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From the issue dated February 13, 2009

## Pension Shortfalls Put Pressure on Strained University Budgets

By MEGAN ECKSTEIN

With the stock market in decline, college pension plans are losing money, and administrators are scrambling to cover the shortfall.

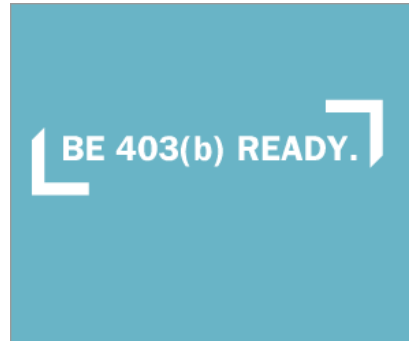
At some institutions, defined-benefit pension plans are at their lowest levels in decades. Many plans now hold less than three-quarters of the money they will need to pay retiree benefits, says Olivia S. Mitchell, a professor of insurance and risk management at the Wharton School of the University of Pennsylvania.

That figure lags behind the holdings of public pension plans over all, which have been financed at around 85 percent over the past few years, according to the Governmental Accounting Standards Board, an independent agency that establishes standards of financial accounting and reporting.

"The market has tanked and continues to go down," Ms. Mitchell says. "Universities are going to have to come up with money ... in order to restore funding levels."

Colleges' pension problems could bring other difficulties with them. Although an underfinanced pension system is not an immediate threat to an institution's credit rating, it is treated as a debt-like obligation and could affect the rating, says Roger Goodman, a vice president at Moody's Investors Service.

An overwhelming majority of public universities, and some private institutions, participate in defined-benefit pension plans, which guarantee employees a certain amount of compensation in retirement. The colleges themselves usually pay most of the costs of the defined-benefit plans in which they participate, but in some cases employees contribute small amounts.



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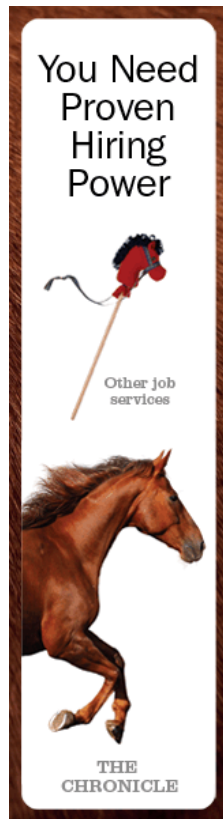
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## **New Stress for Public Colleges**

The pension shortfalls — several billion dollars in some large university systems — are creating new stresses for public colleges, many of which are already grappling with state budget cuts and endowment losses.

In some states, the legislatures are ultimately responsible for ensuring that public colleges' pension systems contain enough money to pay retiree benefits. But if states have to unexpectedly replenish lost pension money, they may have to make cuts elsewhere, including higher education, says Robert L. Clark, a professor of economics management, innovation, and entrepreneurship at North Carolina State University.

Colleges are dealing with their pension deficits in various ways. The University of California, which saw its pension investments drop by about \$6-billion as of June 2008, faces a shortfall of 5 percent — or \$2-billion — if it does not add money to the plan. (Financing formulas do not require that institutions replenish the full amount of losses in a given year.)

Administrators in California will very likely address the possible shortfall by dipping into the system's operating budget and requiring employees to contribute to the plan for the first time in almost 20 years, says Paul Schwartz, a university spokesman.

The system's Board of Regents is scheduled to decide this month whether to pour \$875-million into the pension fund, mostly university money but also some employee contributions. [Late last week, after this article went to press, the regents approved that proposal.]

The decision will come just a year and a half after the system put off plans to resume contributions — and it will follow more than two decades of surpluses. At times the plan was bloated, with almost 50 percent more money than it needed, allowing the state to avoid paying into the plan since 1990. But the surplus has run out.

A pension system in Missouri that covers professors at many of the state's regional colleges dropped in value by about \$2-billion in 2008. Although the colleges' contribution rates are locked in for the coming fiscal year, the institutions will probably have to find room in the 2011 budget to increase its contributions, says Christine A. Rackers, manager of investment policy and communications at the Missouri State Employees' Retirement System.

The colleges' one solace is that not all of their faculty and staff members participate in the slumping defined-benefit plan. In 2002 the regional institutions started funneling new faculty members into a defined-contribution plan, which removes employers' liability. Now, whenever that fund's value drops, the new employees are on the hook.

In Pennsylvania, Gov. Edward G. Rendell has warned that the state's flagship university may need to increase its contributions to the State Employees' Retirement System.

Pennsylvania State University's pension plan incurred significant investment losses last year, a spokesman says; its value will not be made public until April. As of December 31, 2007, it had a 3-percent shortfall.

About a third of Penn State's faculty and staff members participate in the plan. In recent years, the university has contributed about \$10-million annually, or at least 3.2 percent of employee payroll, to the state's pension system, says Albert G. Horvath, vice president for finance and business.

It is too early to know how much the university's contributions would be increased as a result of the pension's declining value, he says.

Some defined-benefit plans are proving especially costly during this market downturn, says North Carolina State's Mr. Clark, but it is unlikely that there will be a shift toward plans that place less liability on the employer. Some state pension systems considered such a move a decade ago, after noticing that the private sector had moved toward defined-contribution plans. But the states decided against the switch, largely because of short-term costs and labor issues.

For now, colleges are stuck trying to compensate for the lost money. The full extent of the damage may not be clear until this fall, when financial reports for the current fiscal year can be analyzed.

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