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## Opinion



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### Daniel Weintraub: Pension fund ills can be traced to big giveaway

By Daniel Weintraub -- Bee Columnist  
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The public pension nightmare unfolding across California began with one bad decision based on faulty logic in the heady days when the stock market run looked as if it would never end.

The decision came when the board of the California Public Employees Retirement System (CalPERS) urged the Legislature and the governor to take \$9 billion that was deemed a surplus and use it to boost pensions for retirees and those still working for the state.

Those excess earnings in the retirement fund, the pension board concluded, belonged to employees and retirees. But the board was wrong. The state never should have given that money away.

Now, with the stock market depressed and the surplus gone, the pension fund is turning to

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taxpayers to keep it solvent. The state next year will owe more than \$3 billion to the fund -- twice what taxpayers paid in this year. And the same story has begun to play out in cities and counties across California that followed the state's lead and gave big pension increases to their workers.

The investment losses would have been difficult to absorb under the best of circumstances. But by giving away the surplus, the state pension board compounded its problem.

To understand why the pension managers' logic was so flawed, consider the nature of the public employee retirement program.

Called a defined benefit, the workers' pensions are guaranteed, inviolable as a contract. The employee pays in a certain amount, typically 5 percent of salary, and in return is assured a pension for life, along with an annual cost of living increase after retirement.

The employers, in this case the taxpayers, also pay into the retirement fund -- in an amount determined annually by the pension system's board. If investment returns lag, the taxpayers are bound by law to make up the difference with higher contributions. Employees and retirees bear none of the risk.

Thus, when the reverse happens, and the pension fund generates excess earnings, those dollars can and should be held in reserve as insurance against the day when earnings fall again. If the gains are big enough, they also can be used to reduce the taxpayer contribution to the plan, as long as the fund remains actuarially sound, able to pay all of its obligated

liabilities.

Such defined benefit plans differ from the increasingly common private sector alternative, the defined contribution plan, the best known of which goes by its Internal Revenue Service name: 401(k). In these plans, the worker bears all of the risk associated with his or her investments. If the investments go poorly, the retiree is left with less money to live on. If the investments do well, the employee, having absorbed the risk, gets all the reward.

But in 1999, with the stock market booming and the taxpayers' required contributions to the pension system declining, state employees demanded a share of the windfall.

"We had 16 years of Republican administrations where benefits had not been improved," said Casey Young, who was then CalPERS' liaison with the Legislature. "You had the labor folks basically saying, 'We haven't had any improvements for a long time. Employers got all the benefit of the run-up in the stock market. It's just not fair.' "

Ron Seeling, the chief actuary for the system, said the benefit boost was a natural move for the labor-dominated pension board.

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"These board members, at least six of them, were elected from within the members of this system, and you've got some of the politicians who sit on our board, elected by virtue of the support of some of the unions, and they're representing their constituents," Seeling said. "They're representing the members of this system the best they see fit."

At the time, most state workers already were able to retire at age 60 with 2 percent of their salary for each year worked, or 60 percent for a 30-year veteran of state employment. That benefit was far richer than most private sector workers get. Highway Patrol officers could get 2 percent for each year worked at age 50.

The new benefits would allow regular employees to retire at 55 with the same benefits they used to get at 60. Highway Patrol officers were given a 50 percent increase in their pensions.

The board also urged lawmakers to approve an extra cost-of-living increase for those already retired and to phase out a leaner, cheaper retirement plan the state had adopted in the early 1990s to control pension costs.

But because the state and its workers had been paying all along to finance only the lower benefits, the increases created a huge unfunded liability overnight. Together, the changes were expected to cost about \$7.7 billion up front. That figure later climbed to \$9 billion. CalPERS' leaders assured lawmakers and the public that the retirement fund's surplus was so big that it could absorb this hit and keep rolling.

"This is a special opportunity to restore equity among CalPERS members without it costing a dime of additional taxpayer money," the board's president, William Crist, said when the benefit package was approved in 1999.

Crist could not have been more wrong.

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#### About the Writer

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