California state workers' pensions under assault

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6 December 2010

The California state budget, passed in early October, mandates brutal cuts to social programs as well as pension plans. Governor Arnold Schwarzenegger made "pension reform" a precondition before approving any budget plan. California's budget deficit is now estimated to be $25.4 billion, a far larger number than state officials originally estimated. An offensive is now under way to blame California's fiscal crisis on pensioners and retirees and make them pay for the deficit.

Before signing the October 21 budget bill into law, Schwarzenegger once more attacked pensioners saying, "Pension debt has become the silent thief of our treasury, robbing vital programs such as education, parks, public safety and environmental protection. With this reform, we will put California on the road to fiscal health."

As result of the latest budget agreement, the California Public Employee Retirement System (CalPERS), the largest pension fund in the US, will see a one-time 3 percent wage increase in exchange for a yearly 3 percent contribution from pensioners, in addition to a five-year increase in the retirement age. Also, the budget stipulates that pensions will now be based on the last three years of employment instead of the pensioner's highest paid year of employment.

The new stipulations will cut $100 billion from state pensions over the next few years and roll back some pension benefits that were approved by the state legislature in 1999 in a law known as SB 400, which expanded pension benefits and allowed public employees to calculate their pension benefits based on the years immediately preceding their retirement.

A two-tier system, with reduced benefits for newly hired state workers, is now in effect. Many factors contributed to this attack on pensions, not the least of which was the backroom dealing between the governor and the unions, particularly the Service Employees International Union (SEIU). The SEIU cynically tried to position itself as a force that the governor could bargain with in carrying out these cuts.

On November 9, 95,000 SEIU members voted for pay cuts after the union presented the vote as the only way to prevent furloughs. SEIU Local 1000 President Yvonne Walker boasted, "We've done our part to get the state through this unprecedented budget crisis." Thus, the unions have demonstrated their willingness to implement brutal austerity measures with the government.

As a result of the vote, all workers' contributions will increase by 3 percent. Current workers may retire at age 55 with pensions equal to 2 percent of their pay for every year they work, while newer workers may not retire with these benefits until they are 60. Furlough days have essentially been institutionalized.

The second major factor in the calls for pension "reform" has been the huge budget deficits CalPERS has incurred as a result of its enormous investment losses during the 2008-2010 financial crises. The state currently is struggling to pay $75.5 billion in pension obligations; $40.5 billion for the teachers' retirement plan, the California State Teachers' Retirement Plan (CalSTRS), and $35 billion for the CalPERS fund.

These deficits however, are based on numbers calculated before June 2008, before the worst financial losses for the fund took place. As of this month, CalPERS has fallen to $200 billion in assets as a result of its ill-placed investments on Wall Street, while CalSTRS has dropped to $134 billion. To make matters worse, when CalPERS set aside money for future pension obligations, they based their figures on overly optimistic investment returns at 7.75 percent or 8 percent while the stock market saw zero growth and thus could not meet these obligations.

When current market values are taken into account, the gap between existing plan benefits and actual plan benefits grows from $282.2 billion to $326.6 billion. The California controller has also estimated that retiree health benefits are underfunded by $51.8 billion, bringing the total pension deficit to $378.8 billion.

The pension crisis will only worsen as the years go by. According to a study released by the Milken Institute, the combined pension liabilities of CalPERS, CalSTRS and the University of California Retirement System will exceed the state's annual tax revenue by 550 percent by 2012. The report calls for the pensions to move away from defined benefit plans to a hybrid of "partial defined" benefits and a partial 401-k-type coverage for newer retirees. Employee contributions will have to increase substantially, in addition to an increase in the retirement age. These are the same proposals that Governor Schwarzenegger requested in a 2005 bill, but was unsuccessful in passing.

Among other findings the report noted that by 2009 pension liabilities cost every working-age adult in California $3,000, and by 2014 will cost every Californian $10,000. The study also noted with alarm that the average pensioner put in 25 years of work for an average of 26 years of benefits. From the standpoint of the ruling elite, pensioners and retirees are simply living too long and costs need to be brought down in order to curb the state deficit and satisfy investors.

In tandem with this all-out assault on public pensions is a vicious propaganda campaign aimed at exposing the supposed lavish benefits that these “grossly overpaid” state workers receive. However, according to a study commissioned by the University of California Berkeley Center on Wage and Employment Dynamics, state workers are paid 7 percent less in wages than their counterparts in the private sectors. Even though their benefits are nominally better, there is no “significant difference” between the two. In fact, state workers in California work more hours every year than private workers do. It should also be noted that these numbers are based on pre-furlough figures.

Now these same pensioners who saw their life savings gambled away on the stock market by top CalPERS officials turned Wall Street investors—three of whom are the subject of a state lawsuit for accepting bribes from their well-connected clientele—are now being asked to foot the bill. This outcome is a direct result of the SEIU’s negotiations with the governor and their subordination to the Democratic Party.

Far from an aberration, many CalPERs board members, including Phil Angelides (state treasurer from 1999 to 2007), Willie Brown, and Steve Westly (state controller, 2003-2007), are prominent Democrats who pursued free-market policies when making investments for the fund. Even though many of these investments were shortsighted and cost CalPERS and CalSTRS pensioners billions of dollars on Wall Street, the Democratic Party was behind them all along. The shareholders’ power and influence over CalPERS continued to undermine the interests of the workers during this time.

On November 16, the *Los Angeles Times* reported that one of CalPERS’ financial firms is the subject of an ongoing investigation by state officials and that the newspaper has requested the pension fund to disclose thousands of documents relating to this investigation, which may uncover fraudulent business deals and “improper relationships” between investors and CalPERS board members.

In line with these corruption scandals are moves on the part of the CalPERS board to further privatize the fund. The investment committee of the fund recently approved a new framework for allocating assets that would combine private and public equities in a new growth category. Two new classifications were also created. The real assets category now includes infrastructure, forestland and real estate while the inflation-linked assets include inflation-linked bonds, commodities and TIPS.

Another move to subordinate pensions to the free market is the decision by CalPERS on November 15 to drop its annual “Name and Shame” list of underperforming companies with which CalPERS engages. Instead the fund will conduct private negotiations with these companies unbeknownst to shareholders and pensioners.

The assault on pensions in California is no doubt being seen as a template for the rest of the US. In the first 10 months of 2010, 19 states enacted pension reforms that would reverse defined pension obligations with increased employer contribution rates, raised retirement ages, and reduced benefits, according to the Pew Center on the States. Many more states will move to bring down pension costs in the coming year as new governors and legislators from both parties arrive in office to proclaim austerity measures. In 2009, 11 states made such changes, compared to eight states in 2008.

Retiree health benefits will also be severely affected as states begin to bridge the gap between pension benefits that were promised and the actual money set aside for these plans. In a February 2010 report entitled “The Trillion Dollar Gap”, the Pew Center estimated that in fiscal year 2008 states and localities underfunded their pension liabilities by $452 billion and owed another $555 billion for retirement health care, bringing the total shortfall to $1 trillion.

Democratic Attorney General Jerry Brown will now assume the office of governor and has made clear his determination to decimate the pension systems. On his web site, Brown not only gave his approval to the new pension reforms, but also said he would have employers contribute more to their pension plans and force new workers to work longer and retire later in life to receive their benefits.

Brown revealed to the *Sacramento Bee*, “I think a defined pension plan can be very good, but it has to be actuarially sound, and that means you have to contribute. And right now because the stock market is going down it’s not as buoyant as it once was.” The SEIU not only called on its members to vote for Brown but provided his campaign with millions of dollars in dues.

President Obama’s bipartisan budget deficit panel seeks to ram austerity measures in the form of cuts to Social Security, Medicare and state pensions. In the aftermath of the November elections, the government is hell-bent on making workers pay for the economic crisis and the budget shortfalls. The unions will be essential in carrying out these attacks.