments," Arnold wrote in response to e-mailed questions. "The problem is only getting worse. Governments have a history of delaying tough decisions until an emergency."

Pension Gap

U.S. state and local pensions have shortfalls of at least $1.4 trillion because of stock market losses and the failure to set aside enough to cover future retirement checks. That's been a drain on governments since the recession, with officials forced to pump more money into their pensions just as they were cutting spending on schools, roads and other services.

In Detroit, indebted pensions were part of the city's $18 billion bankruptcy, which is threatening to cut payments to retirees. In New Jersey, Governor Chris Christie this year decided to skip $2.4 billion in payments to the worker pension plan as he faces a new round of budget shortfalls. Illinois, the lowest-rated U.S. state, had its rating outlook cut to negative by Standard & Poor's last month because of doubts that a decision to reduce benefits will survive legal challenges.

National Effort

Arnold has pushed for overhauls in 30 cities and states, including Rhode Island, Kentucky and San Jose, California. Arnold says he and his wife have spent about $12 million on the pension debate since 2008.

Public workers who oppose what they see as his push to cut pension benefits estimate his contribution to be at least four times as high.

"His foundation is spending a lot of money on public pension issues and they're spreading it to a lot of different groups," said Keith Brainard, the Georgetown, Texas-based research director with the National Association of State Retirement Administrators in Washington. "It's clear that they're trying to affect the debate."

Arnold has angered public workers, who say his campaigns are gutting negotiated pension benefits they earned and need to ensure secure retirements.

"Every time we have a new offensive against pensions, Arnold is behind it," said Jordan Marks, executive director of the National Public Pension Coalition, a group in Washington that supports public workers. "John Arnold is involved in a number of attempts to eliminate pension plans around the country."

Foundation's Goal

The foundation's goal isn't to cut benefits for workers, said Josh McGee, vice president of public accountability.

"Laura and John Arnold Foundation believes those who have dedicated their lives to public service deserve to be part of a sustainable system that places them on a path to a secure retirement," said McGee. "Pension reform must establish a fair, workable plan to pay down the accumulated pension debt as quickly as possible, require governments to pay their pension bill in full every year, and create a retirement savings system going forward that is affordable, lasting, and fair."

The coalition estimates Arnold has spent $52 million, when it factors in everything, including expenditures that aren't described as related to pensions in disclosures made on his Web site. Arnold said 3.8 percent, or $12 million, of the $320 million by his foundation, in campaign contributions, and in charitable giving has gone to the pension debate. Either amount is minuscule compared with what unions have paid to maintain the status quo, he said.

Hedge Fund

Arnold shut down his Houston hedge fund, Centaurus Energy, which traded energy commodities, in 2012, after about 10 years. Before that he worked in Enron's wholesale division, where he was head of natural gas derivatives. Laura Arnold had worked in several places as a corporate attorney. After he wound down the hedge fund, he and Laura created the foundation.

Arnold said he is trying to use his estimated $2.9 billion fortune to clean up a legacy of bad policy decisions by state and local officials where "special interests or market failures have led to poor government policy. "

It's part of a larger push by his foundation, which has made $261 million in grants for everything from poverty and criminal justice to education and the functioning of state and local government, to "improving our society," Arnold said in a March 31 commentary published on the Chronicle of Philanthropy's Web site in response to critics.

Union Donations

Arnold said in his e-mailed response that the most influential parties in the debate over pensions are "unions, their leaders and the politicians who depend on their donations."

"Organized labor has spent millions funding research reports that support the status quo and billions on the political process to support elected officials who reject reform," wrote Arnold. "Virtually everyone involved in the debate on public pensions has had financial or political interests in the outcome. We do not.”

Bringing change to pensions would be difficult without the support of Arnold and his foundation, said San Jose Mayor Chuck Reed, who worked to reduce his city’s pension obligation and also has pushed to reduce pension liabilities statewide. Arnold’s foundation helped bring legal and financial expertise to both, Reed said.

“If you don’t do something the problem is just going to get bigger and bigger and eventually the governments could end up in bankruptcy,” said Reed. “I’m glad they decided to focus part of their expertise on pensions. Their advice is extremely valuable.”

Unfunded Liabilities

Arnold, through his foundation, has paved the way for legislation that cuts the risk and ultimate cost of pensions. Even so, states such as Kentucky are still grappling with large unfunded liabilities because cuts apply only to new workers.

“The most pernicious problem in any state with a significant funding shortfall is that they have failed to make contributions as required,” said Monique Morrissey, an economist with the Economic Policy Institute, a Washington research institution that focuses on the role of low- and middle-income workers in the economy. “There’s a large hole in many states because of years of systematic underfunding.”

That is one reason Arnold’s foundation works with groups such as Pew, the Brookings Institution and the Reason Foundation to help government officials understand the magnitude of pension commitments and develop changes that will allow them to continue to offer benefits, Arnold said in the e-mail.

‘Lasting Improvements’

“We support organizations that help governments make decisions based on evidence and data to produce concrete, measurable, and lasting improvements to society,” Arnold said.

It’s the same objective stated by some of his partners.

“We share the goal to help states design and adopt retirement systems that are fair, affordable and fiscally sustainable—while at the same time preserving governments’ ability to recruit and retain a talented public-sector workforce,” said Greg Mennis, director of public sector retirement systems, for Pew, in a prepared statement.

In Kentucky, restructuring the retirement plan led to “a fair and effective retirement system” that will improve its fiscal health, Pew said.

As a state, Kentucky has the second most-underfunded pension plan in the U.S. behind Illinois, with about 47 percent of the assets needed to cover future estimated payments to retirees, according to data compiled by Bloomberg.

Cash Balance

Last year, Kentucky switched new employees to a so-called cash balance plan, which pays benefits based on how the money is invested instead of what employees earned and how long they were on the job.

The legislation, which passed with bipartisan support, put the state on course to “honor the commitments made to state workers and retirees” and addressed “financial uncertainty that threatened our state’s credit rating,” said Governor Steve Beshear, in an April 4, 2013, statement.

Under the restructuring, workers’ benefits don’t increase as sharply with years of service as they do under the previous plan, according to a report from the Urban Institute, which also has received funding from Arnold’s Foundation. Though employees with short tenures may accrue more money in the short term, those who work 35 years would only receive three-fifths as much as they would under the traditional plan, according to the Urban Institute report.

Lawmakers came together in part because of a Pew report. “We relied on Pew as a source of objective information,” said Representative Jim Wayne, a Louisville Democrat who was on the committee considering changes. “It was not objective. We gutted the pension program for new hires.’

The plan also many not solve the state’s underfunding problem as intended, Brainard said. That’s because only newly hired workers are covered under the plan, meaning the outstanding obligation for currently retired workers and existing employees continues.

‘‘Switching to a different type of plan doesn’t address the existing unfunded liability,” Brainard said.

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By Darrell Preston
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To contact the reporter on this story: Darrell Preston in Dallas at dpreston@bloomberg.net

To contact the editors responsible for this story: Stephen Merelman at smerelman@bloomberg.net Jeffrey Taylor, William Selway