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Philadelphia urged to do more to avoid Detroit bankruptcy

Attracta Mooney

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Philadelphia has a $5.7bn pension deficit

Philadelphia has been urged to "take all necessary" action to tackle its $5.7bn pension deficit amid fears the city could suffer the same fate as Detroit, where a $3bn public pension funding gap contributed to its bankruptcy.

The organisation tasked with preventing Philadelphia from going bankrupt has urged the city's mayor, council and pension fund board to pass legislation to fix the problem.

Philadelphia's public pension scheme, which manages the retirement funds of 64,000 current and former employees for the Pennsylvanian city, has less than half the money it needs to pay present and future pensioners. It had assets of $4.8bn in mid-2014.

The city's funding ratio — a measure of assets to liabilities — is below that of 17 of the 21 local pension plans in the 10 most populous US cities, according to the Pennsylvania Intergovernmental Cooperation Authority (Pica), which oversees the financial health of Philadelphia.

Harvey Rice, executive director of Pica, said Philadelphia city officials are "not doing enough" to reduce the pension deficit. "Much more needs to be done," he said.

In 2013, Detroit filed for bankruptcy after raking up debts of £18bn; its public pension scheme was estimated to account for a sixth of that total.

Philadelphia's financial position is better than Detroit's. Standard & Poor's, the rating agency, gave its bonds an A+ rating, meaning its risk of default is low. However, Mr Rice said a lack of improvement in Philadelphia's pension scheme would put the city's budget significantly under strain.

The city's contribution to the public pension scheme has increased from 5 per cent to 16 per cent of Philadelphia's budget over the past decade, Mr Rice said.

"If no measures are put in to curtail the pension deficit, it will continue to grow to a bigger percentage of the budget," Mr Rice added. "That would be a big concern to the city."

Mr Rice said public employees should be forced to increase their contributions to the city's defined benefit scheme, which provides retirees with a set retirement income based on their earnings at the end of their career.

Pica is also calling for all new employees to be placed into a recently introduced hybrid scheme, which is more akin to a defined contribution plan.

Unofficial figures show the pension fund had a tough year in 2015, returning just 0.29 per cent compared with 15.7 per cent in 2014.

Its funding ratio fell from 46.1 per cent to 43.1 per cent, because of losses from investments. The average funding ratio for city and county pension plans across the US is 75 per cent, according to Wilshire Consulting, the investment advisory company.

A spokesperson for the City of Philadelphia said: "The pension situation is serious, there's no denying that."

He said the city is in discussion with unions that represent its workers about making changes to the pension plans.

The city is due to engage in collective bargaining, where working conditions and benefits are set, with District Council 33, the largest public sector union in Philadelphia, in June. District Council 33 did not respond to requests for comment.

Rob Dubow, chairman of Philadelphia's pension fund board, said the scheme was also looking closely at its relationship with asset managers in a bid to close the funding gap. "We are working aggressively to cut our fees [that are paid to fund managers]. When we look at managers, we try to get the lowest fees possible. We have got rid of managers," he said earlier this month.

Detroit emerged from bankruptcy in December 2014, but last week it warned its public pension fund was again on course for a deficit. The mayor said the fund would be underfunded by $490m by 2024.

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