

# Attracting and Retaining a Qualified Public Sector Workforce

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## Overview -- Defined Benefit Plans

- DB plans are a key labor management tool for public employers which improve effectiveness and productivity, because they attract and retain employees.
- DB firms have longer employee tenure and lower turnover – 20-200 % lower. Turnover would increase under DC and cash balance designs.
- When given a choice, public employers and employees choose to stay with DB plans.
- In the event of a switch away from DB plans, employers and employees would face higher costs and employers would attract a different labor force.



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## Start of 2012 Football Season: NFL Fumbles on Pensions



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## DB Plans are Powerful Labor Management Tool

- DB plans prevalent in the public sector, make up 6.5% of total compensation.
- Research finds productivity gains linked to DBs.
- Firms moving from DB to DC experienced productivity losses relative to firms that kept DBs.
- Roughly 30% of public employees not covered by Social Security.

Source: NIRS, *The Great Recession: Pressures on Public Pensions, Employment Relations and Reforms*

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## DB Plans: Strong Recruitment and Retention Effect

- **Recruitment** - Employees with DBs twice the probability of citing retirement as important factor in taking the job.
- **Retention** - 69% of employees with DBs cite pension as an important reason to stay, versus 37% with DCs.
- **Result** - Lower employee turnover:
  - DB firms have lower turnover rates than non-DB firms, ranging from 20 – 200%.
  - DB coverage increases tenure by 4 years compared to no plan, by 1.3 years compared to a DC plan.

Source: NIRS, *The Great Recession: Pressures on Public Pensions, Employment Relations and Reforms*



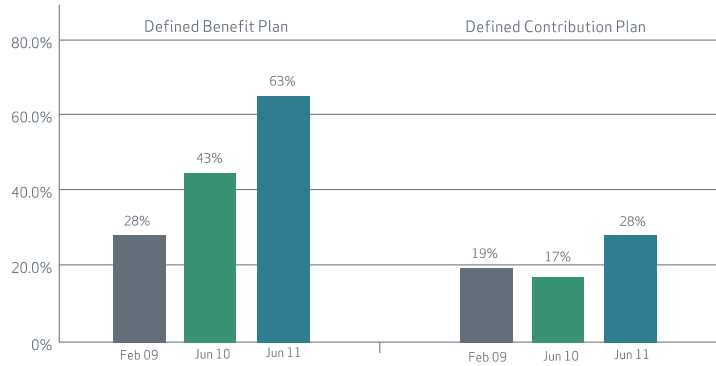
## Towers Watson: *Attraction and Retention; What Employees Value Most*

- In 2011, 63 percent of workers under 40 agreed their retirement plan was an important factor in accepting their job – jumping up from 28% in 2009%.
- More than three-quarters of new hires at companies sponsoring DB plans say the retirement program gives them a compelling reason to stay on the job.
- Among DB plan participants in 2011, 51% say the company's retirement program played a strong role in their decision to join the company, up considerably from 31% in 2009.

Source: Towers Watson, *Attraction and Retention; What Employees Value Most*

## Importance of Retirement Plans to Attract Workers Under Age 40

My company's retirement program is an important reason I decided to work for my current employer



Source: Towers Watson, *Attraction and Retention; What Employees Value Most*

## Most Important Factors in Attracting Employees Younger Than 40 to a Company

Younger than 40 with DB plan	Younger than 40 with DC plan only
1. Job security	1. Job security
2. Base pay	2. Base pay
3. Health care benefits	3. Health care benefits
4. Retirement benefits	4. Vacation/paid time off
5. Vacation/paid time off	5. Organization's reputation as a great place to work
6. Career development opportunities	6. Length of commute
7. Organization's reputation as a great place to work	7. Career development opportunities
8. Promotion opportunities	8. Challenging work
9. Incentive pay opportunity	9. Retirement benefits
10. Length of commute	10. Promotion opportunities

Source: Towers Watson, *Attraction and Retention; What Employees Value Most*

## Most Important Factors in Attracting Employees in 40s to a Company

	Age 40–49 with DB plan		Age 40–49 with DC plan only
1.	Health care benefits	1.	Health care benefits
2.	Base pay	2.	Base pay
3.	Job security	3.	Job security
4.	Retirement benefits	4.	Vacation/paid time off
5.	Organization's reputation as a great place to work	5.	Challenging work
6.	Challenging work	6.	Length of commute
7.	Vacation/paid time off	7.	Organization's reputation as a great place to work
8.	Career development opportunities	8.	Retirement benefits
9.	Length of commute	9.	Career development opportunities
10.	Incentive pay opportunities	10.	Relationship with supervisor/manager

Source: Towers Watson, *Attraction and Retention; What Employees Value Most*

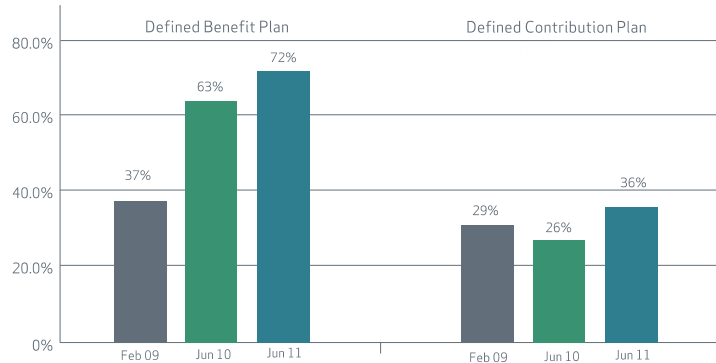
## Most Important Factors in Attracting Employees Age 50 and Older to a Company

	Age 50+ with DB plan		Age 50+ with DC plan only
1.	Job security	1.	Health care benefits
2.	Retirement benefits	2.	Job security
3.	Health care benefits	3.	Length of commute
4.	Base pay	4.	Base pay
5.	Challenging work	5.	Vacation/paid time off
6.	Vacation/paid time off	6.	Challenging work
7.	Organization's reputation as a great place to work	7.	Organization's reputation as a great place to work
8.	Length of commute	8.	Retirement benefits
9.	Career development opportunities	9.	Physical work environment
10.	Organization's product(s) or service(s)	10.	Organization's product(s) or service(s)

Source: Towers Watson, *Attraction and Retention; What Employees Value Most*

## Importance of Retirement Plans to Retain Workers Under Age 40

My company's retirement program is an important reason I will stay with my current employer



Source: Towers Watson, *Attraction and Retention; What Employees Value Most*

## Teacher Effectiveness Increases with Experience

- Teachers become more effective as they gain experience.
- Teacher effectiveness increases sharply within the first 3-5 years of teaching.
- When a mid-career teacher leaves and is replaced by an inexperienced teacher the school as a whole sees a drop in productivity.
- HR Goal: **Retain mid-career teachers, to maximize the school's overall productivity.**

Source: NIRS, *The Three Rs of Teacher Pension Plans: Recruitment, Retention, and Retirement*

## Teacher Turnover Patterns Fit HR Objectives and Lowers Cost

- Low turnover – retain highly qualified teachers.
- Youngest, least experienced teachers have highest turnover rates.
- 394,139 teachers turned over in 2003 out of nearly 3 million teachers across the nation.
  - 44% of these left the profession.
  - 56% transferred to another school.
- Turnover cost -\$12,443 per teacher add up to \$2.2 billion nationally.

Source: NIRS, *The Three Rs of Teacher Pension Plans: Recruitment, Retention, and Retirement*

## Alternative Retirement Plan Designs

- Defined Contribution plans: Employees face more risk
  - Longevity risk
  - Investment risk
  - Inflation risk
- Cash Balance plans are a “hybrid” of sorts
  - Technically DB plans
  - Notional (hypothetical) account, like DC
  - Pooled and professionally invested assets, like DB
- Both accrue benefits as a fixed earnings share, higher in earlier years than later, unlike traditional DB plans.

Source: NIRS, *The Great Recession: Pressures on Public Pensions, Employment Relations and Reforms*

# Annual Wealth Changes for New Teacher, Relative to Earnings

Figure 1:  
Annual Wealth Changes of Teacher Entering in 2011 Relative to Earnings,  
Under DB Plan, Cash Balance Plan, and DC Plan, Constant Normal Cost



Source: NIRS, *The Great Recession: Pressures on Public Pensions, Employment Relations and Reforms*

# Alternative Plan Designs

Table 1: Characteristics of Typical Pension Plans, by Plan Type

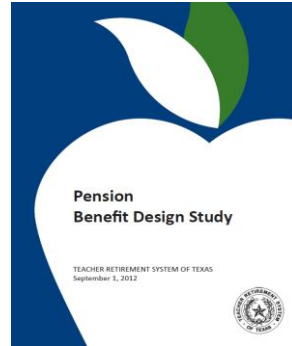
Characteristics	Defined Benefit Plan		Defined Contribution Plan
	Traditional	Cash Balance	401(k)/403(b) plans
Participation	Automatic	Automatic	Voluntary
Contribution	Employer and employee	Employer and employee	Employee with occasional employer matches
Investments	Determined by employer	Determined by employer	Typically determined by employee
Withdrawals	Annuity	Annuity or lump sum	Lump sum
Rollovers Before Age 65	Not permitted	Permitted if lump sum option exists	Permitted
Benefit Guarantee	Often Constitutionally guaranteed	Often Constitutionally guaranteed	None
Early Retirement Benefits	Common	Uncommon	Unavailable
Vesting	Up to a decade Or more	Typically shorter than in traditional pension plans	Typically immediate for employee contributions and often immediate for employer Contributions

Note: Cash balance plans typically do not exist in the public sector. The description thus relies on typical characteristics of private sector cash balance plans. Also, defined contribution plans are generally supplemental retirement savings plans in the public sector and thus tend to be voluntary.



## Texas Teachers Retirement System Benefit Design Study

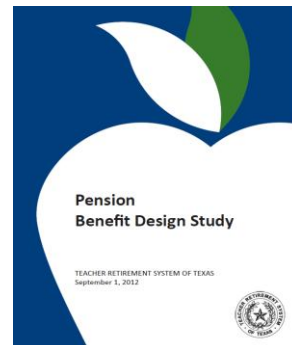
- \$11.7 billion/49% increase in closed DB plan liability due to a more liquid asset allocation
- Cost comparison of multiple plan design options
  - DC most expensive
  - DB least expensive



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## Texas Teachers Retirement System Benefit Design Study

- Simulations to realistically measure probable outcomes for workers in DC system:
  - lower returns
  - higher fees
  - market volatility
- Workers would have only a **50% chance** of reaching **60% of the benefit** provided by the DB plan, **at the same cost.**



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## DB Role in the Public Sector Increase Productivity

- DBs improve public sector productivity:
  - More likely to value their work than private workers.
  - Workers invest more in their skills.
- Moving to a DC design could negatively affect recruitment, retention, productivity among this workforce.

Source: NIRS, *The Great Recession: Pressures on Public Pensions, Employment Relations and Reforms*



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## DB Plans Encourage “Efficient Retirement”

- Employees withdraw from the labor force as their productivity declines.
- DBs can—and are—designed to facilitate appropriate and optimal retirement decisions.
- Crucial during economic downturns; no “job lock” with DBs.

Source: NIRS, *The Great Recession: Pressures on Public Pensions, Employment Relations and Reforms*



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## Market Values Cause Retirement Delays for those with DC plans

Federal Employees with TSP Accounts delayed retirement in Crisis:

- Overall retirement rate dropped from 20 % to 15%.
- 50 percent larger reduction in the retirement rate for FERS retirees compared to CSRS retirees.
- 37 percent of high income FERS employees delayed retirement even though TSP accounts were only 20 percent of their retirement income wealth.

Source: *Defined Contributions Pensions and Retirement Patterns*, Matthew Gustafson, SSRN 2012

## *Decisions, Decisions: Retirement Plan Choices for Public Employees and Employers*

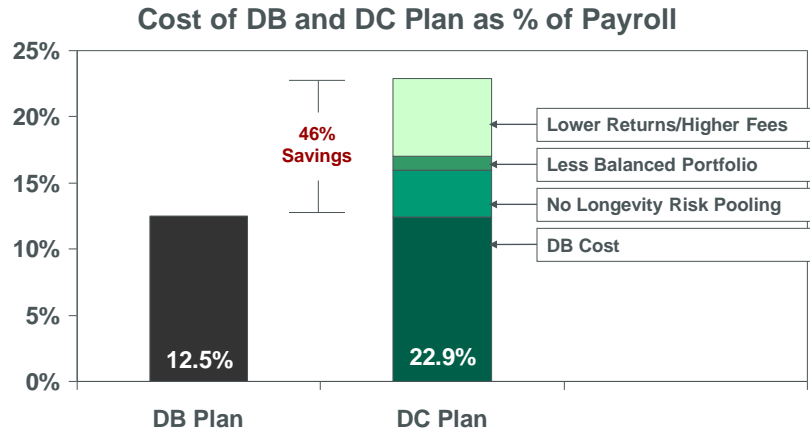
When given the choice between a primary DB or DC plan, public employees overwhelmingly choose the DB pension plan.

DB plans are more cost efficient than DC plans, due to:

- Higher investment returns
- Longevity risk pooling



## DB Plan Can Deliver Same Benefit at About Half the Cost of DC Plan



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## Decisions, Decisions: Retirement Plan Choices for Public Employees and Employers

Table 2. New Hire Elections in Most Recent Complete Year\*

System	DB Plan Enrollments	DC Plan Enrollments	Combined Plan Enrollments
Colorado Public Employees' Retirement Association	88%	12%	Not offered
Florida Retirement System	75%	25%	Not offered
Montana Public Employee Retirement Administration	97%	3%	Not offered
North Dakota Public Employees Retirement System**	98%	2%	Not offered
Ohio Public Employees Retirement System	95%	4%	1%
State Teachers Retirement System of Ohio	89%	9%	2%
South Carolina Retirement Systems	82%	18%	Not offered

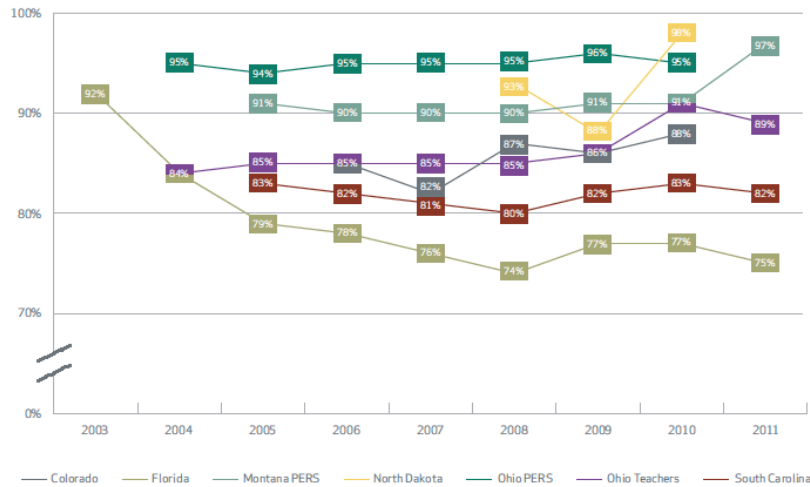
\*Not offered" means enrollment in a combined DB/DC plan is not offered.

\*Data for Colorado, North Dakota, and Ohio PERS are for January 2010 through December 2010. Data for Florida, Montana, STRS Ohio, and South Carolina are for July 2010 through June 2011.

\*\* One new employee out of the 63 eligible joined the North Dakota DC plan in 2010.

## Decisions, Decisions: Retirement Plan Choices for Public Employees and Employers

Figure 1. Total DB Elections over Time



## DB's Role in the Public Sector: The Retirement Plan of Choice

Public workers prefer DBs given a choice:

- 4% of Ohio employees opt for DC plan.
- 68% of Washington employees choose the DB plan over the default combined DB-DC.
- 75% of young teachers in West Virginia opted out of their DC plan and back into the DB plan.
- Utah lets employees choose between reduced DB hybrid and DC-only plan. 80% of new employees chose DB plan. Utah contributes a flat 10% of pay to either plan.

Source: NIRS, *Decision, Decisions: Retirement Plan Choices for Public Employees and Employers*

## Key Take Aways

1. Public employers would attract a different labor force if they switched retirement benefits away from DB plans. Employees would be less committed, and invest less in skills crucial to effective government.
2. Without compensation deferred into the future, employees have fewer economic incentives to stay. Employee turnover would increase under other plans.
3. In the event of a switch from DB plans, employers and employees would face higher costs. Due to both ending the existing DB plan and because of higher investment and administrative costs in the new plan.



## Questions?

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