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## Editorial: Even CalPERS sees a pension problem

Published Tuesday, Aug. 18, 2009

A top official with the California Public Employment Retirement System finally conceded last week what observers of state and local government finances have been saying for years: California's public employee pension costs are "unsustainable."

"I don't want to sugar-coat anything," Ron Seeling told a seminar sponsored by the Public Retirement Journal. "We are facing decades without significant turnarounds in assets, decades of - what I myself, my personal words, nobody else's - unsustainable pension costs."

Seeling's comments, first reported by veteran Capitol reporter Ed Mendel in his Web log, [calpensions.com](http://calpensions.com), should help jump-start a long-overdue conversation.

Seeling is the pension system's chief actuary, the man responsible for calculating pension costs for 1.6 million state and local government employees. He has long defended the analysis that went into granting more generous pensions earlier this decade. So this is a huge admission. But he is not alone.

Dwight Stenbakken, deputy executive director of the League of California Cities, agrees that government pensions are "unsustainable" financially - and politically as well.

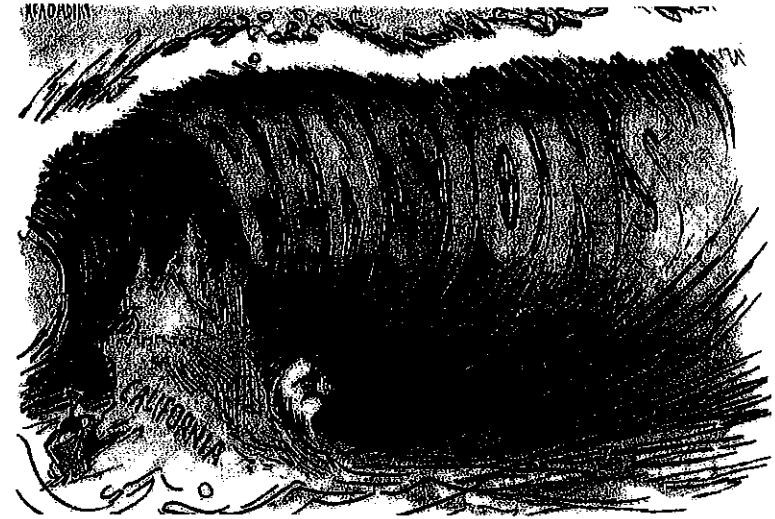
"I just don't think the benefit levels that are in the public sector can be defended in a public debate," Stenbakken told The Bee.

Gov. Arnold Schwarzenegger recently called upon legislators to tackle the pension crisis, but they refused. Now, with pension bills coming due, something must be done.

It's not just that public services are being cut to pay for the pensions. Younger public employees are being furloughed or losing their jobs as limited tax dollars go to support another entire class of retired employees.

If union leaders don't work to negotiate a solution to the problem, they could soon face a revolt from the public - and their own members, who increasingly find themselves on the wrong end of this inter-generational tug-of-war. The time to start talking is now.

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## Governor wants to revamp battered public-worker pension programs

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Published Monday, Aug. 17, 2009

Weeks after wrapping up a deal to close a \$26 billion budget deficit, Gov. Arnold Schwarzenegger is taking aim at what he calls California's next great fiscal problem: the state's battered pension system.

Reviving an idea he floated during budget negotiations in June, Schwarzenegger wants legislation creating a two-tier system that would deliver lower benefits to newly hired public employees - not only state workers but firefighters, police officers, teachers, and other local-government employees.

Along with proposed cutbacks in retiree health benefits, Schwarzenegger says, the plan would save \$90 billion over the next 30 years.

The Republican governor says the state's pension system faces tens of billions of dollars in unfunded obligations and is increasingly unaffordable.

"We cannot continue promising people things that we cannot deliver," Schwarzenegger said at a July press conference.

Public-employee pensions have long been politically untouchable in California, and Schwarzenegger's previous attempt to overhaul the system flopped.

Things might be different now.

The state and local governments that support California's two big pension funds are struggling financially – and are being told they'll need to pump more money into the retirement system to offset the funds' huge investment losses. Taxpayers, struggling to cope with declines in their private 401(k) plans, might not want to spend more on the two funds, the California Public Employees' Retirement System and the California State Teachers' Retirement System.

"From a financial standpoint, I would argue they're unsustainable," said Dwight Stenbakken, deputy executive director at the League of California Cities. "Politically, they're unsustainable. I just don't think the benefit levels that are in the public sector can be defended in a public debate."

Although current workers and retirees wouldn't be affected, Schwarzenegger's plan has enormous long-term implications for the Sacramento area, where state employees make up 10 percent of the work force. State workers, already smarting from their 14 percent salary cut caused by furloughs, consider their pensions something of a birthright – a reward for paychecks that lag behind those of the private sector.

"When workers decide to become state employees, they often trade off higher wages in the private sector for the promise of (more secure) pension benefits in the public sector," said Jim Zamora, spokesman for Local 1000 of the Service Employees International Union. The local represents 95,000 state workers.

Yet at least 10 states have cut benefits for newly hired workers in the past five years.

And Orange County just created an optional two-tier system, though it needs to be approved by the state Legislature.

The SEIU and some other unions say they're willing to discuss Schwarzenegger's plan or other cost-saving proposals – but through contract negotiations, not legislation.

"We're open to talking about it," said Chris Voight, staff director at the California Association of Professional Scientists. The union represents 3,000 state scientists.

Legislative Democrats also say the proposal should be negotiated with the unions first. Schwarzenegger "needs to bring the issue to the table with the unions," said Alicia Trost, a spokeswoman for Senate President Pro Tem Darrell Steinberg, D-Sacramento.

In any event, Schwarzenegger's advisers believe lawmakers will ultimately prove receptive to the governor's proposal because pension obligations are crowding out other state spending priorities.

"I think the appetite (for change) is really there," said David Crane, the governor's special adviser for jobs and economic growth. "Billions in cuts have had to take place because money is needed to meet past pension promises."

CalPERS is declining to take sides, but is offering itself up as a neutral provider of data. CalSTRS gave the governor's proposal a lukewarm reception.

In a statement, CalSTRS Chief Executive Jack Ehnes said the current system "provides a modest income equal to about 62 percent of our members' final salaries. As our members do not pay into Social Security, CalSTRS remains the sole source of guaranteed retirement income for many."

Declines in the stock market and other investments have hammered the two giant pension funds, making it more difficult for them to meet their pension obligations.

The two funds, which lost a combined \$100 billion in the just-finished fiscal year, say they

need more money from taxpayers. CalPERS can impose higher rates at will and plans to do so beginning next summer for the state and in mid-2011 for local governments. CalSTRS needs legislative approval to raise rates and has begun initial talks with lawmakers.

In 2005, Schwarzenegger pushed a ballot initiative to convert CalPERS and CalSTRS into 401(k)-style plans designed to stabilize the state's costs while forcing workers to shoulder the market risk. That plan, like his current proposal, would have affected new workers only.

The governor, under assault from the unions, scrapped the proposal because of a snafu in how the initiative was worded.

In his new plan, Schwarzenegger is trying to turn back the clock – to 1999, when his predecessor, Gray Davis, signed a bill sweetening pension benefits.

The move remains controversial, particularly with fiscal conservatives. The state's annual contribution to CalPERS has tripled since the mid-1990s, to more than \$3 billion, although CalPERS attributes much of that to increases in the state payroll.

Under Schwarzenegger's proposal, newly hired workers would get the same pensions that were in place in 1999.

Keith Richman, a former Republican assemblyman and longtime advocate for pension change, is pushing a November 2010 ballot initiative to scale benefits back further.

"There's no question that the unions are going to fight this type of initiative tooth and nail," Richman said. "But the public has become much more aware of the problem."

CalPERS acknowledges that last year's market meltdown, which cost the fund approximately \$56 billion, put the pension fund in a hole. Its "funding ratio," which compares assets against liabilities, fell below 70 percent in July. Pension funds generally aim for 80 percent.

Although CalPERS' staff considers last year's losses a unique event, the fund doesn't think a return to normal market conditions will cover its long-term obligations.

While final calculations haven't been made, contributions from the state and local governments that use CalPERS, likely will rise 0.4 percent to 2.2 percent, according to a CalPERS staff report. The increases would be considerably higher if not for a "smoothing" system that will stretch last year's losses out over 30 years.

"No one knows what the future returns are going to be like," said CalPERS spokeswoman Pat Macht. "At least in the short term, we can't invest our way out of this."

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## CalPERS warns Congress: Cost of benefits unsustainable

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Published Wednesday, Aug. 19, 2009

CalPERS, the country's second-biggest buyer of health care services, urged Congress on Tuesday to act quickly to overhaul the nation's much-maligned health care system, saying there would be "a huge cost to inaction."

In a letter sent to California's congressional delegation, whose ranks include some of the most influential voices in the national debate, the nation's largest pension fund called inaction "an untenable policy choice."

"Without reform this year, we will not be able to sustain our health care system," said the letter, signed by CalPERS President Rob Feckner and the pension fund's chief executive officer.

The California Public Employees' Retirement System is expected to spend \$5.7 billion this year on health benefits for more than 1.3 million public employees, retirees and their families. Only the federal government buys more health care services than CalPERS.

"We hope our voice will be heard. Being silent would be irresponsible on our part," Feckner said in an interview. "We want to be sure that health care becomes affordable for every American."

The pension fund has dispatched its lobbyists and other officials to Capitol Hill to influence the debate.

"It's important that we weigh in, as the health care debate goes on," he said. "We want to have a seat at the table."

The CalPERS letter underscores the high stakes involved in health care legislation, a high priority for the Obama administration. Some industry groups and a chorus of conservative voices have expressed concern about potential government intrusion into medical decisions. They've also raised alarms about the cost, which by some estimates could exceed \$1 trillion.

The price tag has put pressure on the Obama administration to respond. Health care advocates are increasingly worried the administration may drop its support for a public

insurance plan to compete with private insurers.

"Obviously, he's getting pressure. We hope he doesn't give up on the public plan option. We think that's the right way to go," Feckner said. He noted, however, that he was expressing his personal opinion, and CalPERS has not yet issued a formal position on the controversial public plan option. The public plan is fiercely opposed by the insurance industry.

CalPERS has used its considerable clout to gain favorable deals with its stable of insurers, but it has been unable to contain costs entirely on its own terms.

Since 2003, insurance premiums paid to cover its members have risen by 60 percent.

In recent years, containing health care costs has become an increasing focus of the pension fund.

Of particular concern is the cost of pharmaceuticals. Each year, CalPERS and its members spend about \$1.15 billion on prescriptions -- nearly a fifth of the pension fund's health care spending.

"They clearly have a lot at stake, but the same kind of issues could apply to any kind of employer," many of whom are concerned about rising health care premiums and medical costs, said Joanne Spetz, a health care economist at the University of California, San Francisco.

CalPERS has a history of activism and has not been shy about using its influence in many progressive causes. Because of its massive investments, it wields considerable influence on some of the nation's largest corporations.

The agency has also wielded its clout as a massive consumer of health care services, with the letter being the latest example.

"That allows them significant leverage," said James Hawley, a business professor at St. Mary's College, who closely monitors CalPERS.

Earlier this year, CalPERS announced a pilot program aimed at reducing health-care costs. It joined Blue Shield of California, Catholic Healthcare West and Hill Physicians Medical Group to launch a yearlong experiment to better coordinate care. As part of the program, Blue Shield, with the cooperation of its medical partners, has agreed not to increase its premiums.

"We're trying every angle we can, trying to find a way at cost containment," Feckner said. "There's been a continuous spiraling of health care costs. It's out of control."

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# David Siegel: Health costs are crippling economy

Special to The Bee

Published Wednesday, Aug. 19, 2009

There could be no better example of the old adage, "If you keep doing what you're doing, you'll keep getting what you're getting," than the debate around national health care reform. And what are we getting? Forty-seven million Americans have no health insurance, and tens of millions more have inadequate coverage. And what do we pay for this?

In 2008, health care costs reached \$7,498 per person, 50 percent higher than any other nation. This is crippling our economy, resulting in increasing job losses, with firms like General Motors reeling in part from the cost of providing health insurance. Sharply escalating costs for public programs, such as Medi-Cal and Medicare, divert resources from other important programs. Most importantly, despite these huge expenditures, Americans lag behind much of the rest of the developed world in the quality of our health care as measured by such indices as life expectancy and infant mortality.

Individuals and families are also paying more for what they get. According to several studies by the Kaiser Family Foundation, the average family deductible for those with a preferred provider organization, a PPO, increased 30 to 64 percent in two years. Eighty-four percent of families purchasing coverage had a co-payment of more than \$25 in 2008, while average out-of-pocket costs rose from \$2,827 in 2001 to \$3,744 in 2006.

To remedy some of this, President Barack Obama has proposed a public insurance option that would cover all Americans and provide much-needed competition for private insurance companies. Those who are satisfied with their current plans would keep them. The new public plan would have lower administrative costs (that now consumes up to 30 percent of total health spending as opposed to Medicare, which uses 3 percent for overhead), have greater leverage to hold down prices (by being able to bargain with pharmaceutical companies to get lower prices for medications, for example), and the ability to demand the use of technology such as computerized patient records to improve patient care and safety. Importantly, patients with pre-existing health problems will be covered.

Given these problems, it is not surprising that a vast majority of Americans support major health care change. According to a recent New York Times/CBS News poll, 85 percent of respondents said that the health care system needed to be fundamentally changed, 86 percent said rising costs posed a serious economic threat, and 72 percent supported a government administered insurance plan, like Medicare, for those under 65. When asked

specifically about a public health insurance option in a poll by the Employee Benefit Research Institute, this idea was favored by 85 percent of respondents.

The nation's largest insurers, hospitals, medical groups and pharmaceutical companies oppose the public insurance option. Of course they do. It would squeeze their profits and force them to undertake major reform. And these groups have enormous resources to oppose change. According to a July 6 article in the Washington Post, these groups have hired 350 former government staff members and retired members of Congress to lobby lawmakers. "The hirings are part of a record-breaking influence campaign by the health care industry, which is spending more than \$1.4 million a day." The Pharmaceutical Research and Manufacturers of America doubled its spending to nearly \$7 million in the first quarter of 2009, much of it spent to lobby against the public option.

Not surprisingly, Republican legislators, who have cast themselves in the role of spoilers, oppose the public option. Unfortunately, given the onslaught by the lobbyists, even some Democrats are backsliding on the need for major change. This includes many who are members of the Democratic Blue Dog caucus. We all need to contact our elected officials to let them know that universal health care with a public option is a necessity. If we keep doing what we're doing, we'll keep getting what we're getting. And for health care, this is not good enough.

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