## Comparing Defined Benefit and Defined Contribution Retirement Plans

<table>
<thead>
<tr>
<th>Defined Benefit Plan</th>
<th>vs.</th>
<th>Defined Contribution Plan (Also known as a 401(k) or 403(b))</th>
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</thead>
<tbody>
<tr>
<td>Provides retirement income that lasts and cannot run out.</td>
<td></td>
<td>Does not guarantee retirement income will last through retirement.</td>
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<tr>
<td>Helps retirees budget with predictable, monthly retirement benefits</td>
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<td>Can experience dramatic fluctuations in account value with stock market downturns.</td>
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<td>Offers professional money managers who make investment decisions.</td>
<td></td>
<td>Requires that employee decide how to invest and spend down retirement savings.</td>
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<td>Has low fees.</td>
<td></td>
<td>Often have higher or unclear fees.</td>
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</tbody>
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### Defined Benefit Pensions Can Do More With Less

DB pensions can provide the same benefit as a defined contribution plan at about half the cost.

There are three reasons DB pensions are more efficient than DC plans:

- **10% savings**
  - Longevity Risk Pooling
  - Pensions only have to save for the average life expectancy of a group of individuals.

- **11% savings**
  - Balanced Investment Portfolio
  - Pensions are “ageless” and therefore can perpetually maintain an optimally balanced investment portfolio.

- **27% savings**
  - Investment Returns
  - Pensions achieve higher investment returns because they have lower fees and are managed by investment professionals.

**48% total cost savings**

- **Lower Cost DB Pension**
  - DB pensions can provide the same retirement benefit as a DC plan at about half the cost.
Switching from DB pensions to DC plans increases taxpayer costs, and does not reduce or eliminate any unfunded pension liabilities.

Some states have estimated the transition costs for switching from a DB to DC plan for public employees.

- **Estimated transition costs in New Jersey:** $42 Billion
- **Estimated transition costs in Pennsylvania:** $37 Billion
- **Estimated transition costs in Texas:** $11.7 Billion
- **Estimated transition costs in Indiana:** $3-$10 Billion
- **Estimated transition costs in Minnesota:** $2.8 Billion

Sources:
- How to Dig an Even Deeper Pension Hole by New Jersey Policy Perspectives
- Pennsylvania Public Employee Retirement Commission Actuarial Note
- Pension Benefit Design Study, Teacher Retirement System of Texas, September 2012
- Don’t Fix What’s Not Broken, Keystone Research Center, January 2015
- Retirement Plan Design Study, Minnesota State Retirement System, September 2011
- Case Studies of State Pension Plans that Switched to Defined Contribution Plans, National Institute on Retirement Security, February 2015

Pensions are effective at supporting retirement security for the middle class because they:

- Provide a modest lifetime benefit that doesn’t run out.
- Deliver a regular benefit so retirees have an easier time budgeting.
- Are professionally managed so that employees don’t have to make investment decisions.
- Do not allow participants to borrow or withdraw money before retirement.

In **Alaska**, the switch to a DC plans was sold as a way to slow down the increasing unfunded liabilities. Instead, the total unfunded liability more than doubled, ballooning to **$12.4 billion**.

In **Michigan**, the pension plan was overfunded at 109% in 1997. The state closed the plan to new employees, and the funded status dropped about 60%, with **$6.2 billion** in unfunded liabilities.

In **West Virginia**, the state closed the teacher retirement system in 1991 to new employees to address underfunding. Instead, the total unfunded liability more than doubled, ballooning to **$12.4 billion** by 2014.