NATIONAL PUBLIC PENSION COALITION

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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