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Pension fallout nigh

Liabilities foreshadow bankruptcies

By Troy Anderson, Staff Writer
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Years of bestowing lavish pensions and benefits on public employees has left dozens of the state's largest agencies with billions of dollars in unpaid liabilities that experts warn could start a cascade of bankruptcies, service cuts and tax increases.

According to a Daily News review of agencies in Los Angeles and across the state, California's largest public agencies face setting an extra $108 billion aside in the coming years to pay for promised retiree pensions, health care and workers' compensation claims.

That's a tenfold increase over the $10 billion the state Legislative Analyst's Office calculated among hundreds of public agencies statewide just three years ago.

"It's absolutely stunning," said Steven B. Frates, a senior fellow at the Rose Institute of State and Local Government at Claremont McKenna College. "We're just seeing the beginning of this. It's going to get worse, not better.

"Californians will suffer economically tremendously. Schools, roads, highways, bridges, sewers, water systems and expenditures of these kinds will have to be curtailed and more and more money will be channeled into these huge retirement obligations.

"It's one of the more stunning transfers of wealth in the history of the human race."

The unpaid bills, although they won't materialize all at once, are the result of generous benefits, mismanagement by elected officials, pressures from employee unions, stock market losses, and the longer life spans and pending retirements of tens of thousands of baby boomers, experts say.

And experts say the $108 billion is conservative, estimating it could soar as cities, counties, school districts and other agencies fully calculate the costs - especially retiree health care liabilities - under new federal accounting rules.

Los Angeles County alone currently has a total unfunded liability of $16 billion; Los Angeles city government, $3.2 billion; and Los Angeles Unified School District, $6.9 billion.

Then there's CalPERS - the state's public employee retirement system - with a total unfunded liability of $22.3 billion and the California teachers retirement system with $24.2 billion.

The debts represent the amount by which the liabilities of the retirement plan exceed its assets at any given time - which one expert describes "like an ever-growing family credit card balance."

"The bottom line is that many of these agencies are going to go bankrupt in the future," said former Los Angeles Mayor Richard Riordan, who in the 1990s helped reverse an unfunded liability in the Department of Fire and Police Pensions - now one of a handful of pension systems statewide with a surplus.

"It all goes back to the 1990s when we had the high-tech bubble and they improved the pensions for the bureaucrats in cities, counties and state government. It's ridiculous what we did.

"If you look at the dire predictions of the future of California and our tax revenues, you are going to have total fiscal disaster throughout the state."

In a series of interviews, elected officials, pension system administrators and pension experts agreed that some public agencies may face bankruptcy and will join San Diego - facing a $1.4 billion pension debt - in increasing fees and cutting services to cover ballooning costs.

"It's going to break the bank," said Bob Stern, president of the Center for Governmental Studies in Los Angeles. "There is going to have to be a whole review of this. Future contracts will have to be changed.

"When the money starts flowing to these retirees, as it will, it's sort of like the levees in Louisiana. We know it's going to happen, but are we planning for the future?"

And the debt is likely to come due soon as about half of all federal government employees and a third of California and Los Angeles

County employees are expected to retire in the next five years.

Some agencies are expected to fare better with the issue than others, according to county Chief Administrative Officer David Janssen.

While the Board of Supervisors voted last week to further sweeten the health benefits package for current employees, Janssen said the unions agreed to some concessions including co-pays for hospital emergency room visits and medications.

"Los Angeles County, I think, is fully capable of dealing with the costs of these benefits," Janssen said. "The board has held the line all along on salaries and retirement benefits."

Still, the county grand jury recently said the debts will pose significant financial challenges in the years ahead.

And a Los Angeles city official, who requested anonymity, said the soaring annual contributions already have resulted in service cuts in the last two years.

"Certainly we're not in the shape of San Diego or other horror stories out there," he said. "The city may choose to start looking at some of these issues. On the health side, we may decide to limit subsidy increases. That hasn't been on the table yet, but it's something in our office we've kicked around a little bit."

Other public agencies around the state have already begun taking steps to reduce the unfunded liabilities.

In February, the Legislative Analyst's Office warned that the LAUSD's $6.9 billion unfunded retiree health and workers' compensation liabilities threatens its future ability to operate.

David Holmquist, LAUSD director of risk management and insurance, has presented a plan to the board to set aside $14 million annually for the next 30 years to offset the workers' compensation deficit.

He has also recommended the board hold a two-day retreat next year to come up with ideas and establish a task force to address the retiree health deficit.

"We are trying to look at all of the solutions, but obviously it starts at the bargaining table," Holmquist said.

California is not the only state facing this situation. Nationwide, taxpayers are exposed to more than $366 billion in unfunded public pension liabilities, according to a 2003 analysis of 123 state retirement systems by investment consulting firm Wilshire Associates.

That's more than double a $180 billion shortfall that was estimated just the previous year.

Combined with underfunding in private pensions, the promises made to retirees are projected to cost $700 billion more than the assets available to support them.

Some government and pension officials place most of the blame for the huge unfunded liabilities on the sharp decline in the stock market beginning in 2000, arguing that the funding ratios - at least for pension systems - will bounce back as the markets rise.

"All those straight-line projections don't reflect the ability to earn returns in the capital markets and they assume that everything that is today is going to be in the future on a consistent basis," said Rich Goss, director of the board of the 40-member California Association of Public Retirement Systems.

"We know from history that's not true. If we had this conversation in the mid-1980s, we'd be having the same conversation. If we had the conversation in 1997, the system was swimming in assets then."

But in a Reason Foundation think tank report issued earlier this summer, George Passantino argues that while market losses certainly played a role, the declines only unveiled the weaknesses in government pension systems.

"The fact that a retirement system could turn so quickly from investment nirvana to debt nightmares should give taxpayers and lawmakers cause for major concern," Passantino wrote. "At the heart of the pension crisis is a set of incentives that encourages policy makers to make decisions for which they do not have to bear the consequences."

And while stock market gains in the years to come may reduce pension debts, experts say retiree health care costs pose an even more serious problem because of rapidly escalating medical costs.

Fiscal Crisis and Management Assistance Team Chief Executive Officer Tom Henry - who helps public agencies deal with fiscal crises at the request of the Legislature - said many school districts and public agencies have not calculated their unfunded retiree health liabilities.

Experts say those debts will likely be in the tens of billions of dollars.

Statewide, 70 school districts provide lifetime health benefits, 134 provide health benefits beyond age 65, and 554 provide retiree health benefits up to age 65, according to a survey conducted by the team.

"In all districts we surveyed, they are paying as you go," Henry said. "So the (annual payments are) growing exponentially. In some districts it's doubling year to year. That seems mind-boggling. This is starting to drive all other decision-making in important operational areas.

"That's resulting in cuts to programs and services. The LAUSD is a perfect example. But they are actually, and this is to their credit, ahead of a lot of school districts in addressing this. So far, we've just seen the tip of the iceberg."

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