

State Retirement Benefits: Approaches and Solutions



Legislative Analyst's Office

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State Retirement-Related Costs

2007-08 General Fund (In Billions)

CalPERS	\$1.5
CalSTRS	1.1
State Retiree Health	1.1
UC—Pension	—
UC—Retiree Health	0.1

State Programs— Funding Situations

	Normal Costs	Unfunded Liabilities	
	Funded?	Amount (In Billions)	Addressed?
CalPERS	Yes	\$15	Yes
CalSTRS	Yes	20	No
State Retiree Health	No	48	No
UC—Pension	N/A	—	—
UC—Retiree Health	No	12	No

Problems—Financial

- **Large Unfunded Liabilities**
- **Creating New Unfunded Liabilities**
 - Primarily retiree health
- **Volatility of Payments**
- **Public Employers Assume Almost All Risk**

Problems—Benefit Design

- **May Not Be Meeting Employee Needs**
- **May Not Be Meeting Employer Needs**
- **Nature of Employer Commitment**

Basic Considerations

- **Total Compensation**
- **Personnel Considerations**
- **Governance Issues**
 - CalSTRS
 - UC

Recommendation— Pay for Benefits as They Accrue

- **This Fundamental Public Finance Tenet Suggests Specific Actions**
 - State payments for normal costs of retiree health care (almost \$800 million annually).
 - Some action may be needed on CalSTRS and UC.

Paying for Accrued Benefits— A Corollary

- **We Would Also Urge the Legislature Not to Grant Retroactive Benefits**
 - Violates the basic tenet.
 - Granting of additional benefits during “good times” can not be offset by reducing benefits during bad times.

Recommendation— Address Unfunded Liabilities

- **Not as Clear as to Who Should Pay for “Past Sins.”**
- **However, Current Generation of Taxpayers Is Partly Responsible for the Obligations.**
- **We Believe a Fairly Long Amortization Period—30 Years—Is Reasonable.**

Addressing Unfunded Liabilities— Fiscal Implications

- **Additional Payments Needed to Amortize Unfunded Liabilities Over 30 Years:**
 - Retiree health—\$450 million a year.
 - CalSTRS—almost \$900 million a year.
 - UC retiree health—several hundreds of millions of dollars a year

Pension Benefit Design— Consider More Plans

- **Key Consideration:
What Kinds of Retirement Benefits Will
Attract and Retain Employees?**
- **Current Approach—
Employer Contributions Provided Only for
Defined Benefit Plans—May Be Too
Inflexible**

Illustration— More Flexible Pension Plans

- **State Could Contribute a Fixed Amount to All Employees, Who Would Choose Between:**
 - Defined benefit plan.
 - Defined contribution plan.
 - Hybrid.

Similar Concerns— Retiree Health Benefit Design

- **Current Plan Has Little or No Benefit to Many State Employees**
 - Almost one-half leave state service before any vesting.
- **Huge Uncertainty for State as to Future Health Costs**

Illustration— More Flexible Retiree Health Plans

- **Provide State Contribution to Health Savings Plans**
- **Could Be Geared Toward Providing Similar “Medi-Gap” Coverage**
- **Other Ways of Assisting Employees**
 - Access to state pool.

Increase Legislative Control

- **For All Future Employees,
We Recommend the State:**
 - Be explicit as to benefits to which it is committing.
 - Reserve the right to adjust benefits in future years.

CalSTRS—Governance Issues Complicate State Action

- **State Involvement in Local Compensation Issues**
- **Huge Unfunded Liability**
- **Normal Costs Not Specifically Allocated**

CalSTRS—Possible Approaches

- **First: Clarify State and Local Roles**
 - We recommend that, for future employees, the responsibility lie at the local level.
- **Second: Encourage Flexibility in Design**
 - CalSTRS could still be a provider offering a variety of plans to locals.
- **Third: Address Unfunded Liability**
 - Do after addressing other issues.

UC Retirement Programs— A Different Ballgame

- **This “Superfunded” Pension System Has No Unfunded Liability and No Employer/Employee Contributions**
- **Contributions Will Be Needed in Near Future for Pensions and Retiree Health**
- **UC Has Control Over Benefit Design**
 - **Legislature can influence decisions through funding.**

Conclusion

- **There Are Key Principles That Should Drive Your Recommendations:**
 - “Bedrock”—Pay for benefits as they accrue.
 - Address unfunded liabilities as soon as possible.
 - Clarify employer and employee responsibilities.

Conclusion

(Continued)

- **Just as Critical to Think of Retirement Programs as an Essential Part of Compensation**
- **In Order to Get and Retain Necessary Employees, the State May Need to:**
 - Be more flexible.
 - Provide more choices.