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California Pension Debt Continues to Grow

Stanford Study Shows Pension Share of Budget Likely to Triple

Stanford, CA (December 13, 2011). The Stanford Institute for Economic Policy Research (SIEPR) released a report today documenting the Golden States worsening public pension problems. The report, authored by Stanford Professor Joe Nation with the assistance of California Common Sense (www.cacs.org) researcher and Stanford junior Evan Storms, shows the states pension problem is worse than just two years ago.

The study covers the California Public Employees Retirement System (CalPERS), California State Teachers Retirement System (CalSTRS), and the University of California Retirement Plan (UCRP).

In addition to todays report, SIEPR and CACS are releasing a report on the financial well-being of 63 local or independent public pension systems and a report on San Joses two public pension systems later this week.

Among the findings from the statewide report:

Contribution rates, the share of payroll that state government sponsors of pension plans pay each year, are likely to double or perhaps triple, crowding out education and social services spending. At the state level, barring new revenues, pension spending is likely to rise from its current 5.7 percent share of General Fund spending to more than 17 percent.

Delay increases the costs to the state and other governments facing pension shortfalls. The annual cost to the state of delaying pension solutions is more than $1.2 billion over the next year alone, or $3.4 million per day.

The June 2011 funded ratio, the measure of assets to liabilities, is only 74 percent for CalPERS, using a high rate of return on its investments. At a more realistic 6.2 percent rate of return, the CalPERS funded ratio falls to 58 percent. Private plans with a funded status below 80 percent are required to freeze benefits and face other restrictions.

Using the same 6.2 percent assumption, the June 2011 funded status for CalSTRS is 60 percent. For UCRP, the funded status is 72 percent.

The total unfunded liability for CalPERS, CalSTRS, and UCRP is nearly $300 billion, assuming future investment rates of return of 6.2 percent. Even if the three systems earn 7.75 percent (CalPERS, CalSTRS) and 7.5 percent (UCRP) per year, the shortfall is $142.6 billion, or nearly $12,000 per California household.

Using a risk-free or low-risk discount rate, the total unfunded liability for CalPERS, CalSTRS, and UCRP is $498 billion, 17 percent higher than the $425 billion shortfall estimated in April 2010.

It is highly unlikely that Californias pension systems will invest their way out of their funding problems. CalPERS must earn an annual average rate of return of 12.5 percent for 16 years to ensure that its assets are sufficient to cover its liabilities.

The magnitude of the problem is sufficiently large that prospective benefit reductions for current employees should be examined, despite legal hurdles.

The report authors conclude that Governor Browns reform plan is a needed step in the right direction, more than doubling previous savings from reforms, but it appears likely to reduce the unfunded shortfall by a small amount. Additional reforms are required.

The studies will be available on the SIEPR website at siepr.stanford.edu.

Visit www.cacs.org/transparency_pensions.php to see a suite of interactive data visualizations created by California Common Sense that illustrate the findings of this report and in particular funding status of pension systems throughout California under a range of assumptions.

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SIEPR is an economic policy research organization and is non-partisan in political orientation. SIEPR scholars conduct studies on important economic policy issues in the United States and other countries. SIEPRs goal is to inform and advise policy makers and the public and to guide their decisions with sound policy analysis. In the course of their research, SIEPR faculty train, educate, and support Ph.D. students as future economic policy analysts.

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