SEIU Local 1000: Focus on the Facts

Retiring Baby Boomers No Threat to Pension Plan

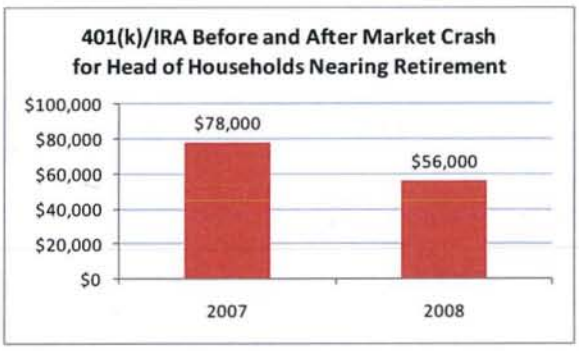
"Defined-benefit" pension plans—like those commonly available in the public sector and most Fortune 500 companies—have been under fire. One strident argument claims that defined-benefit plans face monumental collapse because of the impending retirement of Baby Boomers. For example, an October 2010 report released by the Milken Institute – which received considerable press – blamed supposed pension-fund instability on demographic trends.[i] That argument is baseless.

Defined benefits from California's public-employee pension are prepaid

Even if Baby Boomers retire en masse from state service, California's public employee pension system remains unaffected by shifting demographics because *defined-benefit pension plans are completely pre-funded:* pension funding for each retiree comes from contributions the employee and the employer have *already* made, along with subsequent investments (CalPERS estimates that 63 cents of every dollar in benefits comes from the return on investments).[ii] More employees retiring means more of them were paying into the fund in the past twenty to thirty years.

401(k)s and risk-sharing are not the solution

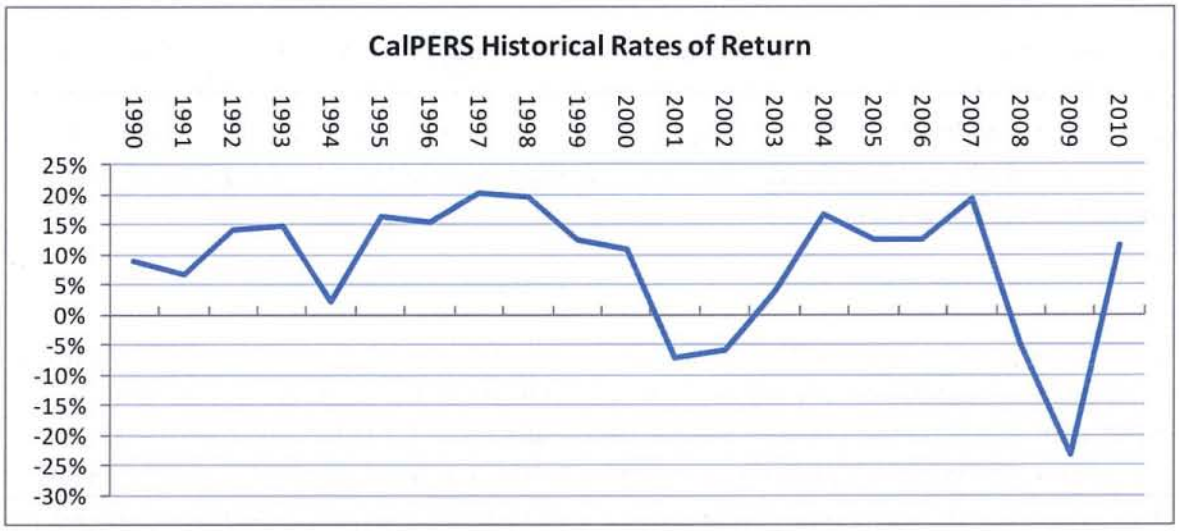
The most common solution offered by defined-benefit doomsayers is switching to a "defined-contribution" plan similar to 401(k) plans. But that so-called solution—or any proposed change in employee retirement benefits – wouldn't ward off any impending catastrophe supposedly wrought by those about to retire because courts have definitively limited any pension-plan changes to newly hired employees.[iii] Even if courts ruled otherwise, 401(k) plans would be a poor substitute for public employees who were promised defined benefits, particularly since 401(k)s are susceptible to stock market shocks that can diminish employees' nest eggs just as they retire. A study by the Center for Retirement Research at Boston College estimated that a typical 401(k) account of someone nearing retirement dropped 39.3% from $78,000 to $56,000 due to the 2008 stock market crash.[iv]



Defined-benefit plans assure monthly payments, providing participants with peace of mind about their old age.[v] Several studies have concluded that defined-benefit programs provide a higher level of security *without necessarily costing more in contributions,*[vi] and that defined-benefit programs have significantly reduced elder poverty.[vii]

Yet another attempt to scapegoat public-employee pensions falls flat

Recent stress on the CalPERS pension system was caused primarily by one event: the market collapse of 2008. CalPERS' investment returns during that time slid to -28.3%[viii] – an unpredictable plummet. Thus, CalPERS' investments in the state-employee pension fund tumbled from a healthy 96.6% funded in June 2007 to 58.4% funded in June 2009. The chart below shows recent variations in CalPERS' return on investments, including the unprecedented 2008 collapse and subsequent recovery.[ix]



Critics are trying to shift blame for CalPERS' temporary downturn from the unexpected market collapse—the true culprit—to public employees' retirement benefits, an easy scapegoat. But this system has remained stable over many fluctuations in the economy. Public-sector workers contribute to an efficient and stable defined-benefits system. They deserve the dignified retirement they paid for.

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[i] Wong & Shen, "Addressing California's Pension Shortfalls: The Role of Demographics in Designing Solutions," Milken Institute October 2010.

[ii] See CalPERS Pension Buck at http://www.calpersresponds.com/issues.php/dna-calpers-pension-buck. The amount has been as high as 75% of every dollar in benefits. See the transcript of Patricia Macht, "Setting the Record Straight" at the CalPERS website at http://www.calpers.ca.gov/index.jsp?bc=/member/video/view/setting-record-straight.xml&pst=ACT&pca=ST.

[iii] Kern v. City of Long Beach, 29 Cal.2d 848 (1947) and subsequent case law.

[iv] The analysis presented in the figure is from Munnell et. al. They assumed that 55-64 year olds have 67 percent of their assets in equities and modeled the change in the balance based on the 42 percent drop in the Dow Jones Wilshire 5000 from October 9, 2007 – the stock market peak – to October 9, 2008. Munnel et. al., "An Update of 401(k) plans: Insights from the 2007 Survey of Consumer Finance," Center for Retirement Research at Boston College, Nov. 2009. http://crr.bc.edu/images/stories/Working_Papers/wp_2009-26.doc_compatibility_mode.pdf

[v] Frank Porell, Ph.D. and Beth Almeida, The Pension Factor, National Institute on Retirement Security, July 2009, at http://www.nirsonline.org/storage/nirs/documents/pension_factor_web.pdf.

[vi] "Protecting the Nest Egg: A Primer on Defined Benefit and Defined Contribution Retirement Plans," Council of Institutional Investors, at http://www.afscme.org/docs/please_add_this_to_pension_facts_you_should_know_section_-_.pdf; see also Beth Almeida and William B. Fornia, FSA, "A Better Bang For the Buck," Journal of Pension Benefits, Vol. 16, No. 2 inter 2009 pp. 11-15, accessible at http://www.nirsonline.org/storage/nirs/documents/Bang%20for%20the%20Buck%20Report.pdf.

[vii] Porell & Almeida estimate that DB pension plans help 4.7 million Americans avoid poverty, and help keep 1.4 million Americans off public assistance, at pp. 14-17.

[viii] CalPERS Facts at a Glance: Investments, at http://www.calpers.ca.gov/eip-docs/about/facts/investme.pdf p. 3.

[ix] CalPERS Facts at a Glance: General, http://www.calpers.ca.gov/eip-docs/about/facts/general.pdf at p. 4.