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Dear Senators and Representatives:

This letter includes Pew's preliminary analysis of Senate Bill 1 based on the actuarial note issued by the Independent Fiscal Office (IFO) on June 3, 2017. By voting in favor of Senate Bill 1, you have the opportunity to help ensure that the Commonwealth's retirement system is sustainable and secure for both taxpayers and public workers for decades to come. Pew supports passage of the bill because it would build upon previous legislation to achieve full funding of the state's pension system, lower costs and significantly reduce risk for taxpayers, and preserve a path to retirement for skilled public workers. Our research indicates that this would be one of the most – if not the most – comprehensive and impactful reforms any state has implemented.

Our analysis of the plan indicates that it:

- **Ensures Pennsylvania fulfills promises to state employees:** The bill maintains and extends the commitment to fully fund the state's pension system. Not only does this place Pennsylvania on a path to move from 49th in making pension contributions to the top half of states, it also is the biggest turnaround in contribution adequacy nationwide. Full funding will also lower costs for taxpayers in the long run.

- **Protects taxpayers by improving cost predictability:** SB 1 implements a risk-managed hybrid plan, including a 401(k) style component and a smaller defined benefit, in which employees contribute more when investments underperform. Meanwhile, the bill will help to ensure that core government services will be protected during future economic downturns by mitigating, according to our analysis of the IFO report, over 60% of unplanned costs – making Pennsylvania one of only seven states with risk mitigation of at least 50%.

- **Preserves and improves retirement security for more workers:** The legislation re-designs the benefit structure for new hires by introducing a hybrid defined contribution/defined benefit plan (see above). It continues to provide a path to retirement security for career workers – with expected replacement income of over 90% on average in retirement, including Social Security – while increasing retirement savings for many younger and mid-career workers who may change jobs. (note that approximately 25% of public workers and 40% of teachers nationwide do not participate in Social Security)

- **Saves Pennsylvania $5B to $20B ($2B to $9B in present value) over 30 years depending on investment performance:** According to the IFO, the bill projects cash flow savings of over $1 billion and an improvement of more than $4 billion in fiscal position if the pension funds achieve their assumed rate of return on investments. If investment targets are not met, the state will save an additional $5 to $12 billion ($2.6B and $5.5B present value). The reform also establishes an investment committee to target further cost reductions of $3 billion by lowering investment fees ($1.5B present value). Pennsylvania currently has the 5th highest fee levels across the 50 states.

Note that the IFO analysis of costs at lower returns is based on a rigorous and thoughtful methodology that is also somewhat conservative in terms of fully accounting for the savings afforded by cost sharing. Pew's subsequent review will provide additional details on the strong positive impacts of the bill's risk mitigation components.

- **Increases transparency:** The investment commission would also be called upon to evaluate emerging standards for alternative investment fee transparency and stress test reporting, actions designed to help policymakers plan for economic uncertainty. To date, only two other states have adopted both of these policy measures.

Thank you for your consideration of this important legislation. We urge you to support Senate Bill 1 and if you have any questions or would like to discuss our analysis, please do not hesitate to contact Chris McIsaac at cmcisaac@pewtrusts.org.

Thank you,

Greg Mennis
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