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## Daniel Weintraub: Governor's pension proposal on the right track

By Daniel Weintraub -- Bee Columnist  
Published 2:15 a.m. PST Tuesday, January 13, 2004

Gov. Arnold Schwarzenegger's instincts on public employee pensions are correct. The only problem with his proposal to rein in the cost of the state's retirement system is that it doesn't go far enough.

Schwarzenegger recognizes that the state went overboard in 1999, when the Legislature and then-Gov. Gray Davis agreed to use a big projected surplus in the retirement fund to goose pensions. Lawmakers were told that the fund was so flush with stock market earnings that the benefit increase would be essentially free, and that costs to taxpayers for the overall retirement program would remain low for years.

Public safety workers were the big winners. They now retire with 90 percent of their salaries after 30 years on the job. But other workers also scored: They

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effectively won a reduction in their retirement age from 60 to 55, when they can retire with 2 percent of their salary for every year they worked for the state.

The package also repealed a lower cost, no-frills retirement benefit in place since 1991 for all newly hired state workers. That second-tier retirement program was costing taxpayers roughly half of its more generous counterpart, even though employees were not required to contribute to their own pensions. Now, everybody goes into the pricier plan.

But when the stock market went south, the taxpayers had to step in and make up the difference, not only for the reduced earnings in the pension fund but for the higher benefits as well. That double-whammy has resulted in the annual cost for retirement climbing from an artificially low \$160 million in 1999 to more than \$2 billion today.

It's the same story throughout state government: programs were created or expanded at the height of the boom, as if revenues would continue to grow at that rate forever. Now the new governor and the Legislature have to decide which programs to sustain and which ones the state can no longer afford.

The problem with the pension changes, though, is that there exists an implied contractual obligation to the workers who were granted the higher benefits. Some might have made life-changing decisions based on the promise of a more lucrative retirement, turning down jobs elsewhere, for example, or buying an expensive new home.

For that reason, Schwarzenegger won't try to reduce benefits to workers already on the payroll. Instead, he wants to increase the premium most employees pay into the pension system, from 5 percent of their salary to 6 percent.

But even though his hands are relatively tied when it comes to current employees, the governor isn't ignoring the problem. He is proposing that the lower-cost benefit package be revived and given to all employees hired from now on.

Schwarzenegger's proposal, then, is a fiscal mirror image of many of the changes adopted during the Davis years. Its short-term payoff would be minimal. But in the long run, long after Schwarzenegger and today's Legislature have left the scene, the reform would pay big dividends to the taxpayers.

The Department of Finance estimates that the proposal would save the general fund about \$20 million in the first year, growing to more than \$200 million by 2010 and, eventually, to nearly \$500 million a year.

But precisely because the change would take years to bear fruit for taxpayers, it's going to be difficult to enact. Lawmakers under great pressure from

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employee unions will not want to cast a difficult vote for a change that won't do much good until after they have left office.

Partly for that reason and partly out of fiscal necessity, Schwarzenegger has proposed to couple the proposal with a bond measure to cover a portion of the state's retirement obligation until the savings begin to kick in. By the third year, the savings would exceed the debt service on the bond, and over the life of a 20-year bond, the net benefit to taxpayers would be \$4.6 billion.

The governor is on the right track. But instead of returning to the second-tier benefit package that was in place for new hires before 1999, Schwarzenegger should be bolder. He should propose, for new employees, ending the traditional defined-benefit pension plan, where workers are promised (and limited to) a particular benefit no matter how well or how poorly the pension fund's investments perform.

Instead, the state should offer new hires a defined-contribution plan similar to what many private-sector employees now enjoy. Workers could put in 5 percent from their paychecks, the state could match that amount, and employees could be given choices in how they wanted to invest their money.

That would give the taxpayers certainty about the size of our obligation to employee retirement while giving workers control over their own savings. It would also make the pension benefit portable, allowing those workers who leave state service after a few years to take their savings and earnings with them rather than forfeiting the money to the state.

It would be a modern and sensible plan with advantages both to the employees who work for the state and the taxpayers who pay for their salaries and retirement.

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#### About the Writer

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