

If It Ain't Broke, Don't Fix It: Oklahoma's Pensions

Testimony to Sen. Kevin Matthews Interim Study on Pension Sustainability (Senate Interim Study 15-10), October 7, 2015

Dr. Stephen Herzenberg (717-255-7145;
herzenberg@keystoneresearch.org)

Keystone Research Center, Harrisburg, Pennsylvania

Stephen Herzenberg Biography

Stephen Herzenberg has been the Executive Director of the Keystone Research Center (KRC), an independent, non-partisan research and policy organization since December 1995. Dr. Herzenberg holds a Ph.D. in economics from MIT. Before joining KRC, Dr. Herzenberg taught briefly at Rutgers University and worked at the U.S. Congressional Office of Technology Assessment. Over the past decade, he has written extensively on the issue of pensions, including in Pennsylvania, Oklahoma and a half dozen other states. Most of Dr. Herzenberg's Keystone Research Center publications can be found online at www.keystoneresearch.org. Among his many other publications are: *Losing Ground in Early Childhood Education*, Economic Policy Institute, 2005; *New Rules for a New Economy: Employment and Opportunity in Postindustrial America*, Cornell/ILR press, 1998; and *Pulling Together or Pulling Apart?* Office of Technology Assessment, United States Congress, September 1992.

Oklahoma's DB Pensions Are Financially Sound

- The Plans' funded ratios are improving rapidly
- 5 plans now over the 80% funded threshold considered healthy
- Plans have performed well with high returns
- Cost-of-living adjustments foregone since 2011 while systems recover
- Plans implement best practices of well-funded plans
- Oklahoma's pensions are extremely modest – and overall public sector compensation even lower

OK Pensions: Funded Status Improving Rapidly

Plan	Actuarial Value of Assets (in millions)	Actuarial Accrued Liability (in millions)	Funded Status as of 7/1/2014	Funded Status as of 7/1/2013
Teachers	\$12,368	\$19,576	63.2%	57.2%
Public Employees (PERS)	\$7,759	\$8,754	88.6%	81.6%
Firefighters	\$2,002	\$3,225	62.1%	58.8%
Police	\$2,086	\$2,205	94.6%	89.3%
Law Enforcement	\$811	\$916	88.6%	81.4%
Judges	\$274	\$259	105.9%	97.3%
Wildlife	\$90	\$109	82.5%	77.6%
Total	\$25,391	\$35,044	72.5%	66.5%

10-Year Rate of Return: OK Plans Ranks 7th

OKLAHOMA STATE PENSION COMMISSION

Total Fund Performance Detail

	Market Value (\$)	% of Portfolio	3 Mo (%)	Rank	YTD (%)	Rank	1 Yr (%)	Rank	3 Yrs (%)	Rank	5 Yrs (%)	Rank	10 Yrs (%)	Rank
Oklahoma State Pension Commission	28,768,271,746	100.0	0.3	32	3.0	18	3.6	36	12.6	5	12.1	8	7.5	7
<i>S&P 500</i>			0.3	30	1.2	95	7.4	1	17.3	1	17.3	1	7.9	2
<i>Barclays Aggregate</i>			-1.7	99	-0.1	99	1.9	81	1.8	99	3.3	99	4.4	99
<i>60% S&P 500 / 40% BC Agg</i>			-0.5	86	0.8	98	5.3	3	11.0	36	11.8	14	6.8	38
<i>MSCI EAFE</i>			0.6	13	5.5	1	-4.2	99	12.0	11	9.5	73	5.1	97
Teachers	14,333,374,931	49.8	0.4	25	3.2	11	3.5	39	14.3	1	13.4	1	8.4	1
<i>TEACHERS Allocation Index</i>			-0.2	74	2.3	53	4.3	14	12.6	5	12.1	8	7.4	8
<i>TEACHERS Policy Index</i>			-0.7	92	1.5	86	2.1	78	11.1	33	11.7	14	6.9	31
PERS	8,625,829,142	30.0	-0.4	83	2.1	60	3.2	49	10.9	40	11.1	34	7.0	29
<i>PERS Allocation Index</i>			-0.6	88	1.6	84	2.8	61	10.3	50	10.4	49	6.6	49
<i>PERS Policy Index</i>			-0.5	86	1.9	72	2.8	61	10.2	51	10.6	44	6.7	42
Firefighters	2,259,982,760	7.9	0.9	8	3.7	3	5.9	1	12.5	5	11.8	14	6.9	31
<i>FIREFIGHTERS Allocation Index</i>			0.3	26	2.6	35	3.6	37	11.9	13	11.9	12	6.8	38
<i>FIREFIGHTERS Policy Index</i>			-0.1	65	2.1	60	4.7	6	12.1	10	12.3	5	7.1	22
Police	2,256,584,027	7.8	1.3	1	3.8	3	3.7	34	10.5	46	10.0	60	6.7	44
<i>POLICE Allocation Index</i>			0.3	28	2.5	38	2.4	69	9.4	74	10.7	44	6.4	61
<i>POLICE Policy Index</i>			0.1	43	1.9	74	0.7	94	9.4	74	10.8	38	6.1	75
Law	891,971,672	3.1	0.7	10	3.1	12	4.4	12	10.8	42	11.1	34	6.4	61
<i>LAW Allocation Index</i>			0.1	42	2.3	51	3.9	27	9.9	61	10.7	42	6.6	53
<i>LAW Policy Index</i>			0.2	34	2.6	35	4.6	9	10.8	42	11.0	37	6.8	38
Judges	300,720,516	1.0	-0.5	85	1.8	75	2.8	62	10.5	45	10.8	41	6.6	47
<i>JUDGES Allocation Index</i>			-0.5	87	1.7	81	2.5	67	10.2	51	10.4	49	6.3	64
<i>JUDGES Policy Index</i>			-0.5	86	1.9	72	2.8	61	10.2	51	10.6	44	6.3	63
Wildlife	99,808,698	0.3	-0.4	82	1.9	74	4.4	12	9.7	66	9.7	68	5.8	85
<i>WILDLIFE Allocation Index</i>			-0.5	86	1.5	87	3.9	27	9.3	77	9.5	73	6.1	74
<i>WILDLIFE Policy Index</i>			-0.6	87	1.0	97	4.9	4	10.0	58	10.5	46	6.6	52
<i>InvestorForce Public DB Gross Median</i>			0.0		2.3		3.2		10.2		10.3		6.6	

Additional Pension Changes in 2013

- To Firefighters' Pensions
 - Employee contributions from up from 8% to 9% of salary (and from 13% to 14% for municipalities)
 - Share of the state insurance premium tax dedicated to OFPRS increased from 34% to 36%
 - Increased retirement ages, vesting periods, and service requirements
- Future revenue surpluses above the cap on the Rainy Day Fund to a new Pension Stabilization Fund

Plans Use Best Practices of Well-Funded Plans

- They make actuarially required contributions since 2011-12
- Cost-sharing – OK employees contribute more to their pensions than workers in most states
- No COLAs or benefit improvements not paid for in advance
- Strong “anti-spiking” protections

These practices consistent with [the lessons from well-funded plans](#) identified by the National Institute on Retirement Security

OK Pensions Are Modest

- Average pensions for the two biggest plans only about \$20,000
- Public sector salaries below private sector...
 - Especially OK teachers: earn 20% less on average than teachers nationally – while overall OK wages only 12% below U.S. average
- Because OK teachers contribute 7% to their own pensions and have no automatic COLA, their pensions are now among the least generous in the country – 87th out of the biggest 100 plans in a National Association of State Retirement Administrators (NASRA) data base

Rep. Randy McDaniel Points to Progress

2011: “At a time when...other states in our country struggle to even address their structural debt problems, Oklahoma's financial condition is already exhibiting remarkable improvement.” Michael McNutt, “New Oklahoma Laws Credited With Improving State Pensions' Fiscal Shape,” *The Oklahoman*, November 11, 2011; online at <http://newsok.com/new-oklahoma-laws-credited-with-improving-state-pensions-fiscal-shape/article/3622054>

Sen. Mike Mazzei Points to Progress

May 2013, “We have made great strides over the last eight years...We have a law in place now that prevents new benefits from being proposed without thorough analysis – cost of living adjustments must now be paid for. The teacher system is finally on a path to fiscal stability and just this year we passed reforms which do the same for the firefighters system.”

The Case for Consolidation Is Not Compelling

Based on a study by the Center for Tax and Budget Accountability

- In the best-case savings from consolidation would be small (0.25%)
- The transition to consolidation has significant costs and risks
- The fees of all of Oklahoma's plans are relatively low
- Each system is well-managed and has good relationships with its stakeholders

Switching to Defined Contribution (DC) Savings Accounts Would Have Significant Costs

- Transition cost to DC of billions – \$40 billion projected cost in PA plans with 3.3 times the assets of OK plans
- 401(k)-type plans yield “less bang for the buck”
 - ...lower returns – people investing on their own do less well than professional managers
 - ...higher costs – Wall St. management, administrative, trading, annuity fees
- [National Institute on Retirement Security](#) estimates that
 - Typical 401(k)-type plans cost nearly twice the contributions for same benefit
 - “Ideal” DC plans have 41% higher costs

Real World Switch to DC: Alaska

- Moved all employees hired after July 1, 2006 into DC accounts
- State unfunded liability of \$5.7 billion ballooned to \$12.4 billion by 2014
- In 2014, the state made a \$3 billion contribution to reduce the underfunding
- Legislation has been introduced to move back to a DB pension plan.

Real World Switch to DC: Michigan

- The DB pension plan was overfunded at 109% in 1997 – and closed
- To “save money,” new state employees offered DC accounts
- By 2012, closed DB plan funded status dropped to about 60% – \$6.2 billion in unfunded liabilities
- In recent years, the state has been more disciplined about funding the pension plan, making nearly 80% of the ARC from 2008-2013.

Real World Switch to DC: West Virginia

- Teacher retirement system closed in 1991 to new employees
- Retirement insecurity increased for teachers with DC accounts – move back to DB plan in 2005 after a study found that equivalent benefits would be less expensive in the DB than in the DC plan
- By 2008, new teachers again covered by the pension, and most teachers who moved to the DC plan opted to return to the DB
- Plan funding level increased by more than 100 percent since 2005

QUESTIONS?