California is known for crises: the workers’ compensation crisis in the early 2000s, the budget crisis following the 2008–09 Great Recession, and the water crisis that has threatened parched California. But the biggest crisis of them all is the state’s government pension problem.

California’s state and local government employees receive defined-benefit pensions that guarantee specific monthly payments to retirees for life. A leading study found that California state workers receive a compensation premium of about 30 percent from their government pensions alone, compared to identical private-sector workers in California.

In theory, these generous pensions are paid for by taking contributions from government agencies and their employees, investing the contributions, and using the investment proceeds to pay the promised pension benefits 20, 30, or 40 years down the road after employees retire.

But in reality, pension officials and politicians of both political parties have deliberately lowballed the contributions and increased the benefits such that there isn’t enough money in the bank today to eventually pay the promised benefits. This deficit is called an unfunded pension liability, and now taxpayers are on the hook to make up the difference between pension promises and pension assets.

California’s unfunded public pension liability, when measured correctly, is two to four times as large as official government estimates: at least $23,000 per California household, and even higher if you live in a community with an unfunded city or county pension plan.

In total, California’s 86 defined-benefit public pension plans are underfunded by a staggering $430 billion. This is the state’s greatest financial challenge since the Great Depression.

The massive tax increases needed to make state and local pension funds solvent have proven to be politically impossible to enact, making the pension systems financially unsustainable. The failure to fully fund the pension promises has allowed the current generation to receive public services that they are not fully paying for, pushing the pension problem onto future generations. Politicians kick the can down the road as pension debts mount.

The unwillingness to confront the true scope of California’s pension costs, to pay for the promises made, and to make changes to control future obligations means these costs are being pushed onto California’s children and grandchildren, who are being forced to pay for promises they did not make and for services they did not agree to. The injustice of this system is apparent to anyone who cares to see.

Left unchanged, the financial burden of the pension problem will crush younger generations, leaving them with a depleted future and a depleted California. The responsibility to fix this problem is as great as any moral imperative because it directly

California’s Public Pension Crisis: Lessons for America

By Lawrence J. McQuillan

(continued on page 6)
A New Year and New Congress

A s the 2014 elections showed, American public opinion continues to grow in opposition to Obamacare (ACA) and Big Government more broadly. After the election, a Gallup survey found that only 37% of Americans approved of Obamacare; moreover, independents and non-whites gave President Obama’s signature healthcare law an approval rating of only 33% and 56%, respectively.

Even Harvard University faculty are in revolt. As the New York Times reported: “Harvard’s experts on health economics and policy have advised presidents and Congress on how to provide health benefits... But those remedies will now be applied to the Harvard faculty, and the professors are in an uproar.” The university’s Faculty of Arts and Sciences voted overwhelmingly against the Obamacare-driven changes to their health plans, such as greater cost sharing and a narrower choice of doctors and hospitals, but they were too late.

Bewildered by Harvard’s cuts in benefits, sociology professor Mary Waters asked the Times: “What is the crisis?” Could it be that ACA architect Jonathan Gruber’s now well-known derision of average voters—that they were “too stupid” to hear the truth about Obama-care—applies to Harvard’s own self-satisfied elites?

How will the new Congress respond to the public clamor? Will it replace Obamacare with market-based healthcare? Senior Fellow John Goodman has shown that, in a free market, consumers would be free to choose plans and treatment options tailored to their own needs—not those of special interests. In addition, competition would drive down costs while increasing access and quality. Details can be found in our award-winning book by Dr. Goodman, Priceless: Curing the Healthcare Crisis, and in our forthcoming book by him, A Better Choice: Healthcare Solutions for America.

To help us move such ideas into impact, please join us as an Independent Associate. With your tax-deductible membership, you can receive a FREE copy of Priceless, California Dreaming, Recurring Rushmore (p. 5), and other publications, including our journal, The Independent Review (p. 3), plus other benefits (see envelope).

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A Case for Patent Reform • Tolstoy Exposes the State

The Winter 2015 issue of The Independent Review offers an exciting array of scholarship on political economy and intellectual history. Here are two highlights.

A Case for Patent Reform

For many decades most economists believed patents were key to the innovation and material progress enjoyed by the West. In recent years, however, many have looked at patents with growing skepticism, with some even suggesting that the patent system be scrapped.

However, economist Arthur M. Diamond, Jr. (University of Nebraska at Omaha) believes these critics miss their mark. To be sure, the U.S. patent system has problems, including overly costly litigation. But, according to Diamond, it can and should be mended, not ended (“Seeking the Patent Truth: Patents Can Provide Justice and Funding for Inventors”).

Diamond argues that critics and defenders of patents often share false assumptions. Typically, they overlook what he regards as patents’ primary moral purpose: to provide justice to inventors. Also, they tend to misunderstand patents’ main economic function: not to incentivize inventors to invent, but to enable them to do so—such as through the licensing of their patents to manufacturers. (Thomas Edison relied on this practice early in his career.)

After developing these arguments, Diamond examines several proposals for improving the U.S. patent system, including crowd-sourcing aspects of the patent-review process and creating specialized patent courts to prevent opportunistic plaintiffs from shopping for a favorable jurisdiction in which to file a lawsuit. Inventors may also find relief from the growth of private-sector institutions created to support them, Diamond explains.

One such example, Intellectual Ventures, a company co-founded by Microsoft founder Bill Gates, claims to help inventors by purchasing their patent rights and thus enabling them to focus on inventing. Such organizations can make up for the flaws of the legal system, but they also have additional appeal: they involve using innovators to find ways to support other innovators.

Arthur M. Diamond, Jr.’s article is available at www.independent.org/publications/tir/article.asp?a=1029 •

Tolstoy Exposes the State

Leo Tolstoy (1828–1910) is world-famous for his epic novels set amidst the turmoil of 19th century Russia, but the writer was also well-known in his day for his criticism of government power and advocacy of Christian libertarianism and pacifism. One of the best examples of his thinking on those topics can be found in his book, The Kingdom of God Is Within You (1893), a work unfamiliar to general readers today but one rich in insight and clever turns of phrase.

The book’s riffs on the machinations of government are especially quotable, according to Independent Institute Senior Fellow Robert Higgs (“Tolstoy’s Manifesto on the State, Christian Anarchy, and Pacifism”). Moreover, they show that Tolstoy saw important truths about the state that almost every other writer has overlooked.

“He even makes an analyst such as [public choice theorist] James Buchanan, who often complained...”

(continued on page 6)
The Independent Institute in the News

Center on Entrepreneurial Innovation
“You’ve got entities holding large numbers of patents, not to make anything, not to have any process to invent, but to sue. It’s a litigation game. It’s a racket. It’s a shakedown.”
—William Watkins, Jr. on Newsmax TV, 9/24/14

Center on Educational Excellence
“The relationship between spending and student achievement is murky at best. Beginning with the 1979–80 school year, when the U.S. Department of Education was established, through the 2010–11 school year, total K–12 student enrollment increased 20%. During this same period, the number of staff designated as ‘teachers’ increased more than 73%. Total public school spending, meanwhile, increased 130%, adjusted for inflation. Student achievement, meanwhile, flat-lined at best, and by some measures took a nosedive.”
—Vicki Alger in USA Today, 10/21/14

Center on Law and Justice
“In 1933, the Hitler dictatorship began to consolidate its power and they used the gun registration records to look up social democrats to, and in fact against all of its opponents, take their guns away, to disarm them. By 1938, Kristallnacht, people don’t realize that the focus of that was to disarm the Jewish population in Germany.”
—Stephen P. Halbrook on Stossel, 10/16/14

Center on Peace and Liberty
“War, unfortunately, is the biggest cause of big government in U.S. and American history. . . . Woodrow Wilson ruined the entire 20th century, now he’s ruining the 21st. He got the U.S. involved in World War I, which led to permanent big government in the U.S.”
—Ivan Eland on Fox News Channel, 10/26/14

Center on Global Prosperity
“There has been (and always will be) demagoguery on the illegal immigration issue. The latest is that they are unsanitary and harbinger of exotic diseases. The truth is that most Americans see these slurs for what they are. And if the White House’s political bean-counters would have looked a little deeper, they would have found that even after all the scaremongering a strong majority of Americans favor giving immigrants a path to citizenship.”
—Alvaro Vargas Llosa in Miami Herald, 10/13/14

Center on Culture and Civil Society
“The fire in the streets of Ferguson is reminiscent of the urban riots that burned nearly all major U.S. cities in the 1960s. . . . Sadly, there has been a lack of police or National Guard protection for the real victims of rioting, then and now: small business owners, including many African American business owners and their employees. . . . Most of those surveyed in Ferguson would agree with the statement made by community activist Jerry G. Watts after the 1992 Los Angeles riot: ‘Rioting is not a democratic act.’”
—Jonathan Bean in The Daily Caller, 11/26/14

Visit our newsroom at www.independent.org/newsroom to read these articles and more.
Because books are our most effective weapons in the long-run battle of ideas, we redoubled our publicity campaign for three books in the last quarter of 2014.

From Washington to Obama

In 2008, we published Senior Fellow Ivan Eland’s book *Recarving Rushmore: Ranking the Presidents on Peace, Prosperity, and Liberty* to much acclaim. In 2010, the book won a Gold Medal IPPY Award as well as favorable reviews from *Booklist*, the *Pittsburgh Tribune-Review*, the *Rocky Mount Telegram*, and *BBC News Magazine*. Since the book’s original publication, however, one president has left the Oval Office and another has moved in and served one-and-a-half terms (and counting). Hence, Eland and the Institute were eager to update the book with new material on George W. Bush and Barack Obama.

That wish came true in October 2014, with the release of an updated edition of *Recarving Rushmore*. The new publication includes revised rankings of every U.S. president, as well as new material on the Bush presidency and an additional chapter on President Obama.

The Independent Institute also worked with expert publicity consultants to maximize media exposure. The result has been dozens of radio interviews nationwide, as well as appearances at the Liberty Political Action Conference and on TV shows such as FoxNews “Fox & Friends,” Arise TV, and others.

Defending Innovators

A specter is haunting the high-tech world: the specter of the patent troll. What exactly is a patent troll? It’s a firm or person who buys up legal rights to questionable patents and uses them as the basis for aggressive lawsuits against manufacturers who, at least superficially, seem to be in breach of the plaintiff’s patent rights.

These frivolous lawsuits aren’t just a boon to lawyers; they’re also a significant drain on the U.S. economy, as defendants must redirect tremendous resources to fighting them or risk a judgment that can amount to millions—or even hundreds of millions—of dollars, as Research Fellow William J. Watkins, Jr. explains in *Patent Trolls: Predatory Litigation and the Smothering of Innovation*.

Firearms Control Before the Holocaust

Research Fellow Stephen P. Halbrook has written several books for us, and each one is a model of scholarship. But his most recent book is his most powerful. That’s largely because of the somber nature of his subject matter.

*Gun Control in the Third Reich: Disarming Jews and “Enemies of the State”* recounts how the Weimar Republic enacted firearm registration to help quell political violence, and how the Nazis utilized gun ownership records when they took over the reins of power.

Because the story of gun control is so little known, Halbrook and the Institute were especially eager to redouble our efforts to promote this book. The campaign has included targeting additional media outlets to those that covered the book in 2013.

The campaign was a rousing success, resulting in appearances at the University Club (New York), and reviews, interviews, or citations on C-SPAN’s BookTV, FoxNews’ *Stossel*, WorldNet Daily, the “Dick Morris Show,” *Catholic Insight*, *The Daily Bell*, the “Bill Meyer Show,” and Brietbart.com. *
impacts the quality of life our children will enjoy and their chances for upward mobility.

Fortunately, it is not too late to fix the problem. In my forthcoming book, *California Dreaming: Lessons on How to Resolve America’s Public Pension Crisis*, published by the Independent Institute, I explain how six reforms would solve California’s pension problem in an equitable, responsible, and sustainable way that preserves pension benefits already earned, provides competitive pensions going forward, and grants the flexibility needed, so that future generations are not paying for deals they did not make.

The recommendations—most already in place in the private sector—would require financial transparency and full annual funding of each pension plan without “pension obligation bonds.” Also, the reforms would give state and local governments the flexibility to switch to defined-contribution pension plans going forward for all employees. In addition, voters would be required to pre-approve any pension plan change that increases financial obligations.

The recommendations would bring California’s public pensions in line with those in the private sector and ensure that California never faces such a crisis again. It is time to fix California’s pension crisis permanently to help restore the California dream and provide a reform blueprint for the rest of America.

*California Dreaming* also explains that current and future retirees would be wise to accept the recommended reforms because the alternative could be much worse for them. Recent federal bankruptcy court decisions in both the Detroit and Stockton municipal bankruptcies have ruled that pension checks of current and future city retirees may be cut in bankruptcy proceedings. Both cities were driven into bankruptcy by unaffordable pension obligations.

The reforms offered in *California Dreaming* would bring California’s public pensions in line with those in the private sector and ensure that California never faces such a crisis again. It is time to fix California’s pension crisis permanently to help restore the California dream and provide a reform blueprint for the rest of America.

Lawrence J. McQuillan is a Senior Fellow and Director of the Center on Entrepreneurial Innovation at the Independent Institute. His Institute book *California Dreaming: Lessons on How to Resolve America’s Public Pension Crisis* is forthcoming.

**The Independent Review: Tolstoy Exposes the State**

about people’s ‘romantic’ views of politics and the state, seem himself utterly romantic,” Higgs writes.

Two quotes from Tolstoy’s book illustrate his brilliance:

• “Undisguised criminals and malefactors do less harm than those who live by legalized violence, disguised by hypocrisy.”

• “The good cannot seize power, nor retain it; to do this men must love power. And love of power is inconsistent with goodness; but quite consistent with the very opposite qualities—pride, cunning, cruelty.”

As Higgs notes, Tolstoy’s words presage themes explored by later analysts of government power, including F. A. Hayek, Mancur Olsen, and even Higgs himself.

Literary scholars have shown that Tolstoy was a man of his time. Robert Higgs has shown that the master storyteller was a thinker for ours, as well.

I f reform-minded lawmakers in the 114th Congress wish to improve Americans’ healthcare, they must do more than repeal the Affordable Care Act (Obamacare). They must replace it with measures that will empower patients, create real competition among health insurers and healthcare providers, and minimize the distorting role of government in the medical marketplace.

Independent Institute Senior Fellow John C. Goodman proposes his ideas for achieving these objectives in Healthcare Solutions for Post-Obamacare America.

In Part I, he diagnoses six major flaws of the Affordable Care Act, including its impossible mandates, inadequate funding, disruptions to the labor market, and disparate impacts on employers. One example of the latter, Goodman explains, is a loophole in the law allowing large employers who self-insure to offer workers slim health plans with no hospital coverage or specialist services. Workers offered such plans become ineligible to buy tax-favored, Obamacare-exchange health plans that include those benefits.

In Part II, Goodman discusses six principles for commonsense reform (choice, fairness, universal coverage, portability, patient power, and real insurance), precepts that build on his Healthcare Contract with America and his award-winning book, Priceless: Curing the Healthcare Crisis.

In Part III, Goodman proposes several measures that would improve healthcare quality, affordability, and access—including four reforms that, in concert, would fix most of the problems created by Obamacare. They include:

• Replacing all the Obamacare mandates and subsidies with a uniform tax credit for everyone;
• Replacing all the different types of medical savings accounts with a Roth Health Savings Account (featuring after-tax deposits and tax-free withdrawals);
• Allowing Medicaid to compete with private insurance and giving everyone the right to buy in or get out; and
• Denationalizing and deregulating the Obamacare exchanges and requiring them to offer change-of-health-status insurance.

Government shouldn’t mandate that individuals be covered by health insurance, but it could encourage households to buy private coverage by offering them the right kind of tax credit—a refundable, fixed-sum tax credit that discourages buyers from purchasing too much or too little insurance.

In the Report’s visionary final chapter, “Why I Am More Egalitarian on Healthcare Than Most Liberals,” Goodman describes how lifting various government controls in health-insurance markets would empower the least advantaged members of society.

“The result,” writes Goodman, “would be a healthcare system that would be unquestionably more equitable than what you see in either Britain or Canada and a lot more equitable than what we will experience under the Affordable Care Act.”

Download this report at www.independent.org/publications/policy_reports/detail.asp?id=44.
Enrollment for our expanded 2015 Challenge of Liberty Summer Seminars is open! with applications pouring in!

And, thanks to supporters such as you, these will be our best ever!

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Students told us they loved talks such as Senior Fellow Robert Higgs’s “Ideology and Government Growth” and Research Fellow Anthony Gregory’s “Property Rights and Civil Liberty,” with spirited question-and-answer panels daily, and getting to pick faculty members’ brains during informal social and meal times.

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But meeting this demand exceeds our resources, and we launched a campaign with a goal of tripling our capacity in 2015—and we’re so grateful for each of you who have stepped forward.

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Help inspire new advocates for liberty, today! •