

## **LITTLE HOOVER COMMISSION (LHC) JUST THE FACTS ABOUT RETIREMENT SECURITY**

**LHC Claim:** Treated like another speculative house during the boom, the state allowed public agencies and employees to pull equity in the form of increased retirement benefits from the pension funds whose value was inflated by optimistic market return estimates. The retirement promises that elected officials made to public employees over the last decade are not affordable, yet this is a mortgage that taxpayers cannot walk away from easily.

**FACT:** The type of rhetoric contained in this report is inappropriate for any serious balanced discussion of this issue and demonstrates a complete lack of understanding of the principles of retirement systems.

**LHC Claim:** Even the “teaser rates” reflecting aggressive investment assumptions are re-setting, revealing a higher cost to maintain a level of benefits that have become more generous than reasonable.

**FACT:** The investment assumption rate (7.75%) used by CalPERS and others has been well below the actual return rate of more than 8.6 % in 15 of the last 20 years.

**LHC Claim:** Public agencies face the prospect of increasing required contributions into their pension funds by 40 to 80 percent of their payroll costs for decades to come.

**FACT:** There is no empirical data to support this contention.

**LHC Claim:** Public employees might appear to have little incentive to push for reforms...

**FACT:** Public employee groups supported a broad range of reforms in 2010, many of which were vetoed by Governor Schwarzenegger. The state employee groups agreed to roll backs, second tiers, and increased pension contributions that saved the state over \$400 million in the last budget alone.

**LHC Claim:** Pension costs will crush government.

**FACT:** The entire costs of pensions for the state in 2011 will be \$3.5 billion out of an \$85 billion budget. If we paid zero into public employee pensions and eliminated them altogether, we would not come close to solving the budget deficit.

**LHC Claim:** In another five years, when pension contributions from government are expected to jump and remain at higher levels for decades in order to keep retirement systems solvent, there will be no debate about the magnitude of the problem.

**FACT:** The state and local governments are actually paying less as a percentage of their payrolls today than they were in 1980.

**LHC Claim:** The minimum retirement age has dropped to 55.

**FACT:** This is patently false. The formulas were changed, but the minimum retirement has always remained the same (age 50 with 5 years of service credit). The fact is that the average retirement age for a state and local employee is age 60 with over 23 years of service.

**LHC Claim:** Banking on high fund returns and an aggressive investment strategy, employers and employees also have failed to contribute sufficiently.

**FACT:** Every actuarial assumption prior to the market meltdown was within industry standards. In fact retirement systems maintained more assets during the market collapse than virtually every other financial institution. Banks collapsed, brokerage houses disappeared, the entire industry had to be bailed out yet retirement funds still maintain nearly 70% (sufficient funding according to Fitch rating services) of the assets needed to meet their future obligations.

**LHC Claim:** Today, the state’s largest pension systems are dangerously underfunded.

**FACT:** In 1980 when the state was paying 3% more than they are in 2011 for the employer contribution, the fund was only 50% funded. Less than a decade later, most funds were nearing 100% funded.

**LHC Claim:** The retirement systems invest aggressively to help workers accumulate wealth ...

**FACT:** The average PERS retirement is \$2,500 per month. That hardly meets the standard of wealth.

**LHC Claim:** With needed reforms, defined-benefit pensions can remain a core component of public employee retirement plans. The problem, however, cannot be solved without addressing the pension liabilities of current employees. The state and local governments need the authority to restructure future, unearned retirement benefits for their employees.

**FACT:** The collective bargaining system has worked in California. The state and over 90 local jurisdictions have gone to the table and negotiated reductions and increased contributions. The Commissions reward for good faith bargaining is to eliminate the collective bargaining rights of public employees.

**LHC Claim:** Freezing earned pension benefits and re-setting pension formulas at a more realistic level going forward for current employees would allow governments to reduce their overall liabilities.

**FACT:** This demonstrates a complete lack of understanding about how pensions work. Freezing benefits would do nothing to reduce unfunded liabilities and only impact future liabilities which are currently being funded.

**LHC Claim:** The 401(k) element is risk-managed to protect employee investments from market volatility in order to generate an adequate retirement income.

**FACT:** This model has proven to be inadequate for the first generation of retirees who are now reaching retirement age with nothing more than a 401K retirement plan. A recent Wall Street Journal article reported that this new generation of retirees is reaching retirement age with less than 25% of what is needed to maintain the median income in the United States.

**LHC Claim:** Roughly half of all public employees in California do not participate in or receive Social Security benefits, so many public employees rely more heavily on state and local governments to provide larger retirement benefits. Serious consideration must be given to extending Social Security to non-covered, public-sector workers, toward the goal of building a three-part retirement strategy as has the federal government.

**FACT:** While this may seem like a good idea, it would immediately add 6.2% to the employer and employee contributions making the Commission proposal more expensive, not less than current plans.

**LHC Recommendation:** The Legislature should give state and local governments the authority to alter the future, unaccrued retirement benefits for current public employees.

**FACT:** Eliminating the collective bargaining process and renegeing on the promises made to workers who have devoted a lifetime to public service.

**LHC Recommendation:** State and local governments must slow down pension costs by controlling payroll growth and staffing levels.

**FACT:** At virtually every bargaining table there are reductions, furloughs, and increased contributions for employees. Employees are the single largest partner in reducing state and local government budget deficits.

**LHC Recommendation:** The Legislature must create pension options for state and local governments that would retain the defined-benefit formula – but at a lower level – combined with an employer-matched 401(k)-style defined-contribution plan. The 401(k)-style component must be risk-managed to provide retirement security and minimize investment volatility.

**FACT:** Hybrid plans do not reduce volatility. They only shift the volatility to the workers. They have thus far proven inadequate in providing the security and sustainability that is professed in this report.

**LHC Recommendation:** Set appropriate pension eligibility ages to discourage early retirement of productive and valuable employees.

**FACT:** The current average retirement age for employees is 60 (55 for public safety), the new tiers negotiated at the state and local level are expected to add an additional 5 years. Is it the Commission's intention to require workers to work into their 70's?

**LHC Recommendation:** Set a tight definition of final compensation, computed on base pay only, over a five-year average to prevent and discourage pension "spiking." Set uniform standards for the maximum hours that retirees can return to work and continue to receive public-sector pensions.

**FACT:** Labor supported these proposals in bills that were vetoed last year.

**LHC Recommendation:** Restrict pension allowances to exclude service in an elected office. Eliminate the purchase of "air time."

**FACT:** These proposals have de minimis impact on the funding of retirement systems, but employees have demonstrated a willingness to bargain the elimination of similar provisions.

**LHC Recommendation:** The Legislature must prohibit employees and employers from taking contribution "holidays," except under rare circumstances.

**FACT:** Employees have long supported this proposal since; they have never experienced a pension holiday. The employee contribution is statutorily required regardless of the funded status of the system.

**LHC Recommendation:** The Legislature must prohibit retroactive pension increases

**FACT:** This is a subject of ongoing litigation and the Commission's insistence that the Legislature intervenes on behalf of Orange County, again demonstrates the conservative bias of the Commission report.

**LHC Recommendation:** State and local governments must explore options for coordinating pension benefits with Social Security.

**FACT:** This represents an increase of 6.2% of payroll contribution for both the employee and employer above and beyond the increased costs of closing or freezing the existing pension plans. The combination could potentially eliminate any perceived savings from the hybrid/social security plan.

**LHC Recommendation:** The Legislature must require government retirement boards to restructure their boards to add a majority or a substantial minority of independent, public members to ensure greater representation of taxpayer interests.

**FACT:** The Board composition includes two statewide elected officials who are accountable to the taxpayers, three appointees of the Governor or local agencies that are accountable to the taxpayers, and members elected from the membership of the systems who are all taxpayers.

**LHC Recommendation:** All proposed pension increases must be submitted to voters in their respective jurisdictions.

**FACT:** The Commission seems compelled to restrict every opportunity for the collective bargaining process to work and ensure that employees who bargain in good faith can have their benefits taken away by the employer.

**NOTE:** *This document does not cover the full scope of claims or recommendations included in the Little Hoover Commission Report, rather it addresses the most egregious and unfounded claims and exposes the truth about the LHC recommendations. The full document may be viewed at <http://www.lhc.ca.gov/studies/204/report204.html>.*