

IFO Pension Analysis Policies

January 1, 2024

This document outlines the Independent Fiscal Office's (IFO) policies for pension analysis. These policies will be effective unless updated and reissued. A link to the relevant statute that confers pension review duties to the IFO can be found at the end of the document.

IFO's Role in the Pension Legislation Review Process

The IFO's role in the pension legislation review process has two basic steps. First, the IFO determines whether a proposed legislative change has a material actuarial impact to the system(s) specified in the legislation. Second, if the actuarial impact is not material, then the IFO will issue a letter (described below). If it is material, then a note will be issued and the IFO will facilitate an actuarial analysis with the impacted systems. Impacted systems could include:

- The State Employees' Retirement System (SERS)
- The Public School Employees' Retirement System (PSERS)
- The Pennsylvania Municipal Retirement System (PMRS)
- County and Municipal Governments

The IFO contracts with certified actuaries who work on its behalf to provide (1) input and commentary for the IFO's official actuarial notes and (2) advice and guidance to the IFO. The IFO currently contracts with two actuarial firms:

1. Milliman: Reviews proposed changes to state pension systems (SERS and PSERS)
2. Foster & Foster: Reviews proposed changes to municipal pension systems

The IFO, at its discretion, may also contract with other actuaries or financial consultants.

In general, an IFO response to a legislative request provides (1) a brief summary of the legislation and (2) a synopsis of any analysis included in the transmission to the General Assembly. The IFO may provide additional fiscal or economic analysis on an ad hoc basis, if the legislation has expanded impacts that warrant further consideration or explanation outside of the contracted actuaries' direct scope. The IFO may also request that actuaries include specific assumptions or scenarios in their analysis of the proposed legislation.

Types of Responses

The IFO issues **actuarial notes** (material actuarial impact) or **letters** (no material actuarial impact) in response to legislative requests for pension analysis.

There are various proposed changes that could trigger a material "financial and actuarial effect" that would impact forecasts such as employer contribution rates, amounts and unfunded liability. Examples include a change in the net investment return assumed by the systems, a change in funding structure (e.g., employer or employee contribution rates), post-retirement adjustments (e.g., ad hoc supplemental annuities or cost-of-living-adjustments) and benefit design changes (e.g., modification of defined-benefit and defined-contribution plans). By statute, all actuarial notes shall include reliable estimates of financial and actuarial effects from the proposed legislation and legislation that would result in a "substantial benefit design change" also requires the IFO to conduct a risk transfer analysis. A risk transfer analysis attempts to quantify the transfer of risk from employers to employees (or vice versa).

Actuarial notes, in general, have several characteristics that distinguish it from a letter:

- The proposed legislation has an actuarial impact that is material.
- The IFO submitted a formal request to the pension systems to perform simulations regarding the potential actuarial impact. Once a formal request is submitted, current statute provides the state systems (SERS and PSERS) with two weeks to transmit results to the IFO. The IFO includes the official system responses in its transmission to the General Assembly. County and municipal pension systems and related parties do not have a statutory two-week transmission deadline.
- The IFO's actuary is contacted to perform an analysis or opine on the output submitted by the systems. If the actuary performs work related to the request, the IFO includes that work product in its transmission to the General Assembly.

Statute does not specify a timeline for the IFO to transmit a letter or note. However, it does allow the General Assembly to advance legislation to Second Consideration if (1) the unamended legislation has been on First Consideration for 20 legislative days or (2) if 20 legislative days have passed since a request was made to the IFO to analyze an amendment to the legislation.

Response letters could include one or more elements of a note, but would not include all. For example, the IFO could contact the systems if a proposal imposes significant administrative costs, and include those estimates in a letter, but not include a simulation of actuarial impacts as there would likely be none. Alternatively, the IFO could reach out to its contracted actuary if there are potential material actuarial implications that cannot be known for certain or are not definitive.

Types of Analysis Outcomes

The manner (note versus letter) that the IFO responds to a legislative request is determined by the projected actuarial impact of the proposed legislation. There are four possible outcomes:

- **De Minimis:** The legislation has little, if any, financial or actuarial impact. These changes are generally technical in nature. Legislation in this category will result in a letter.
- **Not Material:** The legislation has a modest or moderate impact but would not materially impact the actuarial status of the system. When possible, the IFO will include an estimate of the financial impact or number of employees affected. This response will often include an estimate, or commentary, from the impacted system(s) and its actuary. Legislation in this category will result in a letter.
- **Potential Material Impact:** The legislation could have moderate or significant financial or actuarial implications, but the size of the impact is unclear and/or cannot be estimated reliably. In these cases, the IFO will request information from the systems to help determine whether an actuarial note is required. It may also request input from its contracted actuary. Legislation in this category will result in a letter.
- **Material Impact:** The legislation would have definitive, substantial actuarial impacts. Legislation in this category will result in a formal actuarial note.

For actuarial notes and letters, the term "material impact" is measured relative to current law (analysis of an unamended bill) or to the estimated net change to current law made by an amended bill. More specifically, for amendments:

- If an amendment further materially changes the original material impact of a bill, and the net impact is still materially different than current law, then a note is required.
- If an amendment essentially nullifies the material impact of the original bill, and the net impact largely reverts to current law, then it is not material and a note is not required, only a letter.

The IFO issues brief letters for legislation that results in de minimis (e.g., a technical correction) or not material (e.g., very small number of employees impacted) determinations. These letters provide a short description of the bill or amendment. They may also include limited commentary or analysis from the systems if relevant data are available (e.g., estimate of administrative costs, number of employees affected, modest actuarial impacts).

For proposed legislation with a potential material impact, the IFO will contact the systems and attempt to score out the impact of the proposal based on data and analysis supplied by the systems. The IFO will include any relevant analysis or commentary from the systems as part of an extended letter. The IFO may also contact its actuary in these cases, depending on submissions by the systems. This category would not include actuarial simulations.

For proposed legislation with a material impact, the IFO will issue an actuarial note. The IFO will work with its contracted actuary and coordinate efforts between the actuary, the systems and relevant legislative staff. As noted, these types of proposals may not directly impact the benefit design, but would have a material actuarial impact on the systems. In these cases, the IFO requests the systems and its actuaries to conduct actuarial simulations in a manner that facilitates the analysis of proposed legislation and its intent. The IFO may also provide additional financial or economic analysis based on the output from requested simulations.

Analysis Request Policies

Per statute, requests for actuarial notes can only be made by official requestors. These include:

1. President Pro Tempore of the Senate and Speaker of the House of Representatives
2. Majority Leader and Minority Leader of the Senate
3. Majority Leader and Minority Leader of the House of Representatives
4. Chairperson and minority chairperson of the Senate Appropriations Committee
5. Chairperson and minority chairperson of the House Appropriations Committee
6. Chairperson and minority chairperson of the Senate standing committee to which the bill is referred
7. Chairperson and minority chairperson of the House standing committee to which the bill is referred

Miscellaneous office policies regarding requests for pension analysis are as follows:

- The IFO will not disclose the status or confirm a request for an analysis of a bill or amendment to legislators or legislative staff that are not of the same caucus as the requesting officer.
- An analysis of a proposed amendment to a bill, or an amendment to an amendment, will not be issued until the analysis of the base bill or amendment has been completed. If an analysis of an amendment is requested that has not had a formal analysis of the base legislation (bill or amendment), the authorized requestor must also request an analysis of the legislation that is proposed to be amended.
- A formal request must be submitted on the letterhead of the requesting officer. The proposal to be analyzed should be included and drafted by the Legislative Reference Bureau (LRB) and include an official Printer's Number.
- Once a formal request is submitted, IFO staff may provide initial, informal feedback to requesting members or staff on legislative intent, general expected impact and other issues. However, the IFO cannot assist in drafting proposed legislative language. Drafting of language should be coordinated with the relevant pension systems and/or the LRB.
- The IFO is not able to expedite any analyses by the systems, nor can it comment on the current status of requests at the systems. For those questions, legislative staff should contact the systems directly.

- Depending on the complexity of the proposed legislation, members and legislative staff should anticipate that the IFO's actuary will require at least a few days and up to two weeks after receipt of system simulations to complete its work. For significant changes and complex legislation, the IFO's actuary will need at least a week to complete its work. On occasion, the IFO's contracted actuary identifies issues that must be addressed, and the systems must run additional simulations. Moreover, the IFO's contracted actuary cannot begin its work until the simulations and analysis are transmitted by the systems.
- After transmittal of a letter or note, the IFO can brief and answer questions from legislators, committees and caucuses on the analysis. The IFO may also release additional analysis, reports and studies regarding proposed and enacted legislation as described in statute.
- The IFO will transmit a letter or note to the requestor. Shortly after transmission, the IFO will post the analysis on its website and transmit the note or letter to all members of the General Assembly by email (per statute).

Relevant Statute

The IFO's duties for pension review and analysis are described in 615-B of the Administration Code of 1929 (Act of April 9, 1929, P.L. 177, No. 175). The code can be found at this link:

<https://www.legis.state.pa.us/WU01/LI/LI/US/PDF/1929/0/0175..PDF>.