Wall Street Takes Workers' Retirement Money and Uses It Against Them

BY
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Workers' retirement savings aren't usually thought of as a stimulating topic. But we should pay closer attention, because public pensions are a key way for Wall Street to steal wealth from workers and hoard it for themselves.

As the private equity industry launches ads to protect its lucrative tax preferences, we should remember that this industry is the unseen man behind the curtain driving many social ills — from high hospital prices to surprise medical bills to nursing home deaths to media layoffs to a housing crisis that has become a human rights emergency. A *Businessweek* cover put it best: You live in private equity's world, even if you don't know it.

But a series of new reports remind us that there is another person behind the monocled, mustache-twirling oligarch running the Emerald City's secret control panel — and that person isn't a billionaire. It is the faceless pension official in a state capital or city hall who is using workers' retirement savings to finance the Wall Street takeover of Oz.

In the process, teachers, firefighters, sanitation workers, and other government employees are being fleeced. Their retirement savings are being skimmed by finance industry executives, who are using the cash to lobby for self-enriching tax breaks while waging a class war on everyone else. All that money could end up bankrolling a new round of housing profiteering and infrastructure privatization, using workers' money to wage a war on workers themselves.

The relationship between the finance industry and public pensions has become one of this gilded era's biggest schemes to redistribute wealth from workers to Wall Street — but the theft barely gets any attention outside the business press. I've been reporting on it for a long time (and I've faced the wrath of politicians like Chris Christie for doing so). So I know well that the term "pension" is considered a mind-numbing, cure-for-insomnia kind of topic that corporate media mostly ignores.

In the popular imagination, a pension is known, if at all, as a shitty European hotel, a pool of extra cash that Gordon Gekko tried to pilfer in the Bluestar Airlines deal, or a small bit of subsistence pay that grandpa used to get back in the day, when times were different.

But here's the thing you need to know: public pensions are a huge business, and quite exciting to the world's richest people in the here and now.

That's because, while fewer and fewer workers today get pension benefits, there is now $5 trillion in public pension systems that have accrued government workers' retirement savings over decades. That giant pool of capital, overseen by appointees tied to Wall Street–bankrolled politicians, is the fuel behind the finance industry's conquest of America.

Pension money is deferred compensation: Millions of public-sector workers — who are often paid less than their private-sector counterparts — have accepted lower up-front wages in exchange for pension contributions to fund their future retirement benefits. Two decades after pension officials began funneling more of that money into private equity, hedge funds, and real estate, roughly one-fifth, or about $1 trillion, of the cash is now in these opaque "alternative" investments. These investments generate outsize fees for financial firms, bankroll Wall Street's political machine, and capitalize the corporations that are pillaging the middle class.

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This is a wildly lucrative business — and money managers are now trying to rake in even more from public pensions and also break into the even larger 401(k) market. You can see investment firms' desperation in Wall Street's cynical ad campaign trying to convince Americans that private equity firms are consistently delivering outsize investment gains for pensioners (they're not).

The question is: Will this racket continue and get even bigger?

Spoiler alert: the following piece is a deep dive — but it has to be. In many ways, the tale of the unholy union between public pensions and the shadowy world of alternative investments connects much of the reporting my colleagues and I have been pursuing for the past several years.

This is it, the big heist, the rigged game that connects corrupt local officials, soulless Wall Street robber barons, rapacious corporate CEOs, and the public-sector workers who may be unaware that their pension contributions are financing a giant scam that harms us all.

Retirement Savings Are Bankrolling Billionaires

Perhaps funneling pension money into risky and opaque Wall Street schemes could be justified, if they had produced great returns for retirees. But while investment fees have been a jackpot for Wall Street firms, the returns haven't been so fantastic for pensioners.

Two big industrial states tell the larger tale.

In Pennsylvania, pension officials just admitted that they pumped about two-thirds of the state retirement system's assets into alternative investments. That strategy generated below-average returns for retirees, but it generated $4.3 billion worth of fees for Wall Street firms — which is more than the entire amount workers paid into the fund in the same time period.

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In other words: all of the money pulled out of Pennsylvania public workers' paychecks in the last four years that was supposed to go to their retirement savings was instead used to pay Wall Street firms' fees — and in exchange, workers were given investment returns that did not beat a low-fee stock index fund.

Next door, in Ohio, a new forensic investigation by former Securities and Exchange Commission attorney Ted Siedle estimates that the state teachers' pension fund is paying more than $460 million in fees every year, and alternative investments have wildly underperformed compared to their projections. Those fees are more than twice the amount the state saved in 2017 when Ohio officials halted cost-of-living increases that would allow pension benefits to keep up with inflation.

Even more shocking: Siedle reports that the pension fund is likely paying big fees to private equity firms on uncommitted capital — which is money set aside to be invested but not yet deployed. He estimates that Ohio pensioners are annually forking over $143 million of such fees *for investments that haven't even been made*. That's enough to restore most of the cost-of-living cuts, but it is instead being used to pay investment firms. As Siedle puts it, the state is effectively "paying managers for doing nothing."

All these figures may be understated. A study last year by CEM Benchmarking concluded that only about half of all investment fees in America's multitrillion-dollar pension system are even being disclosed. The SEC has twice warned of rampant fee fraud in the private equity industry. But workers and journalists can't see all those fees, because many states and cities passed Wall Street–sculpted laws exempting investment firms from open records statutes.

Ohio and Pennsylvania are hardly isolated incidents. State and local pension funds are among the biggest backers of alternative investments, and that has meant a huge transfer of wealth from retirees to Wall Street firms. One 2020 analysis by Oxford professor Ludovic Phalippou found that private equity firms have raked in nearly a quarter-trillion dollars in performance fees in the last fifteen years. In California, one pension fund alone has shelled out more than $3.4 billion on fees to these firms.

Now, multiply that over hundreds of state, county, and municipal pension funds, and you start to understand the true scale of the upward transfer of wealth every single year.

In exchange for that enormous jackpot, public pensions are rarely generating returns for workers and retirees that beat low-fee stock index funds.

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The outsize fees aren't unrelated to those weak returns — they are central to funds' underperformance. After all, it is difficult to consistently generate market-beating returns for retirees when money managers are skimming 2 percent off the top and then pocketing 20 percent of any capital gains — which is standard in the alternative investment world.

Making matters even worse for retirees is the "dumb money" phenomenon, a snarky Wall Street term describing how pension officials doling out OPM — other people's money — can be less meticulous and less sophisticated in negotiating fee terms and shareholder rights than private investors who are gambling with their own cash.

This dynamic was at play when finance firms swindled pension funds into buying crappy mortgage-backed securities in the lead-up to the financial crisis. It remains a particularly pernicious problem, considering that Wall Street money managers can use fine print to reserve the right to prioritize returns for their friends over the returns they provide pension funds — even within the same investments.

Unlike publicly traded stocks, which sell on exchanges at transparent prices, stakes in private equity, hedge funds, and real estate can have different terms for different shareholders in the same investments. That means there is no guarantee money managers aren't using "dumb pension money" to juice the returns of other investors with stakes in the same partnerships.

Workers' Money Is Funding the War on Workers

Government workers getting ripped off by fees is bad enough — but that is not where this story ends. The other chapter of this tale is about how the fee revenue and the underlying investments are being used to exacerbate inequality and intensify America's class war.

First and foremost, the fees being skimmed off the top of workers' savings are going into a financial industry that has become an elaborate tax haven helping billionaires evade the levies that the rest of us pay.

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At the corporate level, much of pensioners' savings is flooding into private equity and real estate partnerships, which are avoiding $75 billion a year in taxes by not reporting income to tax officials, according to one study recently cited by the *New York Times*. And those fees skimmed from workers then fund Wall Street's political apparatus, which has successfully preserved the special tax loopholes, created the secrecy laws, and secured the Supreme Court rulings that fortify the financial industry's vast architecture of theft.

Meanwhile, fine print in investment agreements allows Wall Street firms to use investors' money

— read: pension money — to fund their lavish lifestyles, including their private jet travel.

At the individual level, the wages of firefighters, sanitation workers, and other government employees are directly inflating the pay of the richest people on the planet. Billionaire private equity moguls skim fees off government workers' investment earnings, and then use the infamous carried-interest tax loophole to classify their vig as capital gains rather than as regular income subject to higher tax rates. Some pension officials have also approved these billionaires using so-called "fee waivers" to ram even more of their fees through this pernicious loophole.

The private equity industry continues to defend the loophole as a fair and constructive tax policy, but let's state the obvious: society gleans no benefit from providing a preferential tax rate to a Wall Street kingpin pocketing 20 percent of the winnings off teachers' retirement investments while delivering returns that don't beat a cheap Vanguard fund. That lower tax rate doesn't protect shrewd investment expertise or "hard-earned taxpayer dollars." It unfairly shelters the easily earned winnings being reaped by professional con men — and now, government workers' pension money is effectively financing the private equity industry's new ads defending the loopholes.

Beyond the fees, there is the real-world impact of the investments themselves. And there, too, the story is deeply troubling.

Pension money has flooded into alternative investment funds profiting off looting hospitals and media companies.

Pension money has also backed private equity funds that bought up the hospital staffing companies delivering massive, out-of-network medical bills to patients that insurers have refused to pay. Congress passed legislation last year to end surprise medical bills at hospitals, but the law doesn't cover ground ambulance companies, which have also been snatched up by pension-backed private equity firms.

Through alternative investments, pension money has continued to provide capital to the fossil fuel industry that is creating the climate crisis threatening all life on the planet.

Pension money was not only investment capital behind the mortgage-backed securities that blew up the global economy, it has been invested in the private equity firms that have bought up more and more of the nation's housing stock, from suburban single-family homes to mobile home parks. Pension-backed private equity and real estate firms have jacked up rents, neglected tenants, and used investment funds to bankroll the campaign against rent control. And now the private equity industry is relying on pension money to boost its plans to buy up even more suburban homes.

Pension money has even continued to flow to the private equity firm that controls major fast food chains paying low wages, and whose umbrella company recently claimed credit for killing a national $15 minimum wage.

Pension Money Could Fuel the Biden-Republican Privatization Initiative

Taken together, workers' retirement money is being leveraged to enrich oligarchs and fund their war on workers — and get this: very soon, government employees' pension savings could be the capital that funds the privatization of whatever is left of America's crumbling public infrastructure.

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The new bipartisan infrastructure framework announced by President Joe Biden includes a push for "asset recycling" — the process whereby governments sell off roads, bridges, airports, and other public assets to Wall Street investment firms.

If this sounds familiar, that's because — in the spirit of Biden's promise that "nothing will fundamentally change" — the proposal is a recycled asset from President Donald Trump's kleptocratic White House. And indeed, Trump's infrastructure adviser — who worked at infrastructure investment firm Macquarie — is talking up Biden's proposal as a way to help Wall

Street firms buy up and profit off everything from federally owned dams to airports.

This is the kind of scheme that politicians love, because it lets them quietly enrich their Wall Street donors while boasting that they are making public investments. It's the "public-private partnership" model that corporate predators like McKinsey tout, that transportation secretary Pete Buttigieg loves to brag about, and that public pension money may end up bankrolling, if history is any guide.

Back in 2015, more than seventy public pension funds provided capital to fund the Indiana Toll Road privatization scheme, a project that has been beset by big problems. Despite the cautionary tale of Australia's foray into asset recycling, Biden's infrastructure proposal could take such privatization schemes national, ignoring evidence that they can end up raising user fees, reducing public oversight, and letting corporations use state-backed monopoly control over public assets to boost their private profits.

Investment industry executives and right-wing think tanks are already beating the drum for more pension money to fund the initiative — and if past is prelude, that cash will come through to both finance the schemes and pay the big investment fees to the corporate firms involved.

Casino Gambling and a Culture of Corruption

The evil genius of our financialized economy is how it makes us complicit in capitalism's crimes. Our basic necessities of life — our jobs, wages, retirement savings, food, transportation, and housing — are often intertwined with abusive corporations and business models.

Public workers' pension funds operate inside this system, and their participation in a financialized economy is not a crime unto itself. They have a fiduciary responsibility to provide retirement benefits to millions of workers, and that requires reliable investment returns.

The question, though, is: Why have pension overseers sought those earnings in investments that finance and fuel corporate pillage?

One argument has been that at least some of the worst industries have delivered decent investment performance, and such returns are all that pension funds should focus on. That line of reasoning has been used to justify union representatives on pension boards approving all sorts of private equity and hedge fund investments, and it has been used by some unions to fight against divestment from fossil fuel companies.

And yet, these ends-justify-the-means claims about great returns don't pass the smell test. For all their elaborate investments, pensions have recorded weak returns time and again, and in the specific case of the fossil fuel industry, there is a strong and growing body of evidence that divestment is the fiduciarily responsible move.

Another argument — most prominently championed by New York state comptroller Thomas DiNapoli, who runs one of the world's largest pension funds — says that investing pension money with corporate villains is good because it gives workers at least a small shareholder voice against wrongdoing. But while it is certainly true that shareholder initiatives have constructively influenced some corporate behavior, that positive impact is far outweighed by the decidedly negative effects of hundreds of billions of dollars of pension money capitalizing some of the worst industries and greediest billionaires on the planet.

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So, what's *really* driving this sordid relationship between public pensions and private profiteers?

It's a mix of casino gambling and graft.

For years, many state and local governments have refused to make their promised payments into pension systems, instead diverting the cash into boondoggles like giant corporate subsidies and high-income tax cuts. This is the equivalent of getting a job with a promised 401(k) and then watching your company CEO just refuse to make the 401(k) contributions and instead use the money to redecorate his office.

Without adequate employer-side contributions, pension funds are relying on investment returns for the majority of their revenues — and pension officials have faced widening gaps between pension assets and owed benefits. So, in desperation, they have headed for the Wall Street casino to put bigger and bigger piles of pensioners' chips on the roulette tables run by private equity, hedge funds, and real estate magnates.

Save for a few occasional shouts of protest, unions representing workers and retirees have largely gone along with such desperation gambling, probably because they feel like they get something out of the bargain: they get Wall Street helping them create the misleading illusion that everything is going fine. Indeed, in the short term, financial firms' bullshit promises of big future returns for pensioners make it seem like mounting pension deficits will be taken care of, which helps unions avert a dangerous legislative battle over whether states should raise taxes to fund pension benefits or slash those benefits.

But, as we've seen in Wall Street–pillaged states like Kentucky, the problem is that reality eventually rears its ugly head when the casino returns are subpar, the pension system is nearly bankrupt, and opportunistic politicians use the crisis as justification to slash promised benefits.

That said, pension officials are not just desperate. In the enormously powerful position to distribute OPM, many of them are complicit in a giant grift.

State and local pension officials could run their funds like Nevada's, which has generated solid returns for retirees by putting most of its money in index funds, rather than in the alternative investment casino. But that would mean that those officials would have a boring work life, like the guy who runs that fund in Carson City.

By contrast, when state and local pension officials open up their funds to lots of exotic Wall Street investments, they get the chance to live a more exotic life for themselves.

For instance, as a *Philadelphia Inquirer* exposé recently showed, pension managers get to travel all over the world to lavish investment conferences held by the firms managing retirees' money.

To give you an idea of what these conferences are like, we recently uncovered an agenda from a 2017 investors meeting held by the private equity firm TPG at the posh Phoenician resort in Scottsdale, Arizona. Guests there were treated to a talk by CNN host Fareed Zakaria and a live performance by Cirque du Soleil. We scored the agenda from a public records request sent to some of the attendees: Wisconsin pension officials.

Speakers at the Carlyle Group's investor conferences have included former president Barack

Obama, Fox News host Tucker Carlson, and numbers pundit Nate Silver.

Between the trips and the wining and dining, these pension officials sometimes tip over into straight-up self-enrichment schemes that land them in legal hot water. (Although at least one of the highest-profile pension grifters on Wall Street was rewarded with an MSNBC gig, where he gets to push austerity on the middle class).

Other times, pension officials' own personal investments create cartoonish conflicts of interest that critics argue provides an incentive for them to direct ever more pension cash into high-fee Wall Street firms.

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The status perks can be just as pernicious. As one pension overseer once told me, getting appointed to a pension board anywhere in America means that when you get off a plane in New York, billionaires are happy to wine and dine you, because even if you're from some nondescript midsize city, you still represent hundreds of millions of dollars in potential investment business.

Put another way: being a pension investment officer or board member in some nondescript locale is one of the few government gigs in town that potentially gets you treated like a celebrity by the richest and most powerful people on the planet.

As for the elected officials who either appoint pension officials or directly oversee pensions themselves, pay-to-play laws passed in the wake of corruption scandals officially prohibit them from raising campaign money from finance executives seeking pension business. However, when these officials in unglamorous jobs like state treasurer and city comptroller say they're open to funneling pension money to private equity kingpins and hedge fund tycoons, it means they get to hobnob with those prospective donors for their future runs for higher office.

And sometimes they can just evade or circumvent those pay-to-play laws anyway.

The end result is where we are today: giant pools of public employees' savings now provide the financial foundation for a feudal economy and corporate avarice on an all-encompassing scale.

The fix here isn't to eliminate public pension benefits — on the contrary, recent moves by states to expand access to such benefits are a way to combat inequality.

No, the solution is to better direct these pools of capital into investments that provide a decent return and that actually finance businesses that benefit society.

But doing that requires first an understanding of the current problem, and then a commitment by workers, their unions, and their elected officials to finally change an entire culture of corruption.

You can subscribe to David Sirota's investigative journalism project, the *Daily Poster*, here.

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