Rhode Island workers' pensions cut as hedge funds profit

John Marion
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In a lengthy article August 3, the *Providence Journal* described the state government's increasing investment of pension assets in hedge funds. While the state claims that it is using the hedges to protect future pensions from economic risk, the article makes clear that speculators have made substantial profits—including $45 million of hedge fund fees in the year ending June 13—while gambling with the money. This shift has occurred in the wake of a 2011 pension "reform" that increased retirement ages, suspended cost-of-living adjustments on retiree pensions, and required that workers contribute increasing amounts to their pensions.

According to the *Journal,* $1 billion of Rhode Island pension funds, more than 13 percent of the $7.5 billion total, are now invested in hedge funds that gamble on residential mortgage-backed securities, global currency fluctuations, fracking operations, and other schemes.

Three hedge fund managers are mentioned by name—all trustees of the Manhattan Institute think tank—who were hired in the fall of 2011 by Rhode Island's State Investment Commission and its chair, state Treasurer Gina M. Raimondo. Raimondo is described as "a Democrat and former venture capitalist who is contemplating a run for governor in 2014." In 2012 she won an Urban Innovator Award from the Manhattan Institute, but claims that she doesn't remember meeting the three hedge fund managers she had hired.

In a follow-up on August 8, the *Journal* reported that Raimondo's office had released only "heavily censored copies of reports detailing hedge-fund operations" and had let the hedge funds decide which "proprietary information" should be kept secret from the public.

While Rhode Island has now invested a bigger portion of its pensions in hedge funds than most other state and municipal systems, the gambling is part of a national trend. The *Journal* cites a study by financial firm Prequin and concludes that "public pension plans are the largest single investors in hedge funds." In other words, at a time of unprecedented attacks on workers' retirement benefits by state and local governments, the lie that there isn't enough wealth is being used to hide hedge fund thievery.

Customarily, state and local governments in the US have rationalized their underfunding of defined benefit pension plans with complex actuarial calculations and accounting methods that allow for manipulation of the estimated interest on the pension liability. Even a one percent change in this discount rate can have a substantial impact.

The transition from such accounting to outright gambling goes hand in hand with the general growth of wealth inequality in the years since the 1991 recession. An actuarial report on Providence's retirement plan found, for example, that the funded ratio of police, fire, and management pensions decreased from 57.4 percent in 1994 to 31.9 percent in 2011.

Rhode Island is now penalizing its public employees because state and municipal governments underfunded their pension plans for years. One disturbing provision of the 2011 "reform" legislation is that there will be no cost-of-living adjustments (COLA) on pension payouts until the state has funded 80 percent of what it owes.

The 2011 pension legislation created a hybrid benefit structure, which includes the traditional defined benefit plan, but also a new defined contribution plan sometimes requiring drastic employee contributions. The defined contribution plan, similar to a 401(k), will require a five percent contribution from state workers, general municipal employees, teachers, and nurses in the state's Department of Behavioral Healthcare, Developmental Disabilities & Hospitals. Government contributions to this plan will be only one percent of workers' wages. General municipal employees who want a COLA on their defined benefit plan payouts will need to double their current contribution to two percent of their wages. Police and firefighters, who are not eligible for the defined contribution plan, will have to contribute eight percent of their wages in order to get a COLA on their defined benefit payouts.

Workers who are laid off and then recalled will need to pay for "service credit" to include the layoff period in the number of years they've worked toward retirement. Using a complicated transitional formula, the legislation also raises the retirement age from 62 to the "Social Security normal retirement age."

The supposed lack of money for the basic right to a good pension did not stop Rhode Island from lowering its top income tax rate from 9.9 percent to 5.99 percent starting in 2011. The same tax legislation also lowered the capital gains rate to 5.99 percent. It kept the corporate tax at 9 percent, but also maintained a minimum tax for corporations of $500 per year. According to Rhode Island's Senate Fiscal Office, 92.7 percent of the state's 48,597 corporate filers used this loophole in 2008, paying only the minimum amount. The Senate report found that in fiscal year 2010 all corporate taxes—including Provider Assessments on "non-profit" Health Care providers—totaled less than $400 million, while regressive sales taxes accounted for more than $1 billion in state revenues.

An April 2012 study by the Pew Center for the States examined state documents and found that Rhode Island was not evaluating the effectiveness of tax incentives it gives to corporations, nor was it "using data to inform policy choices."

It is not surprising, therefore, when the *Journal* reports that of the 18 hedge fund managers in Rhode Island, seven are billionaires and were ranked last year among the 40 richest by Forbes.

Rhode Island's unemployment rate was above 9 percent in May, and in recent years the cities of Central Falls, Providence, and Woonsocket have launched vicious attacks on teachers and other public employees. In May the state's Revenue Estimating Conference noted that Rhode Island is the only US state in which the population has "consistently" decreased since 2010. The exodus is no doubt a result of chronic unemployment, which has reached 12 percent at times since the 2008 crash.

Rhode Island has a complicated system of public sector pensions, which gives some authority to municipalities about whether their workers participate in Social Security, but also includes a state-administered Municipal Employees Retirement System (MERS). The latter was also "reformed" by the 2011 legislation.

An August 3 article in the *Los Angeles Times* about Central Falls, a small working class city that has been a test bed for municipal bankruptcy and attacks on workers' livelihoods, gives some idea of the impact of the pension crisis. The *Times* interviewed a retired firefighter—who in one fire was injured by a falling wall—who expected a yearly pension of $36,000 after 19 years of service. After Central Falls filed for bankruptcy, his pension was cut by a third to $24,000.

Another firefighter with 35 years of service told the *Times*, "I feel like I was robbed" and that he and his wife have become "prisoners in [their] own house" because of a lack of retirement income. Such statements reflect the simple fact that the ruling elite has no compunction about stealing benefits promised to workers throughout their careers. Before the state offered a limited amount of funding, Central Falls cut the pensions of its retirees by up to 55 percent.