Defined Contribution (DC) vs Defined Benefit (DB) Retirement Programs

The purpose of this memorandum is to revisit the need to keep a Defined Benefit type of retirement system which is found in Tier I and II in the KPERS retirement system. Information about Tier III is available on the KCPR Website, www.ksretirees.org. The positives of a Defined Benefit retirement system are listed below, followed by the several concerns about moving away from the present plan. This concern first surfaced during the KPERS Commission of 2011 and then again in 2015. During the 2021 Kansas Legislation system, the idea was raised in the House and on the floor of the Senate. This has led KCPR to address the topic once again. KCPR has long supported the full funding of the present plan as well as calling for a COLA to be added to KPERS.

Important Pension Positives:

Sherry Chan, the chief actuary of New York City, states the following in an op-ed in *Crain's New York Business entitled, "Public Pensions Help the Whole City, Not Just Retirees."*:

1. All citizens benefit from public pensions, not just the retirees.
2. While public pensions may carry debt, they also create revenue.
3. Unfortunately, pension costs, funding levels and their liabilities seem to be the only matters highlighted. In her op-ed, she points out what she calls the 'right reasons" to care about public pensions:
   A. Pension Money stays home and gets recycled.
   B. Public pensions are predictable contributors to the economy.
   C. Pension Costs and Economic Benefits are both shared by all.
   D. **Pensions are important in small communities during economic troubled times as they provide basic economic stability.**
4. A Defined Benefit (DB) retirement plan contains a formula to calculate the benefit so a potential retiree knows exactly what their benefit will be.

The problems related to DC type programs are numerous. Here are some commonly listed concerns:

"If employers continue to control the retirement system and manage it for their own benefit, then within our lifetime "retirement" will inevitably revert to what it was in the 1930s and before. Society-and taxpayers-will be paying for service to support the millions of elderly, formerly middle-class Americans."
"Retirement Heist" by Ellen Schultz

This above statement, of course, relates to the push by employers for the DC type retirement program over pensions. Defined Contribution, aka DC retirement programs, refer to a 401k type investment program for retirement.

1. When there is no requirement to be involved in any kind of retirement program, only 40% of those eligible choose to be involved.
2. Money saved by those participating employees will cover 9.7 years of retirement. (The calculation assumes you will need 70% of your working income, including social security, to live on in retirement.)
   A. The gap between money saved and life expectancy for MEN is 8.3 years.
   B. The gap between money saved and life expectancy for WOMEN is 10.9 years.

Pensions Cost Half as Much as a 401(k) Plan. The savings are detailed as follows:

1. 10% Cost Savings from polling longevity risk.
2. 11% Cost Savings from optimal asset allocation.
3. 27% Cost Savings due to higher returns and lower fees.
4. 48% TOTAL Cost Savings! *

With the Defined Contribution (DC), 401k type programs, the following often occurs:

1. DC programs are often subject to higher fees because lower service fees are not available because of the small amount of money held in individual accounts.
   A. Investment costs in a DB pension program average .7%.
   B. Investment costs in a DC investment program can run as high as 2.0%.
2. DC programs most often require the employee to make investment decisions on their own.
3. DC programs eliminate the traditional 3-legged stool concept because of the removal of the pension's contribution.

Results of a pension program converted from a DB pension plan to a DC plan are the following are the following:

1. If underfunding of the existing pension is the primary problem, conversion to DC does not address this legacy expense.
2. The change causes greater retirement insecurity to retirees.
3. Recruitment and Retention problems follow.
4. Since this reduced retirement may cause employees to work longer, the younger potential employees need the older employees to retire to make a place for them.

Causes for changes from pensions to individual accounts (DC) and outcomes:

1. DC programs will cause an extreme social cost.
2. States will not be prepared to care for those who cannot care for themselves. Economic aid will be required for retirement in some form if not in retirement benefit form.
3. There is enough concern about this fact that twenty-five of the 50 states have grave concerns aboutpensions. Five have acted to increase retirement investment sponsor ships by business owners. Kansas is not one of the states that have had these discussions.

Change in plan design results:

1. The experience of the four states shows that changing benefits for new hires does not solve an existing funding shortfall.
2. The 4 most listed are West Virginia, Alaska, Michigan, and Kentucky.

A Brief Statement about Tier III:

This pension hybrid was the result of the KPERS Commission of 2011 which was requested by then Governor Brownback. This system is a combination of DC and DB but is not as strong as Tier I and Tier II.

*2021 NIRS, AARP, & NRTA.