Retirement Plan Design Examples

We are providing these examples to help the Commission better understand the decisions it is making. Neither the Department of State Treasurer nor State Treasurer Janet Cowell is endorsing one of these alternatives over another.

2. DB/DC Choice

This article provides some general background on DB/DC choice in other states:

2a. UNC Optional Retirement Program

The main features of this plan are:

- Defined contribution plan
- Available only to faculty and certain senior administrators
- One-time election between ORP and TSERS within 60 days of hire. Default election is TSERS.
- 5-year vesting for employer contributions
- Employee contributions and any vested employer balance can be rolled over to another defined contribution plan or an IRA if you leave the university at any age
- 6.84% of pay employer contributions
- Mandatory 6% of pay employee contribution. Additional voluntary contributions are possible through other plans offered by the university.
- Choice between four providers offering over 75 funds in total
- Income at retirement is based on investment returns and how you choose to withdraw your money.
- Several lifetime annuity options are available
- Participate in NC Disability Income Plan
- Continue to participate in State Health Plan in retirement

This website has further details on the program.

2b. Florida Retirement System

The main features of this plan are:

- Members have a six-month election window after hire to choose between the DB and DC plans. They are allowed one subsequent change after that window. The calculation of benefits upon a change in election is described on p. 7 of the Florida Retirement System document linked to below.
- There are no employee contributions to either plan.
- The employer contributes 9% of pay to the DC plan. Employee contributions are not permitted to that plan, although employers may provide supplemental plans for employee contributions.

- At retirement, the DC account can be used to buy an annuity with a 3% COLA from a private company (The Hartford). Participants can also choose a variable annuity fund invested in TIPS, which may behave somewhat like an inflation-indexed annuity.
- DC accounts vest after one year. DB benefits vest after six years.
- The DB benefit is 1.60% x 5-year average salary x service, with a 3% automatic COLA. It is unreduced at the earlier of age 62 or 30 years of service.
- At July 1, 2009, the employer contribution to the DB plan was 8.69% for general employees.
- In the most recent year available, 26% of new hires elected the DC plan. The DB plan is the default if no election is made.

The Florida Retirement System provides this document to help employees with the choice.

2c. New Utah plan

For Tier II public employees (new hires after July 1, 2011), Utah will provide:

- Choice between a DC plan and a hybrid (combination of DC and DB).
- The employer contribution is always fixed at 10% of pay.
- Employees who choose the DC plan will receive a 10% of pay employer contribution.
- Employees who choose the hybrid plan will have the DB portion funded by the employer contribution; any excess between the 10% contribution and the cost of the DB portion will go into the employee's 401(k) account; if the cost of the DB portion exceeds 10% of salary, the employee must contribute the difference to fund the DB portion and no employer funds will go into the employee's 401(k) account.
- DB portion of hybrid plan formula is 1.5% x 5-year final average salary x Service. Retirement is unreduced at 35 years of service. Retirees receive a COLA equal to cumulative CPI, up to 2.5% per year.
- The employer contribution for public safety/firefighter employees is 12% of pay and they can retire after 25 years.

While the choice is interesting, the most interesting feature of this design may be the 10% fixed contribution under the hybrid option. This has several impacts:

- As noted in the May meeting of the Commission, when you give choice between a DC plan that costs 6.3% of pay and a DB plan that costs 6.3% of pay, the resulting hybrid will cost more than 6.3% of pay because the late-career hires and people who expect to stay for a whole career will choose the DB plan, driving up its cost. If this effect is really strong in the Utah system, the cost of the DB plan will exceed 10% of pay and employee contributions will increase to cover that, reducing the incentive to pick the hybrid plan. Through this mechanism, the Utah design avoids this classic problem with choice, although the employees making the choice may not understand this feature until it has played out for a while.
- The investment risk is entirely shifted to the employees. If returns are high, then the required contribution to the DB plan will be low, leaving a large surplus to go into 401(k) accounts. If returns are low, then the surplus to go into the 401(k) accounts will be much smaller. If returns are really low, then the cost of the DB plan will exceed 10% and the employee contribution will increase to cover the extra cost.
- Other systematic risks, including mortality and to some extent inflation, are also borne by the employees because of the fixed 10% employer contribution.

For more information, see this webpage.

2d. South Carolina RS/ORP

The main features of this plan are:

- Choice between traditional DB and DC (401a) plan
- Available to all new permanent, full-time state, public school, and public higher education employees
- Election of plan required within 30 days of hire; can change from DC to DB one time between one and five years of service
- Employer contributions for both DB and DC plans is 9.24%
- Employee contributions for both plans is 6.5%
- Choice between four investment providers; 86 total funds
- No disability benefits with DC plan
- Distribution options for DC account include purchasing an annuity, lump-sum distribution, partial distributions, and periodic withdrawals

For more information, see this webpage.

2e. Vermont SRS

The main features of this plan are:

- Choice between DB and DC plan, but eligibility limited to exempt employees and employees in local government units that have elected to provide this option
- One-time irrevocable election
- Employer contribution of 7% (exempt state workers)
- Employee contribution of 2.85% (exempt state workers)
- Fidelity Investments is the sole investments provider
- Retiree health insurance if elected before retirement

2f. North Dakota PERS

The main features of this plan are:

- Choice between DB and DC, but only for non-classified employees
- One-time irrevocable election
- Employer contribution is 4.12%
- Employee contribution is 4%
- Complete vesting for employer contributions after 4 years
- Fidelity Investments is the sole investments provider; 28 funds available
- Disability retirement provisions; no disability insurance
- Distribution options include lump-sums, rollovers to qualifying accounts, and periodic distributions

For more information, see this webpage.

2g. Montana PERS

The main features of this plan are:

- Choice between DB and DC for all new hires
- One-time irrevocable election
- Employer contribution is 4.19% (+2.505% to maintain funding of DB plan)
- Employee contributions is 6.9%
- Complete vesting for employer contributions after five years of service
- Great-West Retirement Services is the sole investment provider; 15 funds available
- Participation in the Long Term Disability Trust Fund (0.3% ER contribution)
- Distribution options include lump-sums, rollovers to qualifying accounts, and periodic distributions

For more information, see this webpage.

2h. Colorado PERA

The main features of this plan are:

- Choice between DB plan, PERA DC plan, and three other state DC plans
- Election of plan required within 60 days of hire; can change between DB and DC (either way) once after two to five years of service
- Employer contribution is 10.15%
- Employee contribution is 8%
- Complete vesting for employer contributions after five years of service
- ING is the sole investment provider for the PERA DC; 21 funds available
- Participation in PERA Disability Program
- Distribution options for PERA DC account include purchasing an annuity, lump-sum distribution, partial distributions, and monthly installments

For more information, see this webpage.

2i. Ohio PERS

The main features of this plan are:

- Choice between traditional DB, all-DC, and combined plan for permanent public employees
- Election required within 180 days of new employment
- Members have three more chances to change their plan: 1st chance before five years of service, 2nd chance between five and ten years of service, and 3rd chance after 10 years of service but before retirement
- Employer contribution is 14% for all plans
- Employee contribution is 10% for all plans
- Ohio PERS is the administrator; 16 funds available

- No disability benefits
- A portion of the DC employer contribution is deposited into a Retiree Medical Account, which the member may use to purchase post-retirement health benefits
- 100% vesting for employer contributions after five years
- Distribution options include an annuity purchased from OPERS, partial distributions, payments for a guaranteed period, periodic payments, or any combination of these options

For more information, see this webpage.

2j. Ohio STRS

The main features of this plan are:

- Choice between traditional DB, all-DC, and combined plan for public school teachers and public higher education professors
- Election period during first six months of employment; if no choice is made, employee is defaulted into the DB plan
- Member must actively choose to stay in the all-DC or combined plan before the end of the fifth fiscal year of enrollment. If no active selection is made, member is defaulted into the DB plan
- Employer contribution is 14% for all plans (3.5% of all-DC plan contributions is used to fund DB unfunded liabilities)
- Employee contribution is 10% for all plans
- Ohio STRS is the administrator; 8 funds available
- No disability benefits
- No retiree health care
- 100% vesting for employer contributions to all-DC plan after one year
- Distribution options include rollovers to qualified accounts, lump-sums, and lifetime annuities

For more information, see this webpage.

The table on the following page summarizes choice designs in a few key areas.

	#1 – Employee Decisions	#2 – Plan Transfers	#3 – Relative Value	#4 – Guidance Offered
NC ORP	One	N/A	Roughly Equivalent	• Handbooks • Plan comparisons
Florida RS	Two	DB → DC: Keep both or transfer present value DC → DB: Transfer present value	Roughly Equivalent	• Handbooks • Plan comparisons • Workshops • Help Line • Modeling tools • Benefit comparison statement included with enrollment kit
Utah	One	N/A	Roughly Equivalent	• Unknown at this time
South Carolina RS	Two	DB → DC: Transfer present value	Roughly Equivalent*	• Handbooks • Plan comparisons • Modeling tools
Vermont SRS	One	N/A	Roughly Equivalent	• N/A (Option available to a small group of employees)
North Dakota PERS	One	N/A	Roughly Equivalent*	• Handbooks
Montana PERS	One	N/A	Roughly Equivalent	• Handbooks • Modeling worksheets
Colorado PERA	Two	DB → DC: Keep both DC → DB: Transfer present value	Roughly Equivalent*	• Handbooks • Modeling tools
Ohio PERS	Four	DB → DC: Keep both DC → DB: Transfer present value	Roughly Equivalent*	• Handbooks • Plan comparisons • Seminars (in-person and on web) • Help Line • Modeling tools
Ohio STRS	Two	DC → DB: Transfer present value	Roughly Equivalent*	• Handbooks • Plan comparisons • Seminars • Help Line

*There is a difference between the Normal ER Cost for the DB plans and the employer contributions to the DC plans in these systems; it appears that the intention was to keep the contributions rates the same for DB and DC. Keeping contributions the same may not be fair because the value of a DB plan to new hires is better represented by Normal Cost, not employer contributions.

3. DB/DC Combination (Hybrid)

This table compares hybrid plans in other states.

3a. Oregon

For new hires since August 2003, the program has the following features:

- The DB plan has a 1.5% multiplier for general employees and 1.8% for public safety.
- Benefits in the DB plan are unreduced at age 65 or at age 58 with 30 years of service.
- There is no employee contribution to the DB plan.
- COLAs are equal to the increase in CPI, capped at 2%.
- The DC plan has a mandatory 6% of pay employee contribution, although employers are allowed to pay this on behalf of the employee and many do.
- The DC contributions are invested in the DB fund and receive the same return as the DB plan. There are no other investment options, so employees bear the investment risk on this piece. This feature was intentionally designed to leave the investment decisions in the hands of professional investors, keep fees low, and give exposure to less liquid investments, although it also does not allow the participant to control the amount of risk they take.
- The DC account can be distributed as a lump sum or in equal installments. There appears to be no lifetime annuity option.

Oregon had a DB/DC hybrid prior to 2003, but guaranteed a high return on the DC component plus shared most gains when investment returns were good. The costs of that plan obviously surged in the 2000-2003 market downturn, leading to the design above.

Here is a brochure for the program.

3b. Georgia Employees Retirement System

For new hires since 2008, the program has the following features:

- The DB plan multiplier is 1%. Unreduced retirement is at age 60 with 10 years of service or at any age with 30 years of service. The benefit vests after 10 years.
- Employees contribute 1.25% of pay to the DB plan. Employers contribute the rest.
- In the DC plan, the employer matches 100% of the first 1% of salary and 50% of the next 4% of salary that the employee contributes, for a maximum employer contribution of 3% of salary.
- The employee is required to contribute at least 1% to the DC plan.
- The employees choose among 13 investment options in the DC plan.
- The DC plan offers a variety of withdrawal options, including a lifetime annuity
- Members prior to 2009 have a traditional DB plan, but may opt into the hybrid program at any time.

This web page provides more details on the new plan and the reasons it was adopted:

3c. Indiana (both public employee and teacher systems)

The program has the following features:

- The DB plan multiplier is 1.1%. Unreduced retirement is at age 65 with 10 years of service, age 60 with 15 years of service, or at age 55 with rule of 85. The benefit vests after 10 years.
- Employers contribute the full cost of the DB plan.
- There is a mandatory 3% employee contribution to the DC plan, although employers can choose to make this contribution on their behalf and many do. The account vests immediately.
- The employees choose among 6 investment options in the DC plan, including one that appears to be invested by the DB plan investment staff and guarantee a positive return.
- The DC plan offers a variety of withdrawal options, including converting your account into a larger benefit from the DB plan.

This handbook provides more details on the plan.

3d. Ohio (both public employee and teacher systems) – This describes the combination plan, which is one of three choices.

The program has the following features:

- The DB plan multiplier is 1.0%, except the public employee system is 1.25% for years in excess of 30. Unreduced retirement is at age 60 with 5 years of service, except the public employees can also retire unreduced at age 55 with 25 years or any age with 30 years.
- Employers contribute the full cost of the DB plan.
- There is a mandatory 9.5% or 10.0% employee contribution to the DC plan.
- The employees choose among 8 or 9 investment options in the DC plan, including one that appears to be invested by the DB plan investment staff and guarantee a positive return.
- The DC plan offers a variety of withdrawal options, including converting your account into an annuity with a fixed 3% COLA through the DB plan.
- Employees are given a choice between this combination plan, a traditional DB, and a DC.

This link provides more details on the plan.

3e. Washington State Plan 3

The program has the following features:

- The DB plan multiplier is 1.0%. Unreduced retirement is at age 65 with 5 years of service (10 in some cases).
- The DB benefit receives an automatic COLA equal to the increase in CPI, capped at 3%.
- Employers contribute the full cost of the DB plan.
- Employees choose to contribute between 5% and 15% to the DC plan, although they have limited ability to change the contribution rate once it is set.
- The employees choose among 11 investment options in the DC plan, including one that mirrors the return of the DB plan.
- The DC plan offers a variety of withdrawal options, including annuities that are provided through the DB plan in certain situations and private insurers in others.

- Employees are given a choice between this combination plan and a traditional DB. The default is the combination.

This handbook provides more details on the plan.

The following table summarizes the design features of the combination plans in a few key areas:

Plan	Relative Value of DB vs. DC	Source of DB Contributions	Source of DC Contributions
3a. Oregon	Roughly same	Employer	Employee, although employers may elect to pay on their behalf.
3b. Georgia	Roughly same	1.25% of pay from Employee, rest from Employer	Up to 3% of pay match from Employer, rest from Employee.
3c. Indiana	Value of DB is higher	Employer	Employee, although employers may elect to pay on their behalf.
3d. Ohio	Value of DC is higher	Employer	Employee
3e. Washington	Roughly same assuming minimum contribution to DC	Employer	Employee