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WHY DOES OPERS HAVE CONCERNS ABOUT THE PROPOSED 2% SHIFT IN PENSION CONTRIBUTIONS FROM PUBLIC EMPLOYERS TO PUBLIC EMPLOYEES?

On May 19, our Interim Executive Director, Karen Carraher, testified before the Senate Finance Committee that the proposed 2% shift in pension contributions from employers to employees would negatively impact the Ohio Public Employees Retirement System. This proposal, which was removed from House Bill 153 after careful consideration by the House Finance Committee, has been the subject of much debate and, as such, it is important that we explain why it should not be put back into the biennial budget bill.

Currently, members of OPERS' State and Local Government Divisions contribute 10% of their earnable salary toward their pensions. Public employers contribute 14% of their employees' earnable salary. (Members of OPERS' Law Enforcement and Public Safety Divisions contribute at higher levels.)

As introduced, House Bill 153 proposed that 2% of the contributions paid by public employers be shifted to public employees. Unfortunately, this seemingly insignificant shift in contribution rates has a very real impact on our System's finances.

Generally speaking, the problems caused by the proposed shift in contributions rates are threefold: (1) the shift reduces the amount of money over which our Board of Trustees has discretion to pay the unfunded liability and health care; (2) the shift would increase the amount that OPERS would have to pay under one of the alternative benefit formulas used for members with shorter terms of public service; and (3) the shift would increase OPERS' future payouts for refunds of member contributions.

First, the proposed shift in contribution rates reduces the amount of money that our Board can use to pay certain expenses, including the reduction of our Unfunded Actuarial Liabilities (UAL) and the cost of providing health care coverage to our retirees. By federal law, an employee's contributions must be used to fund that employee's pension – the OPERS Board has no discretion in this matter. Conversely, employer contributions are not similarly restricted. In OPERS' case, incoming employer contributions are used first to fund employee pensions, and then the System's UAL. If there is money left over after the payment of these necessary expenses, it is used to fund access to health care coverage for our retirees. If the employer contribution shrinks, there will be a negative impact by increased UAL or decreased ability to provide access to retiree health care coverage.

Second, the proposed shift in contribution rates would increase the amount that OPERS would have to pay under the benefit formula often used to calculate a retirement benefit for public employees who have shorter terms of service. That formula is based on the amount contributed by the employee and the 2% shift would increase this benefit.

Finally, the proposed shift in contribution rates would increase OPERS' future payouts for refunds of employee contributions without providing additional revenues to cover those increases. By law, public employees are (at all times) 100% vested in the amount they have contributed to OPERS. The proposed shift would operate to increase not only the amount of the refund of employee contributions (because employees, other than those in the Law Enforcement and Public Safety Divisions, would be contributing at a 12% rate, rather than the current 10% rate), but also the additional amount added to the refunds of those members with longer terms of service, which is funded from employer contributions.

In total, the OPERS actuary has determined that the proposed 2% shift would add 5.5 years to our amortization period (the amount of time it takes to amortize our unfunded liabilities). And, because the fund is currently just within the amortization period allowed by Ohio law (30 years), the proposed shift would effectively push us outside of the statutory limit (to 35.5 years). Since the adoption of the 30-year limit in 1997, OPERS' amortization period has never exceeded the statutory maximum.

OPERS has been providing retirement security for its members since 1935. In that time, we have weathered many 'storms,' including two major economic downturns in the last decade, and yet, we are still more than 75% funded and in full compliance with every state and federal regulation. In November 2009, our Board approved several benefit plan changes meant to ensure the continued long-term

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CONCERNS ABOUT THE PROPOSED 2% SHIFT IN PENSION CONTRIBUTIONS

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stability of the System, in light of the fact that our members are living longer and the need, recognized by our Board, to continue providing access to retiree health care coverage. Restoring the 2% shift in contribution rates would move us further away from those goals. However, if it is the will of the Ohio legislature to restore the proposed 2% shift, we have asked that this discussion occur in the context of the pending pension legislation (HB 69 and SB 3), rather than the biennial budget. OPERS will continue working with the administration, its stakeholders, and members of the Ohio General Assembly to bring about meaningful pension design changes that are good for the fund's solvency and for all Ohioans.

MANDATED DC PENSION SYSTEMS DON'T ALWAYS WORK

Excerpt from a recent PERSpective blog. The full article, which includes additional profiles of the experience in Rhode Island, New Mexico, and Michigan, can be found at: http://perspective.opers.org/pensionreform/mandated-dc-pension-systems-dont-always-work/

While for years we have affirmed the value of defined-contribution retirement plans for some of our members, we noted in a recent blog that there was "scarce precedent" for states creating mandatory defined-contribution plans for their public workers.

We've looked to published reports to uncover the evidence. Our efforts revealed the following details about the few times that states required their public workers to use defined contribution plans:

West Virginia

In "Look Before You Leap: The Unintended Consequences of Pension Freezes," the National Institute on Retirement Security said members of the West Virginia Teacher's Retirement System amassed very little in retirement assets after a plan switch.

The system froze its defined-benefit plan in 1991, and all newly hired teachers were put into a new defined-contribution plan. This structure continued until 2004, when the state's Consolidated Public Retirement Board realized that many teachers had low savings.

The average DC plan account balance was $41,478, with 105 of the 17,767 teachers older than 60 having accumulated more than $100,000 (yielding a monthly income of about $600 if annuitized). The most commonly cited reason for these small account balances was that account holders were unfamiliar with investing.

Concerned that teachers with inadequate retirement income would require governmental assistance, the state enrolled new teachers in the traditional DB plan as of June 30, 2005. Teachers in the DC plan were allowed to switch back, and more than 75 percent did. That reduced the cost of reopening the DB plan, and West Virginia estimated that the switch back would save the state $22 million.

Nebraska

Nebraska adopted two statewide DC plans in 1964: one for state government employees and another for county government employees. Since then, Nebraska's experience has shown that DC plan members retire with lower benefits than their DB plan counterparts. That's because money that is managed and invested by a professional staff into a DB plan earns higher returns, on average, than money in a DC plan.

A December 1998 study found that 10 years after retirement, a retiree with 30 years of service and an average annual salary of $30,000 received about $11,230 annually from a DC plan. A DB plan participant with similar pay and service credit received $16,797 each year.

The Nebraska Public Employees Retirement System found that it spends more in investment management fees, record-keeping fees, educational programs and material with the DC plans than with the DB plans.

For more detailed information on the proposed benefit plan design changes, visit the "Special Coverage" section of the OPERS website at www.opers.org.

The Ohio Public Employees Retirement System (OPERS) is the largest public pension fund in Ohio and the 12th largest public pension fund in the U.S.* In operation since 1935, OPERS serves nearly 954,000 members, including more than 171,500 retirees and beneficiaries.
*Source: *Pensions & Investments*

OPERS Government Relations Team

Gordon Gatien
Government Relations Officer – 614-222-2924

Deborah McCarthy
Assistant Government Relations Officer – 614-222-6466

Christopher Collins
Assistant Government Relations Officer – 614-222-0555

Anthony Tedesco-Nichols
Assistant Government Relations Officer – 614-222-0381

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