

Clearing the Air

Proponents of a privatized state retirement system make a lot of sensational claims about the state of our public retirement system. Many simply don't stand up.

"Public employee benefits are bankrupting state and local government."

- ***The market collapse is the primary cause of the fiscal woes.*** 70% of the increased employer costs to CalPERS between 2000 and 2004 is attributable to the market collapse – roughly \$1.7 billion of the \$2.4 billion difference.
- ***Employee benefit increases are only a fraction of the problem.*** Only 20% of the pension increase can be laid to increased benefits.
- ***Employer contributions may go down in future years.*** The pension fund's return on investments rebounded to 17% in 2004. This rebound will be reflected in state and local budgets beginning in 2006. (CalPERS)

"Taxpayers are footing the bill for public employee pensions."

- ***Taxpayers pay only a fraction of the tab for public employee pensions.*** Seventy-five percent (75%) of CalPERS' total worth comes from investment income. Only 12% of the CalPERS funding comes from state and local budgets. (CalPERS)
- ***Employees are paying more of the tab than employers.*** Over the last two decades, the workers have paid 13% of the cost, vs. 12% that comes from state and local budgets. (CalPERS)

"Public employee pensions are too generous."

- ***California only slightly above the national average.*** In 2003-2004, the average monthly retirement check in California was \$1,591 (\$19,092 per year). The national average is about \$1,500. (CalPERS). That's only about \$500 above the federal poverty line for a family of four (\$18,500 in 2004).
- ***No Social Security safety net for many.*** Unlike the private sector, many public employees do not pay into Social Security, and do not receive Social Security benefits.

"A two-tiered retirement system will mean more money for schools, roads and health care."

- ***No impact on budgets for 10 to 20 years.*** The main legislative advocate for privatized pensions admits it could be decades before there is any budget savings.
- ***Little if any impact for years beyond.*** A CalPERS analysis concludes that, in a best-case scenario, the potential savings for the first decade would amount to \$34 million -- 03% of the current \$100 billion state budget. (CalPERS estimate)

- **No guarantee that taxpayers will benefit from savings.** Nothing in the measure guarantees that savings will be used for schools, roads, health care, etc.

“A privatized retirement system provides fiscal stability for government.”

- **Higher cost to manage the system.** The overhead cost of the average defined contribution plan is 2% of assets. CalPERS’ average cost is 0.18%. (CalPERS). Over time, additional costs could run in the hundreds of millions per year.
- **Fees charged on investments drive up costs.** Mutual funds charge, on average, \$1.35 for every \$100 invested. CalPERS’ rate is about 18 cents per \$100 invested.
- **Cost of existing pension plan will rise.** Without new, younger employees paying into the system, the existing plan will have fewer assets to invest, driving up costs.
- **Short-term costs will be higher.** Cost of setting up system and two-tiered retirement system means higher costs in short term.
- **Potentially huge long-term cost to public safety net.** The rise of defined contribution plans has created a gap between retirement income and projected expenses that’s expected to grow to \$45 billion by 2030. (EBRI) There’s a big bill coming to the states to pay for under-funded retirements, and this will just make that bill that much bigger.

“Money paid into employee pension system benefits only the employees, not taxpayers.”

- **Taxpayers benefit from higher-quality public servants.** Public service pensions attract high-quality workers (police, fire, nurses, IT professionals, etc.), who would otherwise make more money in the private sector.
- **Taxpayers benefit from a more experienced work force.** Employees under traditional pensions are less likely to go job-shopping, and more likely to continue growing within public service.
- **Taxpayers benefit from the pension system’s size and strength.** CalPERS invests between \$17 billion and \$18 billion directly into the California economy.
- **Taxpayers benefit from pension clout.** CalPERS and CalSTRS forces corporations to take California’s needs and values into account in financial decisions.

“The private sector is moving toward defined contribution plans.”

- **Large employers still overwhelmingly offer traditional pensions.** 83% of Fortune 100 corporations offer a traditional pension plan – only 17% offer defined contribution exclusively. 69% of corporations on the Standard and Poors 500 offer traditional, defined benefit plans. (Watson-Wyatt)
- **Trends show traditional plans on the rise among large employers.** From 1985 to 2002, companies with 10,000 or more employees offering traditional

pension plans went up, not down, even through an era of dramatic corporate mergers and market volatility. (EBRI)

- **Increase in DC largely among small companies.** Virtually all of the shift away from defined benefit plans since 1992 took place among employers with fewer than 250 employees. (NASRA)

“The public sector is moving toward defined contribution plans.”

- **The stock crash killed the DC movement in other states.** Since 2000, no new states have enacted a defined contribution plan. (Governing Magazine)
- **Jurisdictions that tried DC plans are switching back.** Nebraska recently dropped its 40-year defined contribution system. The City of Irvine recently re-entered CalPERS after trying DC.

“Individuals can do a better job of managing their money than the pension professionals.”

- **All the evidence points the other way.** An exhaustive study of Nebraska’s abandoned system showed a return of 6-7% for defined contribution vs. 11% for traditional pension plan (Governing Magazine)
- **Defined contribution plans produce lower rates of return.** Over last 11 years traditional pensions outperformed defined contribution plans. The difference was especially marked during the 2000-2002 bear market (Watson Wyatt)
- **Move away from traditional pensions creating a retirement income gap.** Gap could grow to \$45 billion nationally by 2030 – a “demographic ticking time bomb.” (EBRI)

Sources: CalPERS, Employee Benefit Retirement Institute (EBRI); National Association of State Retirement Administrators (NASRA); Watson-Wyatt Investment Surveys 2002, 2004. Governing Magazine, March 2004 – “Pension Pendulum”