Testimony before the Joint Committee on Pensions Systems Review

Presented by: Carlton B. Washington, executive director, SC State Employees Association
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Good morning. Chairman Sheheen, Chairman Herbkersman, and honorable members of the South Carolina Senate and House, thank you for the opportunity to speak with you today.

I am Carlton B. Washington, executive director of the S.C. State Employees Association. We are a non-profit, non-partisan organization established to advance the welfare of state employees and retirees.

I am here today on behalf of the 32,442 classified state employees serving in all corners of South Carolina. I have come here today to be their voice and speak to you on their behalf.

These hard-working men and women are delivering vital services across our state—repairing our aging roads, preventing disease outbreaks, protecting our most vulnerable citizens from harm, inspecting our restaurants and places we take our family to eat, ensuring our air and water are clean, and yes, enforcing our laws.

South Carolina's five million citizens along with all the state's businesses depend on the services state employees provide. Their work is valuable to each one of us every day.

All of us have come here today to discuss what future retirement plans for state employees should look like. We are here to ask questions about what is best for both state employees and the taxpayers of South Carolina.

My message for you is simple and straightforward. On behalf of the more than 32,000 men and women who serve South Carolina as state employees, I appeal to you to stay the course with a defined benefit plan, better known as a pension plan. I appeal to you to stay away from a defined contribution plan, better known as a 401(k) or a hybrid. The 401(k) plan and hybrid are risky and unproven policies that haven't been proven over generations as pension plans have.

2011. The figure now stands at an alarming 9 percent, drastically higher than the national average of 5.98 percent.

Based on a 2016 survey of our members roughly 60 percent of state employees who took the survey would not recommend to professional colleagues that they seek employment with the state of South Carolina. (Attachment 4)

Too many state employees are having to get second jobs or seek public assistance to make ends meet. According to the 2016 survey I referenced, about 58 percent of state employees said they have worked additional jobs to supplement their family income. Roughly 70 percent believed their salary affected their morale, productivity, job satisfaction and retention.

Some of our most critical state agencies are having trouble recruiting and retaining employees. Consider these examples:

1. The Department of Health and Environmental Control DHEC needs many skilled professionals and experts who work to help build and maintain a public health system capable of preventing and responding to the various emergencies and outbreaks that sometimes arise. These public health and environmental control professionals cover chronic disease, aging, safe drinking water, disaster response, tobacco control and much more. The agency needs to be appropriately staffed to meet every day demands including investigating nearly 400 acute disease outbreaks and 55,000 disease reports a year, conducting more than 90,000 inspections covering a diverse range of programs, and having legal responsibilities that include more than 360 state or federal statutes, regulations and provisos.

2. DSS. Social workers' extensive caseloads contribute to South Carolina's failure to adequately protect elderly and disabled victims of abuse, according to a July 2017 Legislative Audit report. As of fall 2016, there were only 74 full-time social workers available to work with vulnerable adults in a state with 1.4 million elderly and disabled

adults.

3. SCDC. In the wake of an inmate's escape from a maximum-security prison, the head of South Carolina's prison system said his department is working to fill vacancies that have left the agency with too few officers. As of this summer, Bryan Sterling told a S.C. Senate panel that about 30 percent of SCDC posts are vacant. The department is trying to boost recruitment and retention and find ways to raise officer pay. For a while our corrections officers were making less than Walmart employees. Turnover rates at SCDC for first-year officers are as high as 50 percent. Several of our correctional facilities have taken drastic measures to recruit. For example, here are some of the "help wanted" signs posted outside of the Wateree Correctional Institution, which is in Kershaw County. (Attachment 5)

4. Our State Highway Patrol is losing more troopers each year than it's training – approximately 100 every year are jumping ship for local police or sheriff jobs. That costs millions of dollars in state money as we continue to have to recruit and train new people. The high officer turnover is compounding already critical problems in law enforcement and corrections in our state.

For all of these jobs, it's time to take a step back and recognize that one of state government's core functions is to provide for the safety of citizens—is South Carolina doing that or is the state cutting too many corners on pay and benefits?

These are just a few of the examples of the holes in state government because the jobs and benefits are, as the study commissioned by the General Assembly shows, "uncompetitive." Too many state employees are worn out by the stress, low pay, and risk. Dropping the pension plan in favor of a 401(k) style plan will only serve to make matters worse—much worse.

A fourth critical consideration in moving to a 401(k)-style plan or hybrid is that it likely could prove to be more expensive for the state and damaging to our economy, since returns are highly unpredictable.

Because in a 401(k)-style plan, members take control of most of the investment decisions affecting their accounts, so it leads to a wide range of investment returns. A 2011 Texas study looked at converting pension-style plans to 401(k)-style and found that two-thirds of its members would do significantly worse, receiving 60 percent or less of the current benefit.

The average worker has about $20,630 in a 401(k) plan in total accumulation.

It's a reality that if we abandon our pension-style retirement plan or even move to a hybrid, many retirees may be forced to seek state services just to live and become a burden in retirement for taxpayers, which could drain our economy.

For a state with an average 401(k) account balance of only $20,630—a mere fraction of what's needed to retire with dignity, the move would jeopardize the retirement security of state employees.

A fifth reason 401(k)-style plans or hybrids could be ineffective and damaging to our economy is that many people draw from them at some point for emergency purposes, leaving lower balances for retirement. If we keep the current pension plan, this will not be an issue.

Undoubtedly, not enough Americans have rainy-day accounts, so they fall into the trap of tapping their 401(k) when they get into trouble. As you might imagine, with fees and penalties, withdrawing out of 401(k)s can take a major bite out of retirement savings.

In addition to emergency expenses, another barrier to South Carolina state employees saving in 401(k)-style plans is that it just costs more to live. Sales tax on vehicles increased this summer to help fund road repairs and, as you know, citizens will be paying 2 cents more per gallon for gas. USC is planning the largest tuition hike in 6 years and the state's other universities have approved tuition hikes as well. It's getting more expensive to live. In Columbia, for example, homeowners and businesses will see their city property taxes increase on top of increases in water and sewer fees.

Another area I would like to focus on that supports the preservation of pensions is that a 401(k)-style plan would be more costly for the state for at least the next few decades. Changing course would raise costs before it lowers them, at least through 2034. The state also would face an increased risk from the closed pension plan that would run parallel to a new 401(k) plan for many decades. Unfunded labilities increase in the traditional system once the state switches new employees to a defined-contribution plan and fewer employees are able to retire with dignity in a 401(k) system. I remind you the average balance of a 401(k) in South Carolina is around $20,000.

According to a 2016 estimate, to move all new state employees to a 401(k) style plan would cost taxpayers $650 million more than the current retirement systems after five years.

Additionally, evidence shows that realization of cost savings and reduced liabilities are never met without significant reductions in benefits.

As one State Senator from Kershaw summed it up during last year's discussion, "moving all new state employees to a 401(k)-style plan "could be a very dangerous thing."

Moreover, there is considerable evidence and experience from other jurisdictions that can help us anticipate the likely consequences if we were to abandon pension plans for South Carolina's state employees.

In fact, several states and jurisdictions have looked at converting large public-sector pension plans to defined contribution or 401(k) plans or hybrids and have concluded that it would cost considerably more to maintain similar benefits. Two states that converted to 401(k) plans at least partially converted back because of concern over how little income they were producing for retirees (Nebraska and West Virginia).

In 2006, Alaska closed the pension plans for teachers and state employers and replaced them with individual 401(k)-type accounts. At the time Alaska closed its defined benefit plans, its unfunded liability was projected to be around 6 billion. By spring 2014, the unfunded legacy liability had grown to almost 12 billion, despite increased contributions by state agencies.

Michigan closed its existing defined benefit plan to new employees in 1997. At that time, it was 108 percent funded. By 2012, that funding ratio had fallen to 60.3 percent and the plan had an unfunded liability of $6.2 billion.

In Minnesota, an actuarial analysis concluded it would cost $2.76 billion over the following decade to convert to a 401(k)-style plan. The study also found that defined contribution members would be less likely to be able to support themselves in retirement and more likely to need taxpayer-supported public aid.

A study in New York City found that it would be 57-61 percent more expensive to deliver the same benefits under a 401(k)-style plan than it would with the existing pension plans.

When Palm Beach, Florida moved, in 2012, from a traditional pension to a hybrid defined benefit contribution plan, the city immediately felt the backlash. 24 public safety officers left for neighboring jurisdictions and another 28 left the following year.

In the case of Palm Beach, without competitive retirement benefits to offer, their police and fire departments became inexperienced and understaffed through depletion. In 2016, the city council voted to return to a traditional defined benefit pension.

In other words, transitioning this way simply has not worked in a lot of other places.
The consistent finding in theory and practice is that pension plans are more efficient at producing income from a given level of contributions than 401(k)-style plans or hybrids. So, pensions work better for the taxpayer and the employee.

According to the National Institute on Retirement Security, changing from pension to 401(k) does not decrease retirement plan costs, but drives up pension debt and almost certainly will increase retirement insecurity.

The state needs to do what it can to shore up pension plans rather than changing course.

The universally-accepted truth in the industry is that 401(k)-style plans or hybrids are less efficient generators of income than pensions. The 401(k) was never designed to be the primary retirement vehicle for working families. Gerald Facciani, former head of the American Society of

Pension Actuaries, said, "the great lie is that the 401(k) was capable of replacing the old system of pensions."

The reality is that some may see abandoning pensions for state employees as a way to improve our bottom line, but that is simply not true. We all recognize that money must come from someplace and that is the challenge. I suggest to you options such as reducing far-reaching sales tax exemptions as a potential revenue stream (3 billion annually).

What should happen, I believe, is that we should continue to strengthen our state's pension plan. The investment return for this year alone is over 11 percent – an extremely positive sign.

We must continue to do better by our employees in this state.

Pensions are the right choice, because:

1. Having quality state employees who dedicate long-term to serving is critical to providing core services of government to South Carolina citizens.
2. 401(k) plans have no proven track record over generations. It is too big a risk now, and for the future.
3. We need to look at shoring up our pension system and employee pay or we unnecessarily risk losing quality employees in droves. Unfortunately, what that means is we lose quality in the services we provide the public. Do we really want DHEC food inspectors, law enforcement or DSS employees who are not of the highest caliber and qualifications?

Let's be honest. Our state workforce is absolutely vital to the overall quality of life for all South Carolinians. We all depend on the quality of services provided by our state government.

The fact that we are being asked to consider a plan that's uncertain and without a track record over generations is bad for employees and bad for the state.

In the end, we need to stay the course and continue getting back on track with the defined benefits pension plan. It only makes sense to shore up what we have, rather than scrapping it all in favor of something that is, overall, inferior. Let's find the best solution for taking care of the people who make this state work. Thank you.