Sorry, Chicken Little

Oklahoma’s Pension Sky Isn’t Falling

BY JOHN R. WOOD

“Oklahoma faces a pension crisis,” said House Speaker Jeff Hickman, R-Fairview, regarding the estimated $11.5 billion dollars the state owes its employees in retirement over the next 30 years. In response, the Oklahoma Legislature has pushed HB 2630 [Rep. Randy McDaniel] and SB 2120 [Sen. Rick Brinkley]. If passed, either would create a mandatory defined contribution plan for all Oklahoma employees who first become employed by any participating employer of Oklahoma Public Employees Retirement System (OPERS) on or after Nov. 1, 2015. Unfortunately, if state workers were successful in getting a raise after many years of not having one, they’ll likely trade that off with an assault on their pension.

Wow, $11.5 billion in pension debt – that’s a lot of money! Our state budget is only $7 billion, what are we going to do?

“The sky is falling!” says Chicken Little.

Slow down! Slow down everyone! Let’s put this in context, please.

Not everyone is running around like Chicken Little in hysteria and paralysis about our pension system, so take a deep breath.

In fact, at least two organizations find that pension reform is a distortion and actually disastrous in the end. “The idea of imminent [public pension] insolvency is a gross distortion,” according to an Institute for America’s Future report, which states: “In addition, a recent Center for American Progress report also finds, it is an illusion that pretends a short-term shortfall caused by a large recession requires moving to a more expensive system that will cost [taxpayers] more in the long run.”

In Oklahoma, there are two major systems administered by the state – the first is the OPERS and the second is the Oklahoma Teachers Retirement System (OTRS). Actually, $11.5 billion is over a 30-year period of time, essentially meaning that the state’s liability is really only $383 million a year. That might mean a lot of money to you, but did you know that Oklahoma has given the oil industry a horizontal drilling tax break amounting to $252 million this year?

You might ask, “Is that fracking right?” Do they need it?

Well, conservative former OKC Mayor Kirk Humphries doesn’t think so; he says: “80% of our wells are

THE OKLAHOMA OBSERVER • 7
horizontal. It’s where the action is. I don’t think that government should incentivize anything that is going to happen without the incentive and, believe me, baby, horizontal drilling is going to happen without the incentive.”

Just think about it, making the oil industry pay the 7% they used to instead of the measly 1% they do now would largely shore up the retirement system quickly. Happening in an oil state? Not likely!

What if the state Legislature could stop the use of offshore tax havens? In January 2013, the U.S. PRIG Education Fund published a report in which it calculated the impact on this practice on each state. For Oklahoma alone, the estimated cost is $239 million.

Both reforms would bring in an estimated $491 million in revenue to the state. This alone leaves the state of Oklahoma with $108 million in revenue and in the black. Can you imagine, if this could happen, it’s a way to shore up the pension question and still make the state money, and—heaven forbid—give state employees a raise after several years without one!

VEGAS RETIREMENT

Rep. Kevin Matthews, D-Tulsa, characterized defined contribution plans as “casino-type retirement” that is analogous to gambling. “This argument boils down to risk,” said Rep. James Lockhart, D-Heavenier. He said employees who invest their retirement savings in stocks could have their retirement wiped out in a stock market crash.

Remember the 2008 recession? Should public employees, who spend 20-30 or more years serving you and me, be subject to the ups-and-downs and turns of the market?

MORE COST EFFECTIVE

Actually, defined-benefit pensions held by public employees are much more cost effective than 401[k]-style retirement plans, according to the America’s Future report.

How is that? Well, it’s because defined benefits bring hundreds of people together to invest in a single portfolio. With a defined-contribution plan, employees bear the risk, while with defined-benefit pensions more risk is borne by the employer.

Overall, defined-benefit plans cost about half as much as defined-contribution plans in providing the same level of benefit, according to research by the National Institute on Retirement Security Defined-benefit plans.

Defined benefit plans realize these cost savings through the way they are structured as a large, diversified, professionally managed investment fund, with the ability to maximize returns over a long time horizon, whereas, 401[k]s are individualized with short-time horizons. The difference for the worker is dramatic!

To illustrate, the aforementioned study finds that providing workers with a secure level of retirement income would cost only 12.5% of payroll with a defined-benefit plan but an astonishing 22.9% of payroll with a defined-contribution plan. That’s a huge difference to the worker!

DON’T TOS BABY OUT WITH BATHWATER

In a 2008 report, Beth Almeida and William B. Fornia, who wrote A Better Bang for the Buck, found that rather simple changes to public-pension plans—such as to increase contributions from employers and workers—should significantly correct the underfunding problem that many plans currently face. It is better to adopt best practices—for example, the Legislature should require state workers to make annual contributions that reflect their share of plan costs. This will likely shore up most defined-benefit plans for the long haul, and minimize the need for making additional contributions in the future.

Can this be done? It already is!

Oklahoma has already adopted several reforms, according to the Oklahoma Policy Institute, such as prohibiting any unfunded benefits, increasing employer and employee contributions, and raising the retirement age for new employees. For example, OPERS has more than an 81% funded ratio on an actuarial basis, according to the Oklahoma Public Employees Retirement System, the liability is only 15% of the state’s total unfunded liability as referred to by Gov. Fallin. OPERS is essentially a healthy system that has surpassed its Actuarial Required Contribution [ARC], meaning that contributions to the system are greater than what is needed to fully pay benefits for current and future retirees. This is good news!

What will truly be a disaster is that if the defined contribution system wins the day, the OPERS and the OTRS employee will not have new money coming into the system. This may very well destroy the system and security of workers, especially current retirees, who have placed all their eggs in the defined benefit in a single proverbial basket. When asked at a recent public meeting [by a ready-to-retire public employee] what is going to happen when no one is contributing to the defined benefit system, even conservative former Speaker T.W. Shannon pointed out that the pensions are obligations. “You can sue,” he said. “We made a promise to these employers, we have to keep them.”

Let’s hope it doesn’t come to that.

John R. Wood, PhD, is a political science professor at Rose State College.