

CASE *Issue* Brief

COLORADO ASSOCIATION OF SCHOOL EXECUTIVES

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Politics and PERA *Separating Fact from Fiction*

When contemplating Colorado's Public Employee's Retirement Association, a well known quote from The Talmud regarding the existence of God comes to mind — "For those who believe, no proof is necessary. For those who do not believe, no proof is possible."

And so it goes with PERA. Since PERA entered the political spotlight several years ago, the pundits and the press seem to have polarized into two opposing camps: (1) those who believe that PERA will very soon disintegrate because of

Did You Know?

For every \$1 paid in benefits — 65 cents comes from investment returns, members contribute 18 cents, and employers contribute 17 cents.

political and/or financial pressures, and (2) those who believe the current controversy surrounding PERA is a total contrivance and that no changes need to be made.

No doubt the truth lies somewhere between these extremes. We believe that PERA is the recipient of exaggerated political criticism over a financial problem that does, in fact, need some attention. So, the purpose of this piece is to accurately and fairly examine the issues.

What is PERA's financial condition? Is PERA stable?

Yes. PERA is quite stable. As of this writing, PERA's market value is in excess of \$35 billion. If there were *flat* investment returns in the future, PERA would have enough cash to pay benefits for over 40 years. By almost every standard, PERA is solvent.

Then what is PERA's financial problem?

PERA has an "unfunded liability" of over \$11 billion. An "unfunded liability" is when one doesn't have enough cash or assets, *on hand*, to cover liabilities that will become due in the future.

For example, if your home mortgage were to be considered "fully funded," you would have enough cash, *right now*, to pay off your mortgage today! But PERA's future liabilities, or the benefits PERA owes at any point in the future, have grown at a faster rate than contributions and returns on the investment portfolio.

Nearly all pension plans, public and private, have some degree of unfunded liability. The question becomes — how much is too much? In 2034, it is estimated PERA will have \$60 billion in assets. But if investments don't

outpace current projections, PERA will need to increase contributions, decrease liabilities, or both over the long term to cover all current and future retirees.

How did PERA get into this predicament?

Several factors have contributed to PERA's current funded status. In 1999 and 2000 when PERA had more assets than liabilities, there was a major political movement to increase benefits, to lower the age of retirement, and to lower employer contribution rates for PERA.

Did you know?

According to latest projections, PERA will have assets totaling more than \$60 billion in 2034.

Some people blame Governor Owens, some people blame the Colorado legislature, some blame the PERA Board of Trustees, but from our perspective, there is plenty of responsibility to share. Regardless of who began this giveaway, every group and association in Colorado, including CASE, stood up and cheered and implored the legislature to ratify the changes.

While many groups pushed for changes, PERA urged caution during this "feeding frenzy" but was drowned out by overwhelming numbers. Now, some of the same politicians who voted for increased benefits and lower contribution rates are the ones pointing fingers and talking about a "crisis."

One result of these changes is that PERA's employer contribution rate has declined by 25 percent since the late 1990s. Current contribution rates and estimated return on investments aren't enough to pay off the debt over time. That's why PERA secured legislation in 2004 that gradually restores the employer contribution rate over a period of years. PERA has proposed legislation to accelerate the contribution rate increases that already exist in state law. In short, employer contributions were lowered during the boom years — now employers need to step up to fill some of the gap.

External events also intervened. After 9/11 and the dot.com bust in 2001, PERA's investment portfolio took a serious hit, just as most of us saw our personal investments head south. While investment returns in recent years have, for the most part recovered, the glory days of the 1990s boom are behind us.

What's the best solution to the problem?

Different groups have proposed numerous "fixes" that range from adjusting how Highest Average Salary is figured, to reconfiguring the benefit package, to privatizing the system. Several bills to make changes in PERA have been floated in this legislative session, none of which have sufficient support for passage and signature by the Governor. Revised legislation, acceptable to multiple camps, is imminent as of this writing.

In addition to a legislative fix, a drive to put a proposal on the November ballot is underway. The proposal calls for changing PERA's board composition and shifting from a defined benefit to defined contribution system. It's not clear yet if this measure will make it to the ballot.

Why all the negative press?

The negative publicity about PERA over the past year is largely the work of organized ideologically motivated activists and profit-minded special interest groups.

Did you know?

PERA has \$35 billion in assets and paid \$2 billion in benefits in 2005.

A Colorado organization, www.fixpera.org, is connected to Americans for Prosperity, a national tax-limitation group (www.americansforprosperity.org). The American Legislative Exchange Council (www.alec.org), a proponent of limited government, also is behind this movement.

Colorado is not the first state to have its retirement system attacked by those who would like to dismantle public employee retirement systems. Last year, Alaska changed from a defined benefit plan (like PERA) for its public employees to a defined contribution plan where members are responsible for investing their retirement contributions. This has also occurred in Florida and Michigan. California's public employees were able to keep an initiative off the ballot that would

have closed the two largest public employee retirement systems in the nation. Other states such as West Virginia have shifted to a defined contribution plan, only to revert back to a defined benefits system.

The reasons for implementing a defined contribution plan are political and financial. Mutual funds and private providers stand to make a huge amount of money by investing PERA's \$35 billion portfolio.

Private investment managers may charge up to 1.5 percent of investments, while PERA management fees are less than one-tenth of 1 percent. That adds up to hundreds of millions of dollars in fees if PERA is changed from a defined benefit to a defined contribution system.

It should be noted that this is a companion movement to the Bush administration's campaign to voluntarily privatize part of the Social Security system. Some believe that individuals ought to be responsible for managing their own retirement savings.

What about talk of changing PERA governance?

Some charge that it's a conflict of interest for members to sit on PERA's Board of Trustees. These individuals call for trustees to serve by political appointment. Currently, trustees are elected by the membership for whom they have a fiduciary responsibility. Isn't that a fundamental principle of our democratic form of government? There is no reason to think that politically appointed trustees can manage

the PERA trust funds any better than a popularly elected governing board.

In short, there is no conflict. PERA trustees oversee the investment of the portfolio. The Colorado legislature sets contribution and benefit rates.

How does PERA's employer contribution rate stack up against other public and private retirement systems?

One concern of would-be PERA reformers is the prospect of a future bail out by taxpayers through increased employer contribution

Did you know?

The average retirement benefit for members who retired in December 2005 was \$2,400 a month, or \$28,800 a year.

rates. In reality, PERA has one of the lowest employer contribution rates in comparison with other public pension plans in Colorado and other states.

The 2006 employer contribution to PERA is 10.65 percent. By comparison, public pension plans for neighboring states show an average employer contribution rate of 17.2 percent.

Even with the scheduled gradual increase of the employer rate up to 13.15 percent by 2012, Colorado will still compare favorably with other public pension plans.

What does all this mean for PERA members?

Don't panic and assume you have to retire now to avoid losing your benefits. We're hearing stories from CASE members that some of our best educators feel compelled to consider early retirement. Keep doing what you love. In our opinion, your retirement is secure.

In the event of a ballot issue, know the facts and be ready to inform others who may be misinformed. As leaders in your communities, you have a responsibility to present accurate information.

Share your concerns about changing PERA with your elected representatives in the legislature. Now. Your voice is important. PERA members, who number 375,000, make up a powerful voting block. Exercise your power.

For the most up-to-date information about PERA and related legislative activity, go to www.copera.org. PERA's Web site has direct links to information about these issues and to your legislators. CASE will continue to provide regular updates to CASE members about this issue.

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