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Pension fund management concerns all segments of the economy. Poor investment returns can increase costs for plan sponsors, erode retirement benefits of workers, and increase reliance on the Social Security program at a cost to taxpayers.

Investment Performance of Pension Funds

Private pension funds now constitute 29 percent of total funds available for investment. The management of these funds concerns all segments of the economy, particularly the 75 million workers, retirees, and their dependents who depend on private pensions for financial security in retirement. This important issue was the subject of public hearings by the U.S. Department of Labor in January.

Poor investment returns can increase costs of the plans to sponsors, erode the retirement income value of benefits, and ultimately increase reliance on the Social Security program for retirement benefits. If plan investment returns are inadequate, the taxpayer will pay the costs.

This *Issue Brief* compares the performance of pension funds with mutual funds, evaluates the factors which influence performance, and considers how performance could be improved.

Although pension fund performance exceeded that of mutual funds in the short run, the returns were much closer over a longer period. The returns of both types of funds outpaced inflation over longer periods.

Investment managers set target rates of returns based on plan goals and compare performance to bond and stock indices, market conditions, or a real rate of return comparable to the economy's growth rate.

How well a fund performs depends more on the asset mix of the fund than on the plan type, sponsor, or investment manager. Among both mutual and pension funds, fixed-income funds outperformed equity funds and balanced portfolios over the last twelve months.

Several approaches have been suggested for improving pension fund performance, including deregulation of certain investments, creation of long-term U.S. government bonds indexed to inflation, and increased holdings of alternative or social investments. Their value to a fund, however, depends on the overall goals and strategy of the fund.

A monthly periodical devoted to expert evaluations of a single employee benefit issue

◆ Introduction

Private pension funds now constitute 29 percent of total funds available for investment. The pensions they finance, in turn, are important to the financial security of 75 million workers, retirees, and their dependents and survivors. The management of these funds, therefore, should concern everyone.

This *Issue Brief* covers the following issues:

- How does the investment performance of pension funds compare with that of other investors?
- How are pension funds performing against inflation?
- What is a realistic target rate of return for funds?
- What determines the performance of pension funds?
- How can pension fund performance be improved?
- How is pension fund performance related to retiree benefits?

The Department of Labor (DOL) recently held public hearings on this issue. This *Issue Brief* relies not only on the published sources cited but also on interviews with several investment managers about some of the issues raised by DOL.

◆ How do Pension Funds Compare With Other Investors?

Comparing the performance of pension funds with that of other institutional investors, like mutual funds, is difficult. In theory, pension funds operate over a longer time span, which should decrease their need for liquidity and for short-term performance. Other investors may be under pressure to show more impressive short-term results. Pension funds also have the advantage of being able to pursue both income and capital gains without having to consider the tax implications of alternative forms of income. Pension funds, however, are constrained by restrictions imposed under the Employee Retirement Income Security Act of 1974 (ERISA). ERISA restricts the types of transactions the plan can enter, particularly with related entities, it requires that plan assets be diversified, and it imposes prudence standards.

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While pension funds differ from other institutional investors, their performance patterns are nevertheless similar. Pension funds and mutual funds provide a useful comparison because many pension plans are themselves invested in mutual funds.

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Table 1
Short and Long-Run Total Returns in Mutual Funds

	Short-Run Returns[a]	Long-Run Returns[b]
Forbes Stock Fund Composite	−10.8%	17.5%
Forbes Bond and Preferred Stock Composite	−0.1	10.2
Forbes Balanced Fund Composite	−2.1	13.9

Source: Laura R. Walbert, "1984 Annual Mutual Fund Survey," *Forbes*, August 27, 1984, pp. 68–119.
[a]Returns for year ending August 1984.
[b]Average annual total returns, 1974–1984.

While pension funds differ from other institutional investors, their performance patterns are nevertheless similar. Pension funds and mutual funds provide a useful comparison because many pension plans are themselves invested in mutual funds. The comparisons discussed below are based on performance data compiled by *Forbes* magazine on 529 mutual funds that invest in taxable securities and a group of pension funds participating in the Trust Universe Comparison Service (TUCS) totaling nearly 25 percent of all pension assets.[1] The compilation of investment performance data in these databases differs in certain crucial respects, making exact quantitative comparisons hazardous.[2] However, the data do provide a basis for comparing broad performance trends.

Pension funds performed better than mutual funds in the short run. In the last year, mutual funds lost from 0.1 to 10.8

[1] The mutual funds were surveyed in August 1984 by *Forbes* magazine. The pension fund data for the year ending in the third quarter of 1984 were compiled by Wilshire Associates in the Trust Universe Comparison Service (TUCS).

[2] Comparisons between mutual funds and pension funds are complicated by the fact that at this writing, data computed on the same basis were not available to the author. That is, mutual fund data were available in both composite form and in quartiles for the current year, and only in composite form for the period 1973 to 1984. Pension fund data were available only in quartiles for both the current year and for the preceding four years. However, EBRI calculations of median performance data for mutual funds for the current year differed relatively little from the composite data. Therefore, the analysis in this section would probably remain fundamentally unchanged if all long-term data were available in the same form.

percent depending on their investment mix (table 1). Fixed-income (bonds and preferred stock) funds posted the lowest losses; stock funds, the highest. In contrast, many pension funds earned positive net returns. The median fund invested in fixed-income instruments earned 8.3 percent and balanced funds earned slightly more than half as much (table 2). The median equity pension fund lost far less than equity mutual funds.

Over a longer period, however, pension fund and mutual fund returns were much closer. Since 1974, mutual funds have earned an average of 10.2 to 17.5 percent per year (table 1). Since 1980 pension funds have earned from 10.3 to 15.3 percent per year (table 2).

◆ How are Pension Funds Performing Against Inflation?

Nominal returns have to be compared with the loss in the purchasing power of accrued pension benefits due to inflation. Since 1974, inflation has averaged 7.8 percent per year. With mutual fund returns averaging 10.2 to 17.5 percent per year, mutual funds earned net real returns of 2 to over 9 percent per year. Since 1980, inflation has averaged 6.5 percent, while pension funds returned 10.5 to 17.8 percent (table 3). Real returns in pension funds thus averaged 4 to over 10 percent per year over this period.

At the same time, however, different time periods or plan samples can yield very different patterns. For example, the S.E.I. Funds Evaluation Service reports that over the last fifteen years the median fund in its sample achieved an average return of 6.9 percent per year, while the average annual rate of inflation was 7.2 percent.[3] The median fund in that group therefore, lost an average of 0.3 percent of its value per year.

Table 2
Short- and Long-Run Total Returns in Pension Funds

Type of Fund	Short-Run Returns[a]	Long-Run Returns[b]
Defined Benefit Funds		
Equity	−0.2%	15.3%
Fixed-income	8.3	10.3
Balanced	4.4	12.8
Defined Contribution Funds		
Equity	−1.0	14.2
Fixed-income	c	c
Balanced	5.1	12.6
Union/Jointly Trusteed Funds		
Equity	−0.9	13.9
Fixed-income	8.3	11.0
Balanced	5.8	11.5

Source: Wilshire Associates, *Trust Universe Comparison Service*, Third Quarter, 1984.
[a]Median total return for year ending September 1984.
[b]Average value of median rates of return, 1980–1984.
[c]Not available.

◆ What is a Realistic Target Rate of Return for Pension Funds?

Performance data are important, but they do not provide an objective standard in themselves for evaluating the performance of pension funds. The standard or target should be based on a plan's goals. There are many target rates of return that could be set. For example, various bond and stock indices have been developed that allow comparison of fund performance against a specific market segment. However, some managers feel that the appropriate target depends on market conditions. In some markets preserving capital could be an achievement. In other markets, such as the current environment, with AAA corporate bonds paying an average of 9.8 percent during the third quarter of 1984, and inflation at an annual rate of 3.3 percent in the year ending in the third quarter, the target rate of return could be much higher.

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While market conditions impose short-run constraints on attainable returns, at least one observer has suggested that over the longer term, pension funds should aim at a real rate of return comparable to the economy's growth rate.[4] Economists estimate that the economy should be able to sustain a long-term growth rate of 2 to 3 percent. Since wages will generally reflect economic growth, an investment return that also reflects growth will mean that the plan shares in the economy's growth and is not becoming an increasing real burden on the sponsor.

[3] Eugene B. Burroughs, "The Fiduciary's Lament: Whither Inflation?" *Pension World* 20 (August 1984): 21.

[4] Eugene B. Burroughs, "More Plans Are Addressing the Real Rate of Return Issue," *Pension World* 20 (October 1984): 54.

What Determines the Performance of Pension Funds?

Some pension funds perform well even in adverse market conditions, while other funds are falling far short of needed returns. Why do some plans perform better than others? Some of the plan characteristics that have been cited in the past as possible influences on investment performance include:

- the type of plan;
- the type of sponsor;
- the investment manager; and
- the investment strategy.

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Type of plan

Defined benefit plans are commonly believed to offer the participant more retirement income protection than do defined contribution plans because the employer bears the risk of poor investment return. Inadequate investment earnings in defined benefit plans must be made up through added sponsor contributions, while poor earnings in defined contribution plans merely reduce participant retirement income. The employer might therefore be more likely to insist on a high return in the defined benefit plan, while being less concerned about the quality of investment performance in the defined contribution plan.

Performance observed in the TUCS database does not bear out this assumption. Defined contribution plans performed slightly better than defined benefit plans in the last twelve months, and slightly worse than defined benefit plans over the five-year period. In the last year, defined contribution plan earnings were about 70 to 80 basis points higher than defined benefit plan earnings, but over the five-year period, defined benefit plan earnings were 20 to 110 basis points higher, depending on the plan's investment mix (table 2).

Type of Plan Sponsor

The type of plan sponsor has also been suggested as an influence on investment performance. Multiemployer plans, for example, do not have the option of increasing employer contributions if the fund performs poorly. Rather, both contributions and benefits are bargained at set intervals. If this makes multiemployer plans more conservative in their investment management than single-employer plans, one would expect multiemployer plans to have lower investment earnings as a result of this risk aversion.

Union and jointly trusteed funds do display lower investment returns than single-employer plans, but, like the differences among plan types, the differences are neither large nor consistent. Over the last year, the median union and jointly-trusteed fund earned almost exactly the same return as the median defined benefit plan (table 2). Over the five-year period, however, yields in the median union and jointly-trusteed plan averaged 30 to 140 basis points lower than in either defined benefit or defined contribution single-employer plans.

Type of Manager

The type of manager employed by the fund could also contribute to the fund's investment performance. Some differences in performance among types of managers can be observed, but the patterns are not consistent. Over the last twelve months, the performance of funds managed internally or by "captive" subsidiaries significantly exceeded that of funds managed by bank and trust departments or investment counselors (table 3). Over the longer term, however, insurance companies outperformed bank and trust departments, investment counselors, and internal managers. Given the relatively short time period of even the long-run numbers (four or five years, depending on the manager) and the fragmentary nature of the available data, these performance patterns do not show that one type of manager is more effective than another. Rather, they suggest that the individual manager selected is probably more important to the success of the plan than the type of manager selected.

By far the most important determinant of an investor's performance is its asset mix. Among both mutual funds and pension funds, fixed-income funds outperformed both equity funds and balanced portfolios over the last twelve months.

Investment Strategy

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[illegible]

Type of Fund	Short-Run Returns[a]	Long-Run Returns[b]
Bank and Trust Department		
Equity	−0.3%	14.5%
Fixed-income	8.4	10.8
Balanced	5.4	12.5
Investment Counselor		
Equity	−0.4	15.5
Fixed-income	8.3	10.5
Balanced	3.5	13.7
Insurance Company		
Equity	[c]	17.8[d]
Fixed-income	[c]	[c]
Balanced	[c]	15.0[d]
Internal Capital		
Equity	1.6	13.2[d]
Fixed-income	[c]	[c]
Balanced	7.3	11.8

Source: Wilshire Associates, *Trust Universe Comparison Service*, Third Quarter, 1984.
[a]Data for year ending September 1984.
[b]Average value of median rates of return, 1980–1984.
[c]Not available.
[d]Average based on four years' data only.

sion funds, fixed-income funds outperformed both equity funds and balanced portfolios over the last twelve months. Among mutual funds, fixed-income funds earned a negative total return of only 0.1 percent, compared with much higher losses in equity and balanced funds (table 1). Among pension funds, fixed-income funds averaged over 8 percent in total returns (table 2). By contrast, equity mutual funds lost nearly 11 percent and pension funds invested in equities lost as much as 1 percent (table 1).

Over the longer term, however, equity funds outperformed both balanced funds and fixed-income funds. Over the last ten years, equity mutual funds earned about 70 percent more than fixed-income funds, while pension funds invested in equities earned about 50 percent more than those invested in fixed-income instruments. Balanced funds, as might be expected, avoided both the highs and the lows of equity and fixed-income strategies, earning at the middle of the performance range.

Summary

Pension plan asset managers generally agree that there is no reason why pension plan investment performance should be worse than that of other institutional investors. While some funds may perform poorly, this is not true of all. In at least two large groups of pension funds and mutual funds, the differences in performance among pension funds are almost as large as the differences between pension funds and mutual funds in both the long- and short-run.

The most important factor determining the investment success or failure of a pension fund or a mutual fund is its investment strategy. This places a premium on the responsibility of the plan sponsor to design the fund and manage it and on the investment managers to achieve the objectives of both the sponsor and the plan.

How Can Pension Fund Performance be Improved?

While many pension funds outperform both other investors and the market as a whole, the incidence of poor performance among pension funds has concerned policymakers enough to encourage a thorough evaluation of the legislative and regulatory environment of pension funds.

Some of the approaches that have been suggested for improving pension fund performance include:

- revising federal legislation and regulations governing pension fund investment management;

- developing new investment instruments to protect pension funds against unexpected inflation or poor investment decisions; and

- increasing pension fund holdings of alternative—and possibly higher-yielding—investments.

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Federal Regulations

Over the last several years, DOL has been working to simplify the regulatory standards that govern pension fund investment practices. Comprehensive plan asset regulations, currently under preparation, will clarify the standards governing pension plan investment in pooled securities and various participation arrangements, as well as debt, equity, and limited partnership arrangements. These regulations should make it easier for pension plans to invest in real estate, venture capital, and oil and gas partnerships. Venture capital managers are also urging DOL to revise the prohibitions on incentive compensation for asset managers.

Investment managers applaud these efforts as well as the publication of the qualified plan asset manager regulations in 1984. Asset managers do not feel, however, that ERISA has imposed unreasonable restrictions on how they manage their clients' portfolios. Therefore, deregulation of certain investments will not necessarily increase demand for them.

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Index Bonds

Both the Treasury and DOL have recently discussed the establishment of long-term U.S. government bonds that are indexed to the rate of inflation. Short-term Treasury securities are already effectively indexed, since their terms are so frequently renegotiated that the investor's inflation forecast can be constantly updated. Long-term securities, however, can carry significant inflation risk for the lender. If, in turn, their interest rate reflects the lender's inflation forecast, the cost of long-term debt can become prohibitive in an environment of inflationary expectations.

Such bonds would assure investors a specific real rate of return regardless of unexpected swings in interest rates or inflation. An advantage of such bonds for the government would be the fact that when inflation rate expectations lag behind actual inflation trends, the government would not be paying a premium for expected inflation that ultimately does not take place.

Index bonds could probably generate some interest among investment managers as part of a generally active investment strategy. If an investment manager tries to reach an optimal mix of risk and yield, index bonds could probably be used to remove the risk from one segment of the portfolio, freeing the attention of sponsor and manager for actively managing and maximizing yields in other segments of the portfolio.

As a sole or major element of a pension fund's—or any investor's—portfolio, however, index bonds could be less attractive. Currently, AAA corporate bonds are paying 9.8 percent, or 6.5 percentage points over inflation. In the current high real interest rate environment, index bonds would impose high opportunity costs on investors.

Rather than investing in a specialized investment instrument, many managers would prefer to set goals according to the behavior of the market. They prefer to set goals based on alternative market activity scenarios and on the plan's risk tolerance and liability structure.

From a macroeconomic policy point of view, managers are also troubled by the fact that index bonds would protect only one sector from inflation. What makes pension participants the only sector worthy of such protection? All taxpayers would pay higher taxes to protect pension participants in the event of unexpected inflation.

Social Investing

Another option that has been proposed for improving pension-fund investment returns is increasing fund holdings of alternative investments. These investments generally offer not only an investment return, but also achievement of various social goals. Investments falling under this heading include mortgages and mortgage-backed securities, venture capital and small businesses, and reindustrialization of declining industries and declining regions of the country.

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There are at least two different approaches to social investing. One approach would allow pension funds to accept lower rates of return than available on traditional investments, if the investment furthers specific social purposes.[5] Such a strategy could tax pension participants and retirees to pay for social spending that benefits society at large.

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[5] Karen W. Ferguson, "The Advocate's Arguments: A Review and Comment," in *Should Pension Assets Be Managed For Social/Political Purposes?* ed. Dallas L. Salisbury (Washington, DC: EBRI, 1980), p. 99.

Another approach argues that certain alternative investments not only advance social goals but also promise higher returns.[6] Among the investments which may offer significantly better yields than traditional investments, at comparable risk, are housing-related investments and venture capital.

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Social investment strategies as well as innovations like index bonds are partial approaches to the building of an investment portfolio. Alternative investments with social value should be pursued if they fit into an overall strategy.

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Both arguments oversimplify the portfolio manager's task and the social policy issues involved as well. In the first case, if the portfolio manager chooses to accept a lower rate of return on a "social" investment—even if, as some recommend, the participants are consulted and agreed to this choice—the result could be retirement incomes that fall short of what is deemed adequate or what is promised to participants. That this is done in the name of a social goal does not mitigate the consequences.

The second social investing argument represents a somewhat simplistic view of financial markets. Investments have to be compared on many characteristics, including yield, risk, liquidity, maturity, and transaction costs. Markets for financial securities are generally considered efficient. Information about securities flows quickly, securities are traded in large enough quantities to make them liquid, and securities markets are well-linked. The efficiency of markets means that market yields and prices generally reflect investor assessments of each asset's features. Therefore, an investment that offers higher return and lower risk than comparable assets may have other disadvantages involving maturity, liquidity, or transaction costs. Investment managers may want to purchase assets with such disadvantages, but they should do so on the grounds that such assets fit the plan's investment strategy and its needs for yield and liquidity, rather than because these assets serve a social goal that might have nothing to do with retirement income security.

Summary

Debates over alternative investing strategies for pension funds must take into account the role of the investment manager, as well as the obligation of the plan sponsor to manage the managers. Social investment strategies as well as innovations like index bonds are partial approaches to the building of an investment portfolio. Alternative investments with social value should be pursued if they fit into an overall strategy. Investment managers should be accountable to the sponsors who hire them, the participants whose funds they invest, and the broader society at large. But this accountability should not mean that investment managers should make social policy in place of elected representatives.

◆ Pension Fund Investment Practices and Retirement Benefits

If pension funds fail to earn a real rate of return after inflation, their ability to deliver benefits could decline. This decline could come about in two ways:

- increased contributions due to lower investment yields could prompt many plan sponsors to terminate their plans; and

- inflation could erode the real value of pension benefits, increasing reliance on Social Security benefits for retirement income.

Increasing Contributions

The sponsor of a plan returning less than inflation plus the real growth rate will find that over time the plan is an increasing burden on business costs. The sponsor of a defined benefit plan is liable for a specified level of benefits regardless of the plan's performance, so a low return could make increased contributions necessary.

The sponsor of a defined contribution plan does not have to make up any shortfall in investment returns, but over time a poorly performing plan could reduce the plan's compensation value to the employees. This, in turn, could lead to increased pressure for wage increases to compensate for the expectation of poor retirement income. For either sponsor, therefore, poor investment performance could be an incentive to terminate the plan and offer more compensation in cash wages.

Declining Real Value of Benefits

Plan sponsors can enrich pension benefits or protect them against erosion through inflation in one of two ways. One way is to increase the rate at which benefits are earned by changing the benefit formula. This affects only active employees. The other way is to grant postretirement benefit increases, either systematically as a function of the rate of change in the price level, or on an ad hoc basis as funds are

[6] Alicia H. Munnell, *The Economics of Private Pensions* (Washington, DC: The Brookings Institution, 1982), p. 102.

available. Poor investment returns would discourage both types of improvements.

Inflation protection through the benefit formula—defined contribution and defined benefit plans can protect the participant against inflation in different ways.

Defined contribution plans can offer two types of inflation protection. First, since contributions are related to salaries, contributions will reflect inflation during the participant's working career to the same degree that salaries do. Second, since benefits in defined contribution plans depend on contributions plus accrued investment earnings, and since investment earnings generally reflect inflation, the value of the participant's account will reflect inflationary expectations in asset markets. Furthermore, at retirement, the participant can use plan proceeds to purchase an annuity. Since the annuity rate also reflects an inflation forecast, the participant can also receive some inflation protection in retirement.

Inflation protection in defined benefit plans is more complicated. Four approaches can be used to protect the benefits of active participants against inflation:

- computing benefits on the basis of the employee's earnings in the last few years immediately before retirement;

- adjusting the salary base or the benefit accrual rate on an ad hoc basis;

- adjusting benefit accruals for inflation prior to computing the retirement benefit; and

- linking benefit accruals to the market value of the plan's assets.[7]

All but the last method require that the plan actuary incorporate the additional inflation protection into the plan's actuarial assumptions. If investment returns do not exceed inflation plus the real growth rate, the plan sponsor has to make up the shortfall in the form of plan contributions. Inadequate investment returns, therefore, would make it less likely that sponsors would adopt plan design features providing inflation protection.

After retirement, benefits can be protected against inflation in one of several ways:

- linking benefits to asset values;

- automatic cost-of-living adjustments;

- benefit escalation formulas that are independent of inflation;

- ad hoc benefit adjustments; and

- supplements contingent on actuarial gains.[8]

Automatic adjustments and benefit escalation formulas require that the sponsor realize a return at least equal to the real rate of growth plus the inflation rate.

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Low investment returns not only make automatic increases expensive, they also make it difficult for the sponsor to institute faster vesting, earlier retirement, or reduced integration with Social Security.

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If the benefit increase is granted automatically, the plan recognizes this added cost as an increase in actuarial liability. The sponsor must set aside funds in each time period to fund this liability in accordance with the actuarial method used by the plan. Because this way of granting benefit increases raises the sponsor's out-of-pocket costs, only an estimated 3 percent of all defined benefit plan participants are in plans providing such increases.[9] Low investment returns not only make automatic increases expensive, they also make it difficult for the sponsor to institute faster vesting, earlier retirement, or reduced integration with Social Security.

If sponsors grant cost-of-living benefit increases on an ad hoc basis, the increases are often a function of the plan's actuarial gains, that is, investment returns that exceed the return assumed in the plan's actuarial forecast. About 51 percent of all defined benefit plan participants are in plans that offer post-retirement benefit increases on an ad hoc basis.[10] This is a relatively painless way for the sponsor to grant an increase, since the funds do not have to come from the sponsor's current earnings. Unexpected investment returns cannot occur continuously, however, because ERISA requires that the plan actuary use the best and most realistic estimate of investment

[7] Dan M. McGill, *Fundamentals of Private Pensions* (Homewood, Ill.: Richard D. Irwin, Inc., 1984), pp. 206-210.

[8] Ibid., pp. 218-229.

[9] U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in Medium and Large Firms, 1983* (Washington, DC: Government Printing Office, 1984), p. 12.

[10] Ibid.

returns in valuing the plan. Accordingly, plan sponsors cannot count on unexpected investment earnings as a routine way to maintain the real value of pension benefits.

◆ Conclusion

Pension plan investment managers handle the largest single pool of funds available for investment. The management of these funds concerns all segments of the economy. Poor investment returns can increase the cost burden of the plan on the sponsor, erode the retirement income value of benefits, and ultimately increase reliance on the Social Security program for retirement benefits. Therefore, if plan investment returns are inadequate, the taxpayer will pay the costs.

As plan sponsors and investment managers deal with these issues, what can DOL do to help?

Continue Deregulation

The process of clarifying and modifying ERISA's investment standards has been going on for some time. Most investment managers applaud efforts to streamline these standards, making them clear, easy to comply with and enforce, and applicable to a wide variety of investment circumstances.

A recent DOL proposal could take this process further. DOL has requested public comments on a proposal to establish an ERISA self-regulatory organization (SRO) that would serve as a source of expertise in the exemption process, aid DOL in developing class exemptions from the prohibited transactions provisions in ERISA, and possibly act as a disciplinary authority that could compel adherence to its standards.[11] This organization could be modeled on similar private-sector organizations in the securities and accounting disclosure fields. Under the Securities Exchange Act of 1934, the National Association of Securities Dealers (NASD) promulgates, maintains, and enforces a code of business ethics among over-the-counter brokers and dealers. NASD is registered with the Securities and Exchange Commission and performs its regulatory functions under the Commission's active oversight. The Financial Accounting Standards Board (FASB) establishes accounting standards for the accounting profession and also functions under the Commission's oversight.

If the establishment of such an organization were feasible, it could offer many advantages to DOL as well as to plan sponsors and investment managers. Currently, the exemption process can consist of as many as eight or more phases or steps, all designed to guarantee that DOL has adequate information for making a decision and that the applicant receives a fair hearing. Requests for exemptions can therefore take many years to clear through the process. Private-sector input in this process could expedite the progress of exemptions since an SRO could draw directly on experts in the affected industry to determine whether the exemption request is valid and consistent with industry practice. At the same time, the organization would not be able to approve all applications indiscriminately since DOL would retain final jurisdiction over applications.

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Managers agree that the best-performing plans are those in which the sponsor actively makes these decisions rather than delegating them to asset managers or avoiding them entirely.

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Let Sponsors and Managers Set Investment Policies

Deregulation is different from setting investment policies for investment managers. If regulatory agencies make it easier for pension plans to invest in mortgage-related securities, venture capital, or other assets, the evidence is that some plans will take advantage of such opportunities. Such innovations, however, are not a substitute for an integrated portfolio strategy. The sponsor still has to make the hard decisions that determine the plan's goals and how they are to be fulfilled. Managers agree that the best-performing plans are those in which the sponsor actively makes these decisions rather than delegating them to asset managers or avoiding them entirely.

Learn from the Winners

DOL's funded study *Investment Practices and Performances of Private Pension Plans* represents the beginning of a much-needed effort to examine the record of both the poorer and the better performers. While some pension plans are performing poorly, others are not. Information on the reasons for differences in performance is sorely needed. While many pension plans subscribe to private performance evaluation services, the disclosure data filed with DOL on form 5500 represent the only universal source of performance, funding, and other data on pension plans. Lack of funding has delayed the release of recent data to the public. The availability of these data would not only improve the information base for making public policy decisions, but would also aid sponsors and managers in improving their performance. DOL should give the processing of this database the highest priority.

[11] *Federal Register*, 49, no. 238, 10 December 1984, 48111.

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