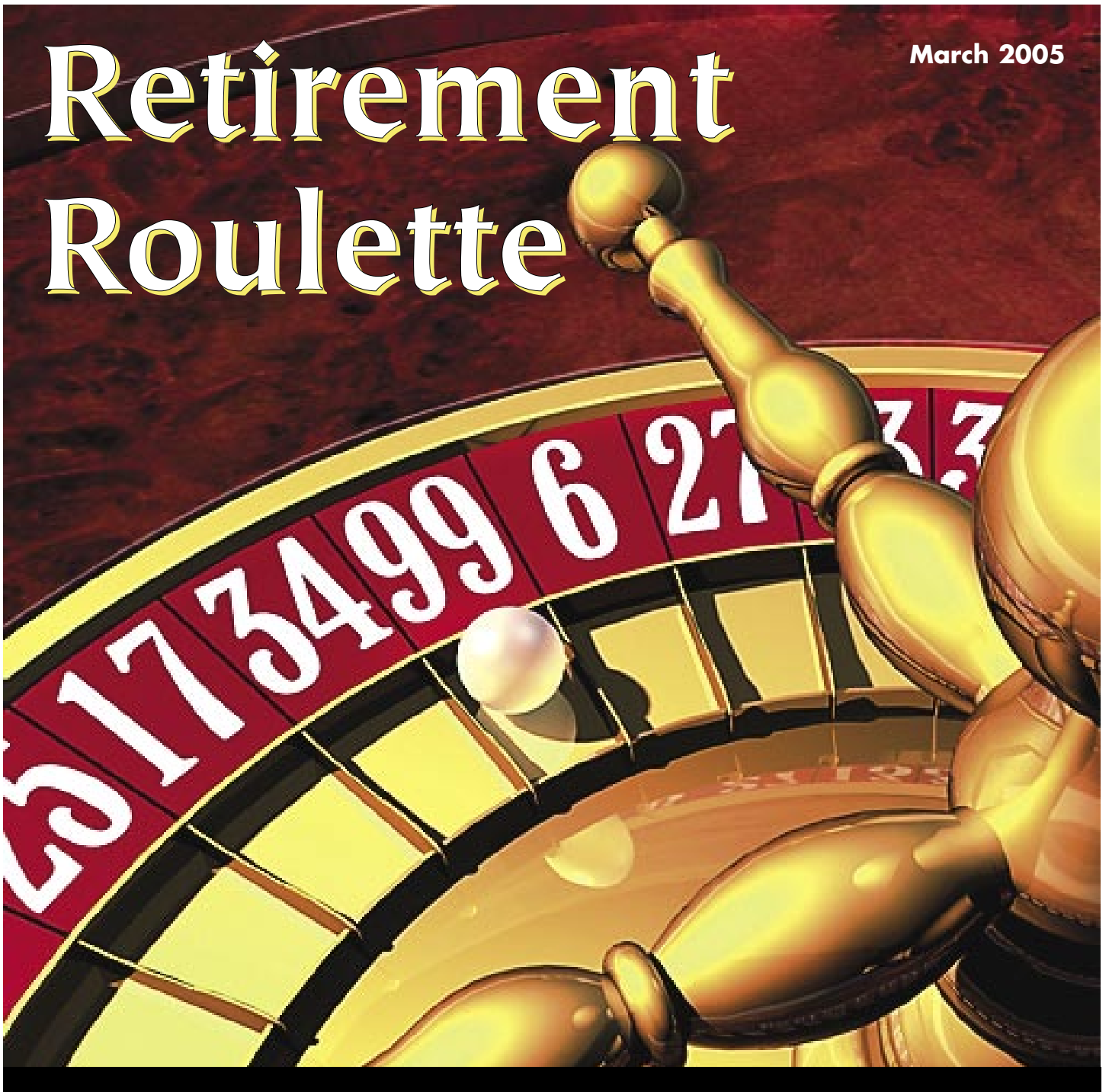


# Retirement Roulette

March 2005



## Don't Gamble With Your Pension



### Inside:

Pension Poker Hurts Everyone.....	p 2
You've Got Questions. We've Got Answers .....	p 4
Adjuncts Know This Game is Stacked .....	p 5
Cal. Treasurer Phil Angelides on Who's Behind These Attacks .....	p 8

# PENSION POKER:

*Shut it Down! This Game Hurts Every Californian!*

The state pension system is under attack and the Governor is leading the charge. He is seeking to dismantle our secure retirement system – the same system that has served California teachers well for decades.

Gov. Schwarzenegger has dealt teachers and other public employees into a new high-stakes game: pension poker. He is supporting constitutional amendments to close the CalSTRS defined benefit program to new members beginning in 2007. When these teachers retire, they will be entirely dependent on 401(k)-type accounts.

That definitely stacks the deck heaviest against new teachers, who will be among the most vulnerable of all Americans. Since they aren't in Social Security, without CalSTRS they will have no guaranteed pension of any kind. Given the track record of defined contribution retirement plans, they'll retire with a lower income replacement ratio and risk running out of money in their "golden years" when health care costs are highest.

But every other player at the table - current teachers (full-time or adjunct), retirees, school districts and taxpayers - will also lose big if Schwarzenegger wins. Current teachers who choose to remain in CalSTRS Defined Benefit Plan and retirees will have their original pension benefit contractually guaranteed. However, the COLA and Purchasing Power Protection which increase the pension to cope with inflation do not have the same contractual guarantees as the original benefit. These could well be cut back – or disappear – along with raises, health insurance, and other "expenses" as the costs of playing pension poker come due for school districts and taxpayers.

School districts and taxpayers lose when the costs of running two different pension systems are totaled up – to a sum of billions of dollars - \$5.9 billion in the first 10 years for CalSTRS alone. That's money spent on pension poker instead of increasing teachers' salaries, providing health care benefits, or improving schools.

Our chances to win start by understanding what's at stake. Defined benefit plans, defined contribution plans, COLA, purchasing power, and income replacement ratio are terms



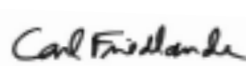
that might put you to sleep if you weren't playing a game you had to win to preserve your retirement security – so we explain them in these pages.

Of course, like lots of professional gamblers, the governor isn't playing with his own money. Who's bankrolling his game? No one explains that better than the Treasurer of California, Phil Angelides, so we've included his analysis on page 8.

Unlike the Lottery, we have no choice about whether or not to play pension poker. We're all in! Therefore, we have to win - because this game is bad not just for teachers' retirement security, but for education and for the future of California. It will drive experienced teachers to other states or alternative careers, increase taxes, and waste education spending as we pay more to give teachers less secure retirements.

The Los Angeles College Faculty Guild is committed to the campaign to shut pension poker down in California. To help you understand what the game is all about - so you can help us tell the gamblin' Governor, your family, friends, and neighbors that this game isn't good for anyone in our state – here's our special issue on the attacks on our pensions.

In Unity,



Carl Friedlander, President Carolyn Widener, Executive VP



# Education Will Lose if Retirement Becomes the New Lottery

A successful educational system requires good teachers, adequate funding, and the respect and support of the public. The Schwarzenegger/Richman proposals threaten all three.

## Without secure retirement, California will lose its teachers

California teachers are a rare breed when it comes to pensions.

Unlike almost all other employees in the private and public sectors, California's K-12 and community college teachers are not in Social Security. They have no guaranteed retirement income other than their CalSTRS pension plan. In most other states, teachers retire with both Social Security and a state-sponsored pension plan. The Schwarzenegger/Richman proposal to leave teachers with only a 401(k)-type plan is the most extreme pension change proposed in the country. Even President Bush's Social Security proposal is voluntary and leaves some guaranteed benefit for those who choose to participate.

Who will want to enter our profession – and stay in it – if it leaves them

among the most vulnerable of all working Americans? If teachers are forced to play retirement roulette, mid-career teachers will be encouraged to leave teaching or go to another state – to take a job where they have more retirement security. Experienced lifetime career teachers will become a rarity.

## A drain on school resources

School districts and community colleges are already underfunded in California compared to what other states spend on education. Imagine the negative impact on our already struggling education systems if districts are forced to cope with new costs. Where will the money come from to

- \* hire and train new employees to cope with the increased administrative complexity of multiple systems?
- \* provide new employees with disability insurance and death and survivor benefits?
- \* pay into Social Security for those who would otherwise have only DC retirement accounts?

(continued on page 7)

*“As trustees, we are greatly concerned about the impact this change would have on the future of our teachers. Under the CalSTRS Defined Benefit Program, our members cannot outlive their benefit. Changing to a defined contribution plan would rob them of that security.”*

– Gary Lynes, CalSTRS Board President

*“We’ve witnessed attempts to eliminate defined benefit plans in other parts of the country. However, our Defined Benefit Program meets the retirement, disability and survivor benefit needs of our members and the public’s need for experienced, able teachers at a reasonable cost. We have a strong, sound system and California’s educators need it to stay that way.”*

– Jack Ehnes, CalSTRS CEO

## 7 things you can do

- » Sign up for e-mail Action Alerts at [www.AFT1521.org](http://www.AFT1521.org)
- » Write your elected officials
- » Author op-eds and letters to the editor
- » Spread the message on campus and in the community
- » Get trained as a spokesperson
- » Sign a COPE payroll deduction card
- » Stay informed through your Guild chapter

# Frequently Asked Questions



## 1. What kind of pension plan is CalSTRS?

CalSTRS is a defined benefit plan that consists of the *Defined Benefit (DB)*, *Defined Benefit Supplement* and the *Cash Balance* benefit programs. These programs provide guaranteed retirement, disability and survivor benefits to more than 750,000 public school and community college teachers and their families. CalSTRS is currently the third-largest public pension fund in the US, with a value of \$125 billion.

The *DB program* guarantees lifetime retirement benefits based on age, years of service and final compensation at the time of retirement. The DB program also pays out disability and survivor benefits. The *DB Supplemental Program* and the *Cash Balance Plan* are hybrid DB/DC plans. Like DC plans, at retirement you have the money in your account, not a life-time monthly allowance set by a formula. Like DB plans, you cannot lose the principal in your account due to market fluctuations.

## 2. How would Richman's bill, the proposed constitutional amendment, ACA 5 (and other similar proposals), change retirement?

Richman has said that public employees receive far-too-generous pension benefits.

The bill would change retirement in four ways:

- Require anyone hired after July 2007 to enroll in a DC plan;
- Allow members currently in DB programs to roll their retirement over to the new DC programs, relinquishing all rights to switch back;
- Authorize government employers to establish their own DC plans and outsource administration and investment to private sector companies;
- Allow the state to contribute an amount from zero to some as-yet-to-be-determined maximum to employee retirement accounts.

The Howard Jarvis Tax Association's initiative would establish a maximum 6% employer contribution for most employees while permitting additional employer contributions for peace officers, firefighters and those not in Social Security.



## 3. Why did the Teachers' Retirement Board oppose the proposed constitutional amendment?

The CalSTRS board voiced four main problems with the bill: It would undermine the funding structure of the current benefit program; California teachers stand to lose more than other employee groups because they don't belong to Social Security; The new plan doesn't include disability or survivor benefits; and Schools would suffer from higher turnover since the new system would not reward longevity as the current system does.

## 4. Pension reform will only affect new employees. Why should I care?

As younger workers are forced into the new plan, funds will be siphoned away from the current system, meaning less money for investments, for COLA's, purchasing power or for new benefits.

## 5. Will forcing all new public employees into DC plans solve the state's fiscal problems?

No. Costs of the current DB plan won't go away. The state will have to pay for the start-up costs of the new DC plans, estimated at hundreds of millions, while funding the current DB plan. It will cost schools and taxpayers more if they pay for death and disability benefits programs and Social Security for employees in DC plans.

# Adjuncts Already Know This Retirement Deck Is Stacked

**A**djunct faculty have been the victims of the very kind of dysfunctional teacher retirement that the Richman/Schwarzenegger proposals would mandate for all teachers. The LA College Faculty Guild has developed local negotiations proposals, supported state legislation, and participated in State and District Task Forces attempting to address the problems for the last 10 years with measured, although slow, progress. Unfortunately, that progress is stalled this year as energy turns to responding to the Richman/Schwarzenegger proposals. The progress may well cease completely if they pass.

For example, the proposals give employers lots of choice about the “new” defined contribution retirement plans. Well, local districts have had lots of choices about adjunct retirement – to the disadvantage of teachers. Before the federal government insisted in the 1990s that employers contribute into Social Security or a Social Security alternative for all part time workers, adjuncts in many districts had no retirement plan at all. To accommodate the federal mandate, different districts adopted different plans with different employer contribution rates.

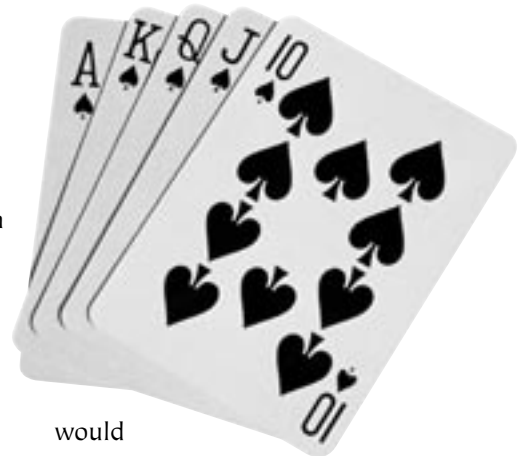
The LA district selected PARS – a defined contribution plan. Although CalSTRS developed a hybrid plan, Cash Balance, the insurance industry selling defined contribution plans succeeded in stopping the California legislature from mandating Cash Balance for all districts. The LACCD management did not agree to the Guild’s demand to make Cash Balance an option until 2003! A few districts agreed to offer Social Security as an option. Although the Guild has proposed this for several negotiations, the LACCD has not agreed to do so.

The result of all this “district choice” is that adjunct faculty members teaching

at two or three different colleges in the greater Los Angeles area can easily find themselves in a different retirement plan at each college – each with different employer and employee contribution rates. Even if different districts offer the same plan, they likely have different employer contribution rates (at Long Beach City College the employer contributes zero!). And, moving from one plan to another is not easy! LACCD faculty wanting to transfer PARS balances to CalSTRS Cash Balance have waited two years to finally be able to do so this coming July.

Should the proposals pass, *beginning in July 2007, new adjuncts would be unable to select the CalSTRS Defined Benefit Plan and currently employed adjuncts would be unable to switch into it.* Currently, although they are all legally compelled to do so, many districts have been slow to offer the CalSTRS Defined Benefit Plan as an option to adjuncts. Still, almost half the adjuncts in the state have found their way into it, demonstrating that many adjuncts, too, want the security of a defined benefit retirement.

Of course, since 93% of the CalSTRS Defined Benefit Plan’s membership is K-12 teachers, the system has had some challenges accommodating adjuncts. For example, after study by the CalSTRS Task Force on Part-time Community College Faculty, CalSTRS and FACCC sponsored successful legislation last year to permit the recalculation of benefits paid to part-time adult education and community college employees who were members of the DB Program prior to 7/1/96. Other issues – from how unused sick leave is calculated for adjuncts to district reporting issues are unlikely to be addressed through future legislation if the Richman/Schwarzenegger proposals pass. These corrections



would mean some new costs for CalSTRS. If CalSTRS has no contributions coming in for new members, the system’s unfunded liability will be exacerbated, creating a formidable barrier to incurring new costs, even to address these inequities.

In spite of these problems, adjuncts in CalSTRS DB at least have access to its disability, survivor, and death benefits. Adjuncts in DC plans such as PARS have no such benefits through those plans or from their educational employers.

Finally, adjuncts should consider the impact of these radical retirement proposals on the finances of college districts. The Guild is very proud of our progress on adjunct salary and working conditions as well as our long-standing leadership on adjunct assignment security through our contractual seniority lists. But, these proposals, if they pass, will force teachers’ unions and districts into expanded negotiations over the design and increased costs of retirement plans. Progress on salary and health care issues will be competing for fewer available dollars. If districts are forced to pick up high levels of the “transition costs,” even the number of classes available to be taught by part-time instructors could be reduced.

The bottom line is that these proposals hurt adjunct faculty, too. It’s in all of our interests to defeat them.

# DB & DC: Benefits and Disadvantages

Feature	Defined Benefit	Defined Contribution
Guaranteed, predictable benefits	Yes	No
Provides higher payout at retirement	Yes	No
Less risk	Yes	No
Better earnings/lower fees	Yes	No
Employer bears investment risk	Yes	No
Professional investment managers	Yes	Only if you hire someone
Early retirement features (including incentives)	Yes	No
Benefit improvements	Yes	No
COLAs	Yes	No
Portability	If purchase service credit	Yes
Attract people to public service	Yes	No
Low administrative costs	Yes	No
Comprehensive coverage, including disability, death, early retirement and past service benefits	Yes	No
Assets collectively invested	Yes	No

## Odds for a Secure Retirement Better with Defined Benefits

### A Case Study of DB & DC Retirement Systems

Pension experts often look to Nebraska as a case study in DB versus DC plans, since the state offered both types of plans for over 40 years.

- At retirement: the average retirement benefit for one DB group was 55% of final pay versus 35% for the DC employee's average retirement.
- During retirement: The same DB plan retiree received an automatic COLA (generally about 2%) and was also eligible for an additional increase to maintain the retirement benefit at 75% of purchasing power. The DC plans did not provide a COLA.
- The bottom line: The DB plans provided a 60 to 70% income replacement while the DC plans provided only about 25 to 30%, although both employees and employers contributed about 11.5% of pay each year. The DC plans' low-income replacement ratio was the result of poor investment returns over many years.

### Investment Returns and Fees

Defined benefit plans usually have better earnings and lower fees. The Council of Institutional Investors' publication, *Protecting the Nest Egg: A Primer on Defined*

*Benefit and Defined contribution Retirement Plans*, lists these data:

- One half of DC plan investors do not diversify, almost none rebalance portfolios periodically,
- Economist Alicia Munnell estimates that during 1985-2001 DB plans outperformed DC plans by 0.8 percent on average. Over a 30-year span, that small advantage multiplies to a 25% difference in total returns.
- Research on advisory fees by Profs Freeman and Brown indicate that DB pension funds pay only about half of what DC plans pay for investment advisory services – 0.28 versus 0.56 percent of assets.
- The Investment Company Institute, which represents the mutual fund industry, found that the total operating expense ratio of DB plans was on average 40 basis points less than that of mutual funds, not even taking into account marketing and distribution fees.
- Defined contributions plans don't cost less, they cost more. Dollar for dollar, DC plans cost more. Costs to administer a defined benefits plan is less than .2% of one percent or 18 cents per \$100 invested compared to as much as 2% of assets or \$1.35 per \$100 in a DC plan.

## Educational Lottery

(continued from page 3)

\* increase employer contributions to the traditional plans if these plans see their liabilities increase without contributions from new employees?

One thing seems certain: money that otherwise would go to salaries, health benefits, and instruction will be diverted instead to cover these additional costs.

### CalSTRS is worthy of the public's trust

Teachers have not abused their defined benefit retirement system. On the contrary, the system has succeeded in encouraging experienced teachers to work longer – to reach thresholds of 30 years of service and 63 years of age.

No teacher retires with 3% at 50 or 2% at 55.

Few teachers file for disability, and those who are on disability pay taxes on their benefits. Employers have paid the same 8.25% contribution into the system on each teacher's salary for the last 15 years – an amount that can only be changed by the legislature. The 2% simple COLA that retirees receive is the most modest of any major retirement system. The state's direct contribution to CalSTRS has been shrinking and is now half of what it was in 1998. The state makes no contribution to retired teachers' health care; where it exists, it was negotiated locally district by district.

CalSTRS retirement is a fair deal for California taxpayers, who have demonstrated time and time again that education is their top priority. It's also a fair deal for teachers – who at least know they will get a monthly amount, based on a formula, for their



lifetime after they leave a full career in the classroom. It's a minimum floor the Governor and all of us need to preserve.

The struggle to protect and improve public education in California has been difficult and is ongoing. The Schwarzenegger/Richman retirement lottery scheme is the last thing this state needs if it wants to improve its public schools.

# Pension 101: Glossary of Terms

· **Defined Benefit Plan** is a secure retirement plan with fixed retirement benefits calculated on a formula based on salary and years of service. You can plan your retirement knowing *exactly* how much you will receive. Funds are pooled and invested by expert money managers. DB plans usually provide disability, death and survivor benefits as well.

· **Defined Contribution Plan** is an individual 401k style plan in which you or your broker invest your money in the stock market or in bonds. During good times, your account goes up. When times are bad, your account dwindles. When you retire, whatever amount is in the fund represents your retirement account.

· **Cash Balance Plan** is a *hybrid plan* that has an account like that of a *defined contribution plan*. Annual investment credits are added to the account, however the employer guarantees that employee account balances will earn interest at a specified rate. Retirement benefits are not calculated on a formula, but like a defined contribution account, whatever amount is in the fund represents your retirement account.

· **Cost of Living Adjustment (COLA)** provides a way to raise retirees' benefits and thereby help them offset increases in the cost of living caused by inflation.

· **Death Benefits** are paid to the survivor of a plan participant who dies while still on the job.

· **Disability Protections** are often built into DB plans as part of the risk pool and cover participants as long as they are disabled, without respect to age. Under a DC plan, a participant who becomes disabled will have access only to what money has accrued in his/her account

· **Plan Participant** is a member of a retirement plan and can be an active member (working), an inactive member (terminated, but not yet eligible for a retirement benefit), or a retired member.

· **Portability** is the right of an individual to move funds from one pension plan to another. Under most governmental defined benefit plans, state law allows employees to recover service credit for earlier years of work for which they will not earn such credit. These laws allow them to "purchase prior service credit," sometimes known as "buying back prior service."

· **Survivor** is the individual designated by a *plan participant* to receive *death or survivor* benefits. The survivor is sometimes called the beneficiary.

· **Survivor Benefits** are paid to the survivor of a plan participant who dies after he or she has retired.

# The Right's Attack on Public Pensions

by Phil Angelides,  
California State Treasurer

*The following was excerpted from a slightly longer editorial that appeared in the LA Times on Feb. 7, 2005*

Gov. Arnold Schwarzenegger says getting rid of public pension plans for California's state and local government workers is about helping to balance the budget. Peel back the budget wrapping on his plan, though, and you will find the governor's real agenda: the California prong of a national attack on the pension funds that have stood up for corporate reform and the interests of ordinary families and investors hurt by the recent wave of corporate scandal.

As recent news reports explain, the driving force behind the proposed pension ban is the same crew of "anti-tax advocates, free-market enthusiasts and Wall Street interests" that is pushing President Bush's Social Security privatization plan. They include Grover Norquist, the president of Americans for Tax Reform, and Stephen Moore, president of the Free Enterprise Fund. They see the governor's proposal as "one of our highest priorities."

Across the country, the governor's ideological soul mates are targeting public pension funds for elimination because those funds — with the California Public Employees' Retirement System and the California State Teachers' Retirement System at the forefront — have stood up for ordinary investors against the rampant corporate abuses.

"Just 115 people control \$1 trillion in these funds," Norquist said. "We want to take that power and destroy it." What bothers him and others is that these funds have rallied other institutional investors to protect the market from abuses and fraud and to support such corporate reforms as linking executive pay to performance, requiring auditor independence, separating stock analysis from investment banking at financial firms, ending insider trading at mutual funds and opening corporate board elections to shareholders.

But protecting the bottom line for members is precisely the goal of the corporate reform movement. CalPERS and the teachers retirement fund lost more than \$1 billion in the WorldCom and Enron frauds.

That's why the governor and his right-wing ideologues have targeted the

pension funds: not because the funds have strayed, but because they are leading the fight on behalf of ordinary shareholders to put transparency and accountability back into American capitalism.

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*"Just 115 people control \$1 trillion in these funds. We want to take that power and destroy it."*

*— Grover Norquist,  
Americans for Tax Reform*

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