Keystone Research Center

To: Editorial Page Editors, Editorial Board Members, and Capitol Reporters & Columnists

From: Stephen Herzenberg, Ph.D., Executive Director, Keystone Research Center

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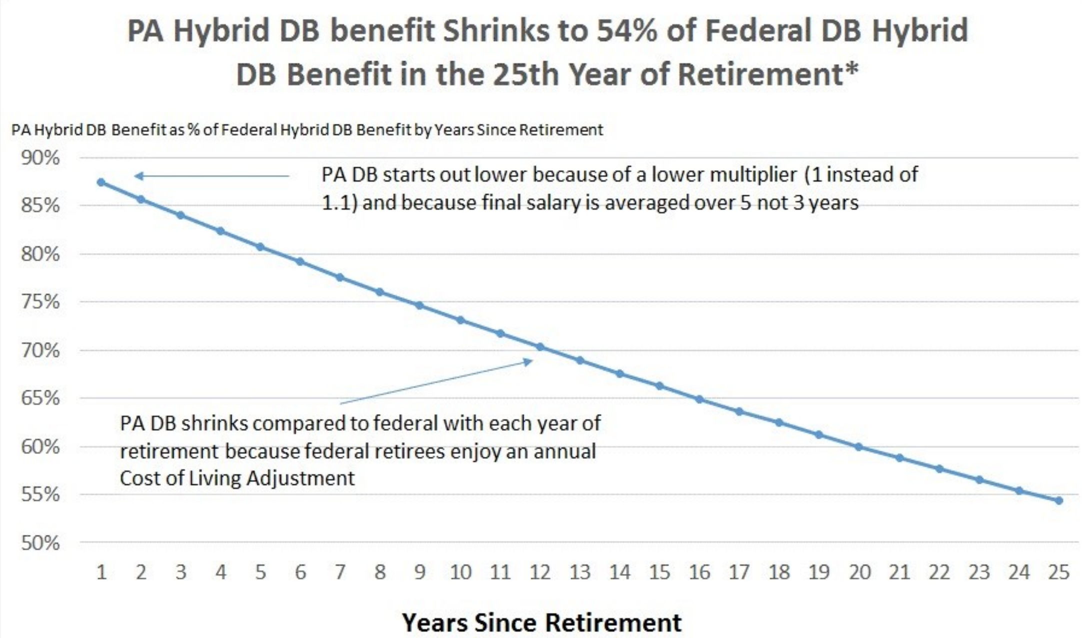
Re: Pennsylvania's Proposed Hybrid Pension

Pennsylvania's House of Representatives may shortly consider the proposed "hybrid pension" developed by the Pennsylvania Senate. The plan would significantly reduce benefits, increase taxpayer costs, and weaken the ability of schools and state agencies to attract and retain great staff. Far from being a "model," the proposed Pennsylvania hybrid would provide a much lower retirement benefit than the hybrid pension received by federal government employees and would, once again, delay pension payments in an irresponsible way that increases pension debt long-term.

Here are the key facts for editorial boards and news reporters as they inform their readers about the hybrid plan and whether it represents good public policy. If editorial boards or others have questions about the plan that are not answered here, please use the contact information above.

Large Benefit Cuts and Benefits Far Below Those of Federal Retirees

- The hybrid pension would cut benefits an estimated 17%-18% below the reduced benefit levels for public employees hired after 2010 that already give Pennsylvania retirees among the lowest public pension benefits in the nation.
- Contrary to some reports, the PA pension hybrid is far inferior to the retirement plan of federal employees that has been trumpeted as a model for PA – and it's not a close call.
  - By the end of a long retirement, the guaranteed benefit provided by the PA hybrid DB benefit would be worth only about half as much as the federal DB benefit.
  - The federal hybrid plan provides as much as twice the employer contribution to DC retirement savings (5% vs. 2.5%).
  - The Pennsylvania hybrid also provides less generous early retirement provisions, less (or no) post-retirement health-care coverage, and would require employees to contribute more to the DB plan if investment returns disappoint.



*Source for federal multiplier: https://www.opm.gov/retirement-services/fers-information/computation/. Impact of 5 vs. 3 year final average salary assumes a 4% increase in salaries each year (inflation plus 2%). Federal COLA assumed to be 2%,which it isif the actual consumer price index is between 2% and 3% so we assume 2%. For the FERS COLA rules, see https://www.opm.gov/retirement-services/retirement-faqs/?cid=422637f6-1d45-4863-9549-b2b605155b40. The Federal Reserve system long-run inflation projection isf 2% (see http://www.frbsf.org/economic-research/publications/economic-letter/2015/april/low-long-term-inflation-survey-based-forecast/).

- **A Change in the Rules – No PERC Note – to Avoid Due Diligence**: The Senate changed legislative rules to avoid having to wait for a report on the hybrid pension plan from the Public Employee Retirement Commission (PERC). A "PERC Note" is a due diligence step that helps lawmakers avoid costly pension policy mistakes. As of this writing, lawmakers are still being asked to act on the hybrid proposal without actuarial studies of its impact on pension costs or on retirement benefits.

- **Higher Pension Costs Because More Than Half of Retirement Contributions for New Employees Go Into Inefficient DC Savings Plans.** The PA pension hybrid would result in more than half (53%) of retirement contributions for new employers going into defined contribution savings plans that have higher costs and lower returns than traditional pooled pensions. As a result of this inefficiency, the cost of pensions for new employees would actually increase (by six tenths of a percentage point across Pennsylvania's two plans) even while delivering lower retirement benefits.

- **Another Costly Delay in Pension Payments**. The Senate plan would reduce pension payments this year even further below the amount recommended by pension experts (actuaries). The state's Public School Employees' Retirement System and many others have already come out against this delay, which will increase the state's pension debt.

Since the hybrid pension plan is not substantively tied to the state budget, it should be set aside or, at minimum, its provisions should be significantly improved. One option for replacing the revenue lost if pension payments are not reduced this year is to increase the minimum wage, which would save the state an estimated $231.5 million in Medicaid payments.

The Keystone Research Center is a nonprofit, nonpartisan research organization that promotes a more prosperous and equitable Pennsylvania economy.