Keeping Politics Out of Public Pension Investing

Times have changed since public pension systems relied predominately on contributions and high yield bonds to fund earned pension benefits. The average state and local public pension today relies heavily on global and private investment strategies to honor pension obligations, making public pension funds some of the largest, most active investors in the world. Unfortunately, some politicians see these investments as opportunities to use billions in taxpayer and member contributions in support of social and political interests.

Codifying activist pension investing policies into law hinders pension administrators' ability to maintain a reliable and resilient investment strategy and violates the fiduciary responsibilities associated with pension governance. Policymakers should consider the following when deliberating activist pension investing policies:

Fiduciary Responsibilities

- Pension funds are governed by boards of trustees with a legal fiduciary responsibility that extends only as far as maximizing returns to benefit retirees and future beneficiaries.
- State laws typically include explicit provisions stating that the primary responsibility of fiduciaries is to run the plan solely in the interest of participants and beneficiaries and for the exclusive purpose of providing benefits and paying plan expenses. As a part of this role, fiduciaries must act prudently by diversifying the plan's investments to minimize the risk of large losses.
- Policymakers must avoid pitting social and economic concerns against fiduciary obligations.

Common Activist Investing Targets:

Political Divesting
e.g., oil and gas, tobacco, firearms, disfavored countries, abortion

Political Investing
e.g., ESG, green energy, climate change mitigation

Technical Complexities

- The average public pension fund holds investments in thousands of private and public funds comprised themselves of hundreds of individual investments that come and go over time, making it difficult to account.
- The global sanctions imposed on Russia in early 2022 showcase how difficult is it to comply with activist investment strategies when assets are intertwined and distributed across multiple funds and exchanges.

Promotes Risk Taking

- Replacing objective fiduciary standards with an activist investment strategy destroys the notion of public pension funds as multi-generational sources of retirement security and effectively turns funds into political action groups.
- Forcing pension boards to base investment decisions on subjective political standards elevates the interest of a particular political constituency over pensioners and taxpayers as a whole, removing the long-term solvency of the pension system as the paramount objective and potentially leaving future generations on the hook for the financial repercussions of those decisions.

Takeaway: Policies directing politically motivated, activist investments counter to fiduciary obligations undermine public pension fund governance and increases financial risk for future generations.

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