Pension Reform Proposal Key Takeaways

- What is the current status of Pennsylvania's public pensions?
  - **$83 billion swing**: PA's pension funds went from a $20 billion surplus in 2000 to a $63 billion deficit as of 2015.
  - Without question, Pennsylvania's pension costs are crowding out other state programs and are the number one driver of school property tax increases.

- What is the new pension reform proposal?
  - The plan found in Senate Bill 1 is based on the **foundation of last year's Conference Committee Report.**
  - Senate Bill 1 would move away from the current risky full defined benefit system, offering a side-by-side hybrid option that pairs a 401(k) DC component with a smaller defined benefit component. Additionally, Senate Bill 1 provides new and current employees with the option of a full 401(k) DC style plan.

- What is the risk mitigation?
  - Pension system "risk" is the impact on employer (taxpayer) contributions when investment returns do not meet projected expectations.
  - **In terms of the dollar value of risk mitigated, Senate Bill 1 would be the largest reform enacted by any state in the country**, according to PEW Charitable Trust. According to the IFO analysis, the reforms in this legislation have **the potential to protect taxpayers from $6.5B to $13B or more over the projection period**.
  - Analysis shows that the proposed plan design changes on their own would reduce risk by 60% or more, including the employee contribution cost-sharing.
  - In a full risk transfer assessment by the Senate Appropriations Committee, when all employees have transferred to the plan, **the risk transfer can be scored at $26.9B if the systems miss their assumed rate of return by 1%**.

- What would be the fiscal impacts of the proposal?
  - According to the IFO report, the new plan will result in $1.4B in cash flow savings AND by the end of the projection period, the financial position of PSERS and SERS is projected to improve by $4.2B with regard to the unfunded liability. **These two numbers combined represent $5.6B in reduced cost of the system over the timeline of the analysis.**
  - **On investments, the reform calls for the state to take action on reducing investment fees by $3 billion**, increase investment fee transparency, and formalize the way the state plans for uncertain investment returns through the use of stress testing. Following through on each of these points will improve PA's national rank on investment fees, place the state among the leaders in investment fee transparency, and make PA an early adopter of stress test analysis.
  - On funding, the plan cements and increases the commitment to fully fund pension promises. Continuing on this path will move Pennsylvania from 49th to the top half of states on making required pension contributions and, according to PEW, **will represent one of the two largest turnarounds any state has enacted** (West Virginia being the other).

- Why is the media reporting "insignificant savings?"
  - First and foremost, with regards to SERS, savings generated by the plan were "plowed back" into the system, paying down the pension debt. This provision, while creating an overall savings to the system with regard to the unfunded liability, reduces the overall cash flow savings as protrayed by the media. A more accurate representation includes the $1.4B in savings generated from the plan design change AND the $4.2B in savings to the unfunded liability generated by the plan, totaling $5.6B in savings.
  - **Reporters are not counting the value of the risk transfer and, as stated by every national pension reform advocate, they should.** As the PEW Charitable Trust notes, their analysis indicates that Senate Bill 1 would be the most comprehensive and impactful reform any state has implemented. This is due to the long lasting impact of moving risk away from the taxpayer and sharing that risk with employees moving forward. **Monetarily, the value of the risk potentially can add an additional $6.5B to $13B in savings, according to the IFO, if the systems returns are lower than projected.**
  - As stated in the Senate Appropriations Committee meeting, the normal cost (the amount the employer pays if the systems hit their assumed rate of return over the course of the projection period) has gone from 9% of salary per employee pre-Act 120 to 0.5% of salary per employee under Senate Bill 1. Quite simply, we are at the end of the rope when it comes to generating more savings from the plan design. In previous pension bills, increased system savings were generated from making current employee changes. These current employee changes, while increasing savings, have not received support of the overall General Assembly, and would receive a court challenge.

- Why does the plan show cost in the early years for SERS and PSERS?
  - The cost increase is the result of a change in actuarial methodology – rather than anything to do with the new pension plans. Even including the actuarial changes, **over the medium- and long-term, these changes would save money for school districts and also make their costs more predictable.**
  - In fact, as the IFO reports, the new benefit reforms themselves are expected to save both systems combined in both the early, medium and long stages of the projection.

- What level of benefit will state employees and teachers receive?
  - **Overall, the benefit is designed to continue providing a path to retirement security for career workers while increasing retirement savings for many younger and mid-career workers who may change jobs due to the defined contribution component that all new employees will be a part of when the new plan begins.**
  - According to PEW, most workers who leave service with 20 years or less would receive a better benefit than current policy and most other states due to portable DC savings (SERS/PSERS data show more than 75% of teachers and over 50% of state employees leave their jobs before 20 years of service). The current system is designed to benefit employees who stay 30 or more years, not for today's more mobile workforce.

- Even more to the point, as the IFO has reported, a relatively high percentage of separations are attributable to employees with less than 10 years of service. For SERS, the figure for CY 2015 is 47 percent, and for PSERS, the figure for FY 2015-16 is 61 percent. Therefore, as an example, a SERS employee with a starting salary of $30,000 who separates after seven years of service **would receive or have access to $2,250 more in benefits under the DC-only option compared to the default hybrid option**.

◆ Does this bill impact current employees?

- Senate Bill 1 creates a new plan design for new employees starting on January 1, 2019 for SERS and July 1, 2019 for PSERS. At those times, ALL new employees (except the law enforcement classes) will enter into the systems in one of the three new plan design options. This includes lawmakers and judges.
- With regard to current employees, an option beginning on the start date for the new plans for ALL current employees (except the law enforcement classes) will be available to individuals currently in the systems. This includes current lawmakers and judges.
- Internal analysis has not been able to find another pension reform proposal in the country that provides an option for all current employees to enter into the new reformed system.

◆ Who is supporting the proposal?

- The Pennsylvania Chamber of Business and Industry
- The Greater Philadelphia Chamber of Commerce
- The Allegheny Conference/ Pittsburgh Chamber of Commerce
- The Pew Charitable Trust
- The Commonwealth Foundation
- ALEC
- Pennsylvania School Boards Association
- The Reason Foundation
- Retirement Security Initiative
- The Pennsylvania Institute of Certified Public Accountants