Making it Worse: A Case Study in Failed Transitions to 401(k) Plans

Politicians who spent years underfunding public pension systems sometimes try to solve the debt problems they created by switching to a privatized, 401(k)-style defined contribution system. Such a switch usually causes more problems than it solves. Independent actuaries have long warned that switching from a defined benefit plan to a 401(k)-style plan will result in transition costs ranging from hundreds of millions to billions of dollars while retiring workers into poverty.

Any time you close a defined benefit plan, you cut off a critical revenue stream – new employees paying into the system. As a result, you increase the debt and costs to taxpayers. Below is a case study of states that have moved to a defined contribution plan and whose taxpayers have suffered the consequences.

Alaska
In 2006, Alaska moved all new teachers and state employees from the traditional pension plan to a defined contribution plan in an effort to curb the pension system’s $5.7 billion unfunded liability. At the time, Governor Murkowski said that the change will “stop the so-called bleeding.”

By 2014, the unfunded liability had doubled to $11.9 billion. The switch was a mistake, says Rep. Mike Hawker, R-Anchorage: “I very much was concerned when we closed our retirement systems and went to a defined-contribution that by closing those systems we were going to find ourselves in the position we are in today, which was ultimately having to step in with a significant financial bailout.”

During the 2014 session, the Alaska Legislature was forced to infuse the pension system with an additional $3 billion, and extend the amortization period from 15 to 30 years. The amortization extension could cost Alaska taxpayers an additional $2.5 billion.

West Virginia
In 1991, West Virginia moved its teachers from a traditional pension plan to a defined contribution plan. By 2003, the Teacher’s Retirement System (TRS) hit the rock bottom funding ratio of 18%, the lowest level for any public plan for a broad group of employees.

By 2005, the situation was critical. TRS was paying benefits to two retired teachers for every one active member still paying into the fund. West Virginia actuaries projected that the state could save $1.2 billion savings in the first 30 years by returning to a defined benefit plan. After approval from the legislature and the governor, more than 80 percent of eligible teachers voted to return to the traditional pension system. TRS is now funded at 58 percent – closing more than half the funding gap in nine years.

Michigan
Despite a managing a healthy fund, Michigan closed its pension system and began enrolling all new state employees in a 401(k)-type plan in 1997. Since then, the system has suffered, with unfunded liabilities skyrocketing from $697 million in 1997 to $5.4 billion in fiscal year 2012. The funding status of the plan dropped from a healthy 92 percent to 60.3 percent.

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Protecting Teachers’ Retirement

A Quick Comparison

Our Current System: Defined BENEFIT
- The employee, the school district and the state contribute to the employee’s retirement account.
- The Teachers Retirement System invests that money to help fully fund retirement for everyone.
- Upon retirement, the employee is GUARANTEED a certain dollar amount in monthly retirement payments for life.

Treasurer Ken Miller’s Plan: Defined CONTRIBUTION
- The employee, the school district and the state contribute to the employee’s retirement account.
- The employee or the state will choose investments that grow or shrink, depending on the stock market.
- Upon retirement, the employee will receive only the money accumulated in the account. The monthly payments last only as long as the money.

MYTH...
The proposed new system is just for new employees. It won’t affect my retirement in the future.

FACT...
In the current system, everyone’s contributions and the investments help fund everyone’s retirement in the coming years. With the proposed system, contributions from the state and the employer may be smaller and no one can say where money will come from to fund retirement for employees in the current system.

Whose idea is this?
- State Treasurer Ken Miller — thinks changing the pension system on the backs of teachers is a great way to save the state money.
- The John Arnold Foundation — run by the Texas billionaire who made millions running Enron before it went under, has contributed $2 million and is sending so-called experts into Oklahoma to advise our legislators and leaders as to why they need pension reform.

MYTH...
The TRS is badly underfunded and must make changes.

FACT...
True, the TRS is one of the most underfunded systems in state. BUT, the TRS has a plan to reach proper funding within 17 years and is well on track. In fact, the TRS has been in the top 1% performing pension funds in the country for the last 10 years.

Who’s fighting for us?
Keeping Oklahoma’s Promises, a coalition of active and retired education professionals, firefighters, police officers, nurses, corrections employees, and others concerned about these changes.

Sign the petition at keepokpromises.org
Teachers Retirement System investments return 22% for fiscal year. Portfolio tops $14 billion.

OKLAHOMA CITY – Investments returns of the Oklahoma Teachers Retirement System (OTRS) topped 22 percent during the last fiscal year, and the fund’s balance exceeded $14 billion, the system’s board of trustees announced today.

OTRS investment consultant, Gregory W. Group of Tulsa, reported the system achieved an investment return of 22.4 percent during the fiscal year.

The consultant also reported the system finished Fiscal Year 2014 with its highest month-end and year-end portfolio balance. As of June 30, OTRS had a portfolio balance of more than $14.18 billion.

New Board Chairman Bill Peacher stated, “It is enormously gratifying to see the system performing so well with its investment program. This is a tribute to the hard work of the board of trustees, the investment committee, the investment consultant, and the OTRS staff over the last several years.”

Lead consultant Gregory Weaver added, “This type of investment performance is nothing short of spectacular. OTRS has had outstanding performance for several years. The three-year return was 13.6 percent, the five-year was 16.1 percent and the 10-year was 9.0 percent. These returns are well above the assumed rate of return of 8 percent that the system uses for actuarial purposes.”

OTRS serves 54,581 retired educators and 89,333 active education professionals. The board will receive a full quarterly investment report showing its peer rankings at a meeting on August 27.

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