Don't Fall for the Cash Balance Gimmick

Cash Balance Plans Cut Benefits and Fail to Retain Good Workers

Cash Balance Plans are defined benefit plans that combine elements of traditional pensions and defined contribution plans, like 401(k)s.

- They try to have it both ways, but end up falling short in meeting key goals.
- Workers who participate in cash balance plans have individual accounts, consisting of "pay credits" and "interest credits".
- The sum of these two ultimately determines how much the worker has for retirement, when the benefit can be taken as a lump sum or an annuity.

Cash balance plans are opaque in the most important area: it is not clear to individuals how much income they will have in retirement.
Traditional pension benefits are typically shown as a monthly or annual amount, not a lump sum. Cash balance plans require individuals to have a much higher level of financial sophistication to make reasonable decisions about retirement.

When states move away from a pension to a cash balance plan, they are redirecting resources to short-term employees and harming those who provided services to their community for decades.

- In public service jobs like teaching or firefighting, employees gain skills the longer they remain in the profession, which benefits the people they serve.
- It also costs taxpayers a lot of money to hire and train new staff.
- Encouraging people to remain in the profession is one of the strengths of traditional defined benefit pensions.
- It is a lose-lose proposition: Taxpayers pay more for higher turnover and lose the benefits of having seasoned professionals. Meanwhile, the workers who dedicate their life to serving their communities are harmed.

If cash balance plans are such a failure, then who is promoting them?

- Anti-pension billionaire John Arnold and his allies at the Pew Research Center
- Arnold and Pew have actively pushed for cash balance plans across the country from Kansas to Virginia and Alabama to New Hampshire.
- They were also involved in Kentucky, which recently switched to a cash balance plan.

Cash Balance Case Study: Kentucky

In 2013, Kentucky legislators agreed to a so-called “pension reform” package that included transitioning many employees out of a traditional pension plan and into a cash-balance plan. Kentucky’s public pensions are terribly underfunded due to decades of neglect by the state’s political leaders.

Instead of taking action to address revenue and funding options, politicians in Kentucky looked for quick fixes to the system. The result has been cutting benefits for workers while increasing the unfunded liability of the pension system and leaving taxpayers on the hook.

After two years of the Pew-promoted cash balance plan, the funding level of Kentucky’s public pension system has dropped by 9%—a far cry from the promised stabilization. Meanwhile, public employees hired after January 1, 2014 are now placed in the cash balance plan.

This is an effective benefit cut (without saving taxpayer money) that will ultimately leave some families living in poverty. Under the new cash balance plan, an employee hired at age 24 who retires at age 65 will see a 13% cut in their retirement benefit compared to what the traditional pension plan provided.