

THE  
**PEW**  
CHARITABLE TRUSTS

**Remarks to the  
Jacksonville Task Force  
on Pension Reform**



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The Pew Charitable Trusts  
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## Three Areas of Focus

1. Paying down Jacksonville's pension debt
2. Considering new plan designs for Jacksonville's Police and Fire Pension Fund
3. Governance and investment practices



# 1. Paying down Jacksonville's pension debt

## Paying Down the Pension Debt

Policymakers have three options:

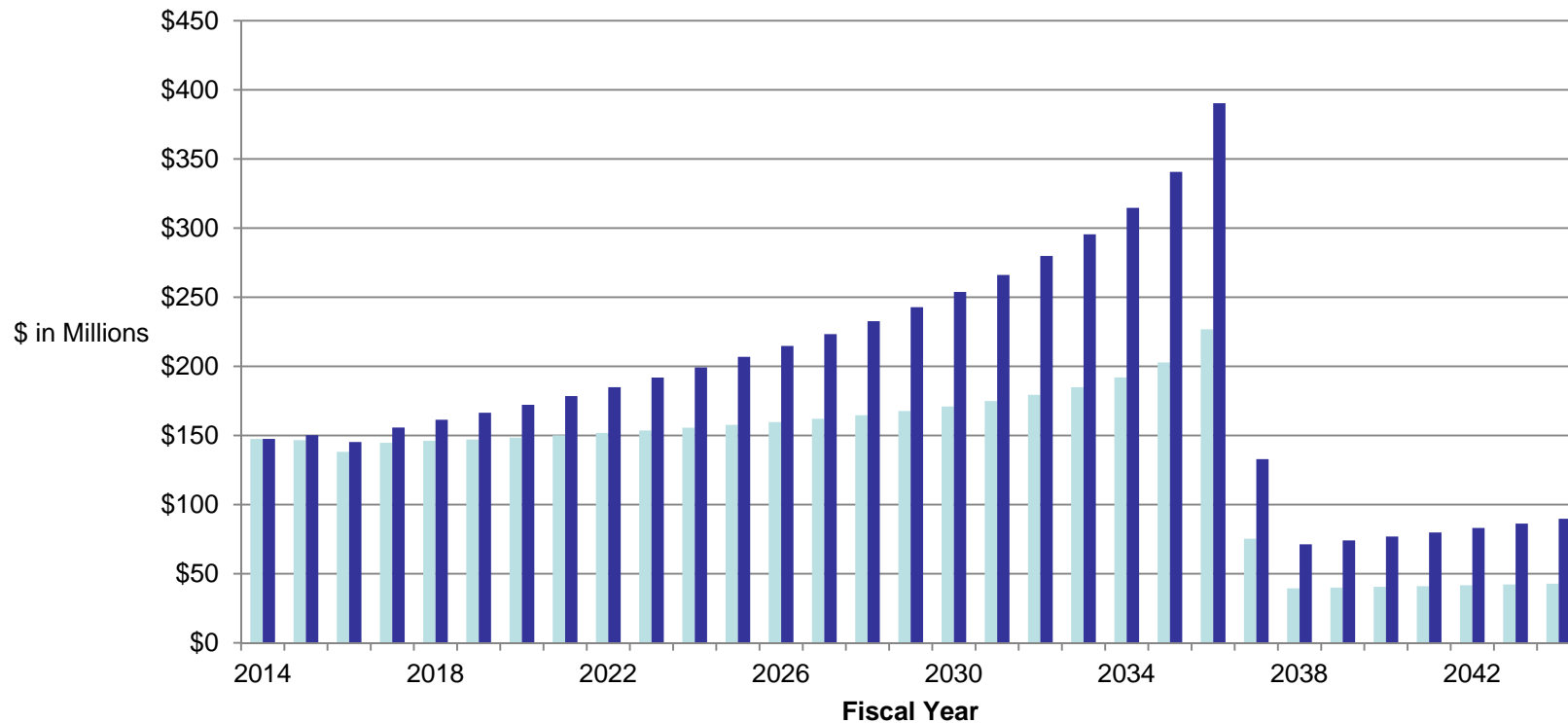
- Cut spending
- Raise revenue
- Ask current employees to contribute more

Whatever Jacksonville decides to do, it needs a credible plan to pay down the existing pension debt without threatening key government services, forcing unsustainable tax increases, or breaking the promise to workers and retirees.

Just like paying a credit card bill, the faster Jacksonville pays this debt off, the smaller the eventual cost will be.

## Annual Employer Pension Costs Baseline

Payments owed by the City of Jacksonville.



Source: The Terry Group, 2013

■ Adjusted For Inflation   ■ Nominal Dollars



## Paying Down the Pension Debt

Right now Jacksonville is on a slow path towards paying down its pension debt.

Finding the money to make those payments and to pay down the debt will be necessary for Jacksonville to find budgetary relief.

Any additional money, from raising revenue or trimming the budget, can be used for one-time contributions or ongoing pension payments. Policymakers will need to consider tough choices like raising property taxes or cutting back on government services in order to keep the promise to Jacksonville retirees.

## Paying Down the Pension Debt: One-Time Contributions

One-time contributions can help lower the existing unfunded liability, reducing the cost of paying down that pension debt. One-time contributions speed up the process of paying down the pension debt and the additional funds can immediately be invested by the plan to help generate returns

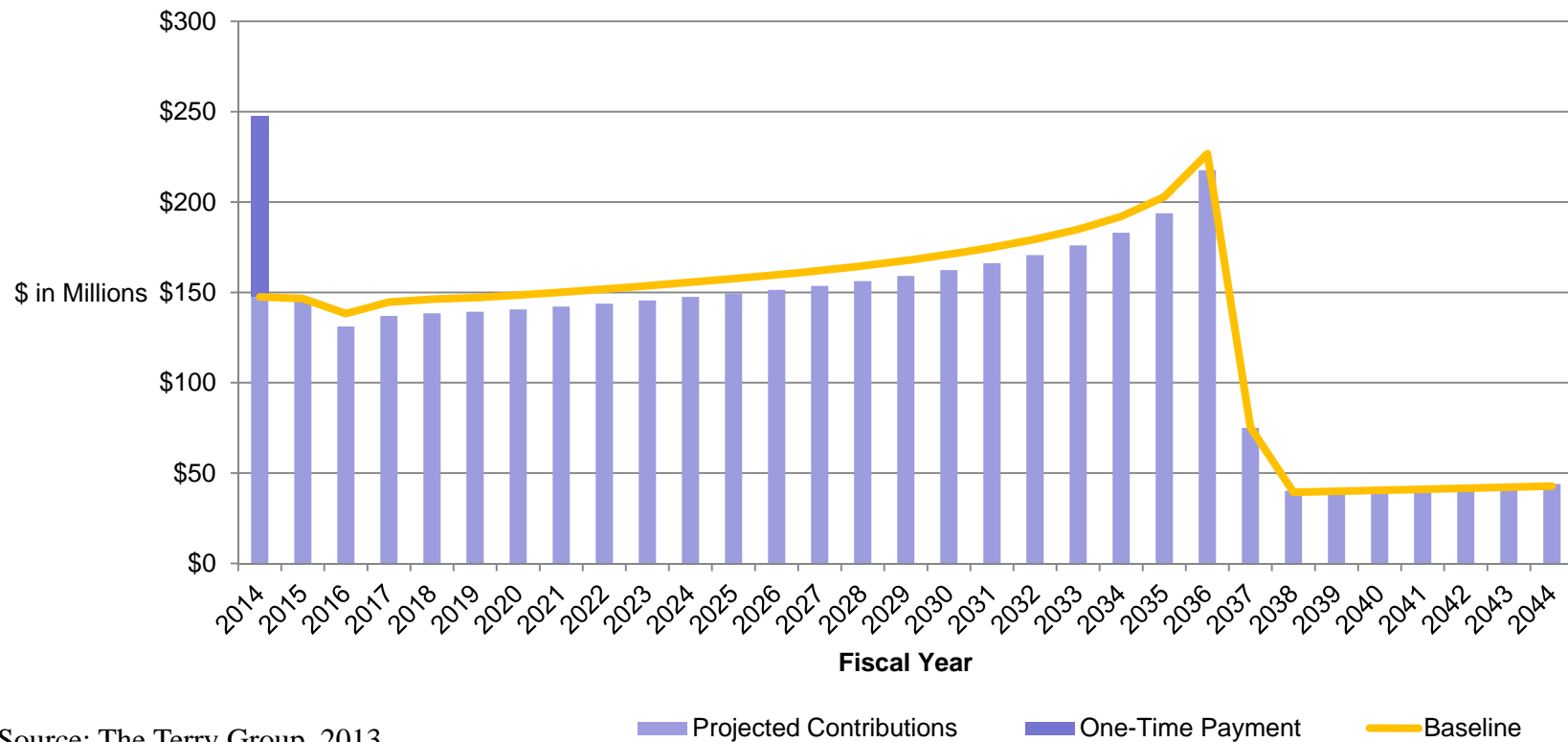
Potential sources include:

- Pension obligations bonds
- Real estate sales
- Selling other assets
- One-time revenue increases or spending cuts

We modeled a one-time contributions of \$100 million. With a \$100 million contribution in 2014, Jacksonville would save \$167 million in subsequent years for a net saving of \$67 million.

## Annual Employer Pension Costs One-time Contribution of \$100 million

Payments owed by the City of Jacksonville, adjusted for inflation.



Source: The Terry Group, 2013

■ Projected Contributions    
 ■ One-Time Payment    
 — Baseline



## Paying Down the Pension Debt: Ongoing Payments

Ongoing contributions are the basic approach to paying down the existing pension debt. Policymakers can find the money to dedicate to paying some or all of the existing required contribution or put in more than the scheduled requirement to pay down the debt faster.

Potential sources include:

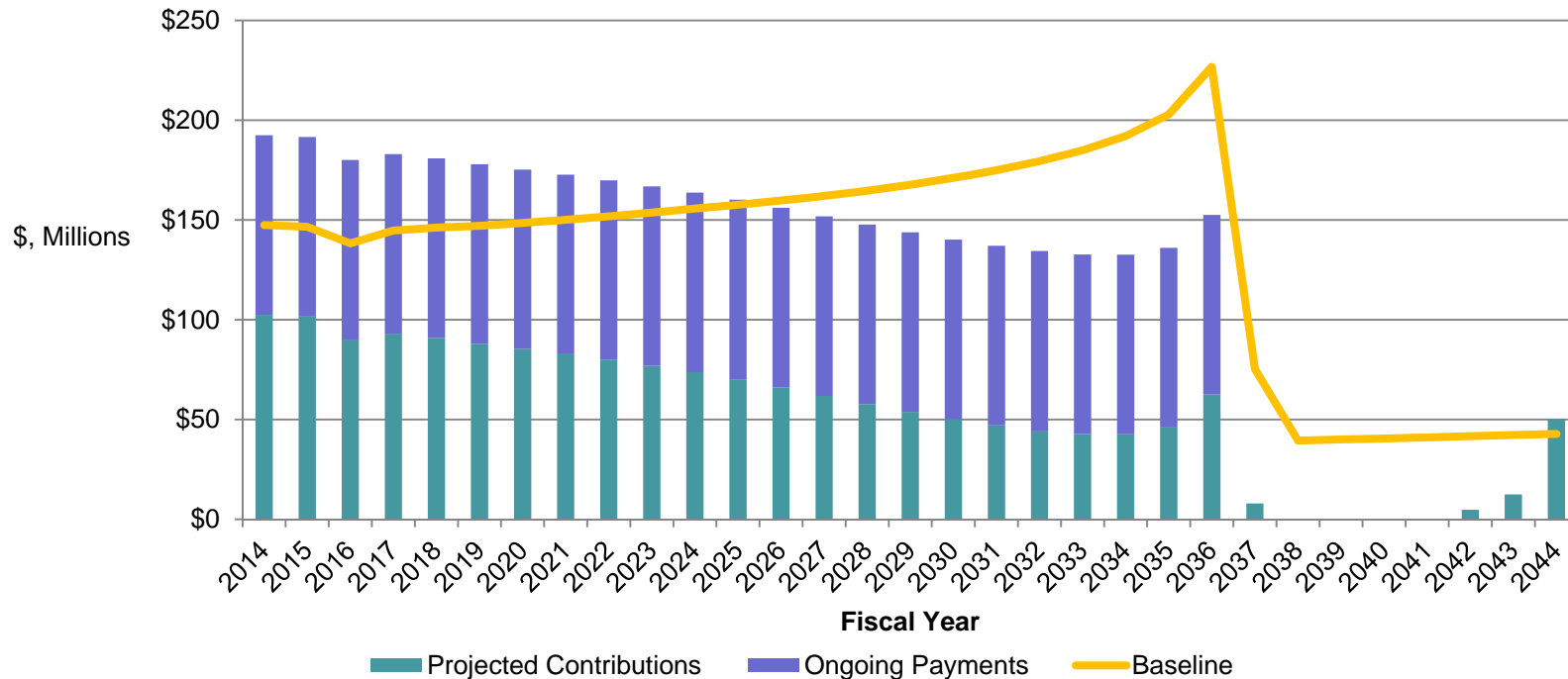
- Property taxes
- Jacksonville Electrical Authority
- Chapter Funds
- Other revenue raisers
- Ongoing budget cuts

We modeled an ongoing contribution of \$90 million where half the money helps the city make the required contributions and the remainder helps pay down the pension debt faster. We project this will reduce total contributions by more than \$380 million as the debt is paid down faster.

## Annual Employer Pension Costs

### Ongoing payments of \$90 million, split between paying the ARC and paying down the pension debt

Payments owed by the City of Jacksonville, adjusted for inflation.



Source: The Terry Group, 2013

## Paying Down the Pension Debt—Shared Sacrifice

There are four basic ways that Jacksonville can ask current employees to be part of the solution to the City's pension debt.

- **Increasing employee contributions:** This has been in several proposals including the Mediated Settlement Proposal which increased new employee contributions to 10 percent of pay and current employee contributions to 9 percent from 7 percent.
- **Reducing COLAS:** Florida legal precedent allows for changing COLAs for benefits not yet earned; a retiree's benefits cannot be changed, while someone early in their career can have their COLA benefit modified.
- **Modifying DROP:** It may make sense to switch the guaranteed interest credit to the assumed rate of return or allow it to float with actual investment performance.
- **Changing the benefit formula going forward:** The Civic Council proposed changing how benefits are earned going forward by current employees.



## 2. Considering new plan designs for Jacksonville's Police and Fire Pension Fund



## Plan Design for Jacksonville: Four Components of a Good Plan

1. Fully funded benefits; employers never skip contributions.
2. Secure path to retirement; all vested workers should accumulate meaningful retirement savings.
3. Use of professionally managed, low-fee investments; public plans should keep fees low and balance returns and risk on behalf of both employees and employers.
4. Access to annuities; workers should be able to get a lifetime benefit that will never run out.

## **Plan Design for Jacksonville: Two Questions to Ask**

- What is the best way for Jacksonville to provide a retirement benefit for public employees in terms of both offering retirement security and giving the right workforce incentives?
- What plan design will be affordable, sustainable, and secure over the long-run?



## Plan Design for Jacksonville

These approaches are targeted to all have employer costs of 10 percent of payroll and reflect proposals that have already been introduced to the Task Force or proposals that Pew has been asked to analyze.

### ➤ Traditional Defined Benefit Plans Proposals

- Plan proposed in Mediated Settlement Agreement
- Plan proposed by Jacksonville Civic Council
- Florida Retirement System benefits for new public safety workers

### ➤ Alternative Plans Pew Was Asked to Analyze

- Defined Contribution Plan
- Hybrid Plan
- Cash Balance Plan

## Plan Parameters: Current Plan

**Retirement Eligibility:** After 20 years of service.

**Vesting Eligibility:** Five years of service.

**Benefit Formula:** 3 percent of final average salary per year of service for the first 20 years, 2 percent for subsequent years with a cap of 80 percent.

**Salary Calculation:** Final average salary based on past two years.

**Employee Contribution:** 7 percent of pay.

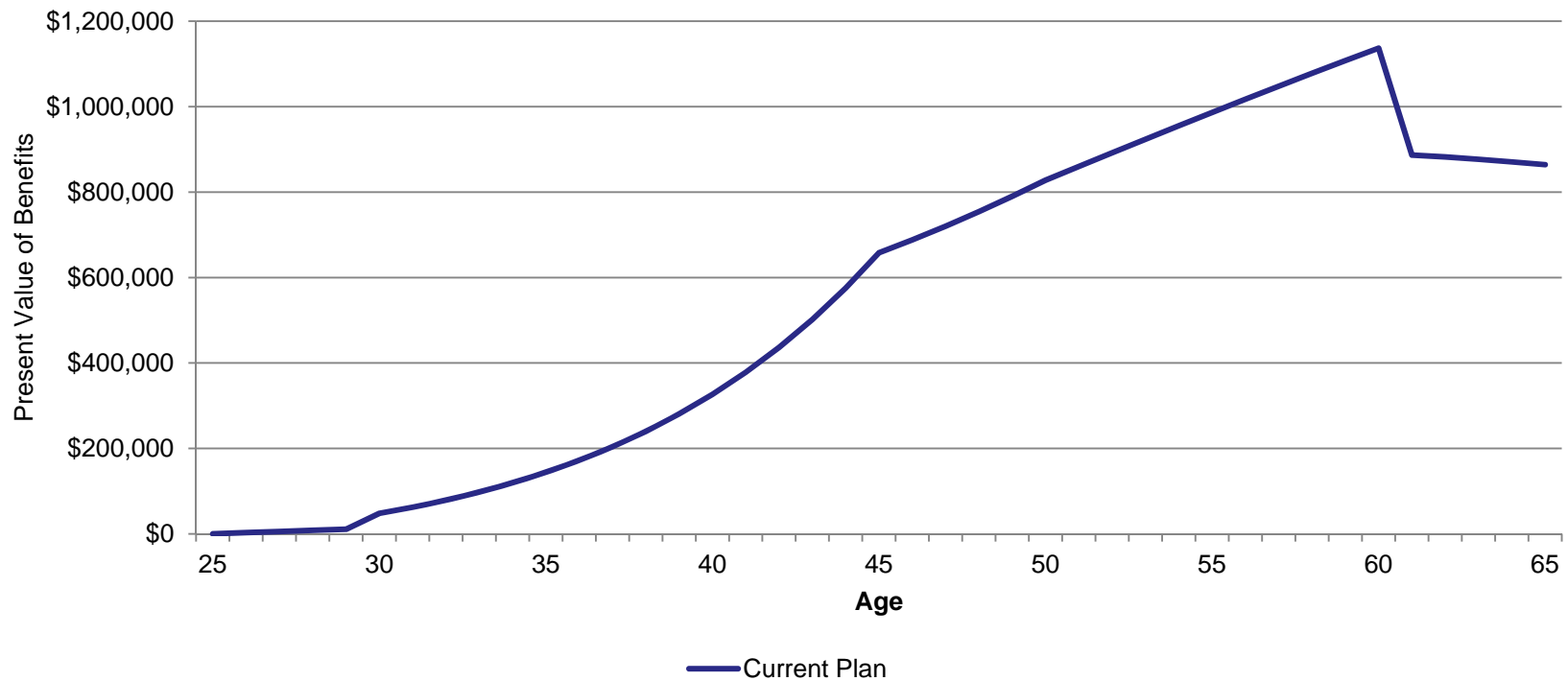
### Other Notes:

- Ancillary benefits, such as built-in 75 percent spousal benefit and the DROP plan, add to costs.
- Benefits include a 3 percent compounded COLA.
- The drop-off in the formula gives a substantial incentive to retire after 20 years of service; the plan assumes that 40 percent of employees who hit that point will retire or enter the DROP program in their 20<sup>th</sup> year.



## Retirement wealth accrual over a career under current PFPF Benefits

The value of earned retirement benefits



Source: The Terry Group, 2013  
Analysis based on new employee entering at age 25  
and is based on plan assumptions.



## Plan Parameters: Traditional Defined Benefit from the Mediated Settlement Agreement

**Retirement Eligibility:** After 30 years of service.

**Vesting Eligibility:** 10 years of service.

**Benefit Formula:** 2.5 percent of final average salary per year of service with a cap of 75 percent.

**Salary Calculation:** Final average salary based on past five years.

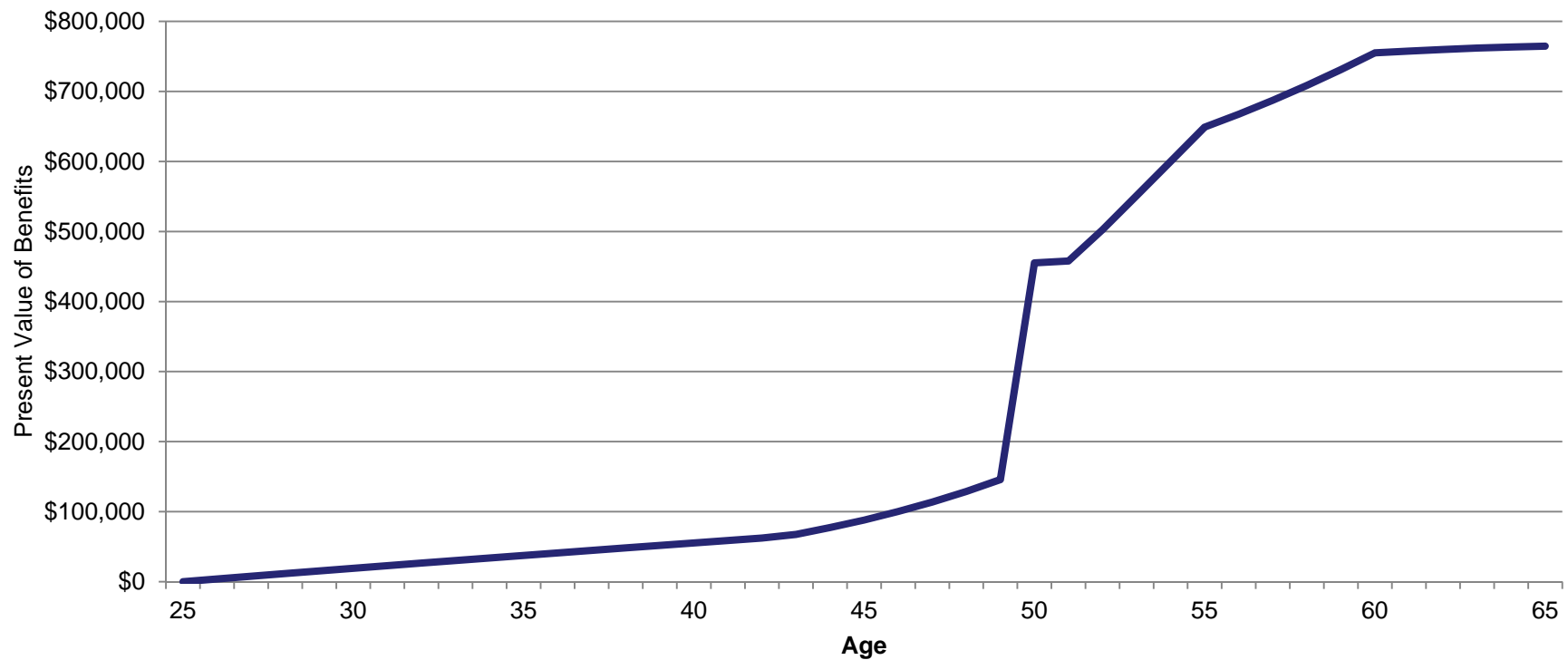
**Employee Contribution:** 10 percent of pay.

### Other Notes:

- Employees who leave before 30 years need to wait until 62 to retire and only get 2 percent of final salary per year—this lowers benefits substantially.
- COLAs are capped at 1.5 percent and only are granted three years post retirement.
- DROP is eliminated and annual benefits are capped at \$100,000.

## Retirement wealth accrual over a career under the Mediated Settlement Plan

The value of earned retirement benefits



Source: The Terry Group, 2013  
Analysis based on new employee entering at age 25  
and is based on plan assumptions.

— MSP



## **Plan Parameters: Traditional Defined Benefit from the Civic Council Proposal**

**Retirement Eligibility:** After 25 years of service.

**Vesting Eligibility:** 10 years of service.

**Benefit Formula:** 2 percent of final average salary per year for first 25 years of service, 2.5 percent for subsequent years with a cap of 65 percent.

**Salary Calculation:** Final average salary based on past five years.

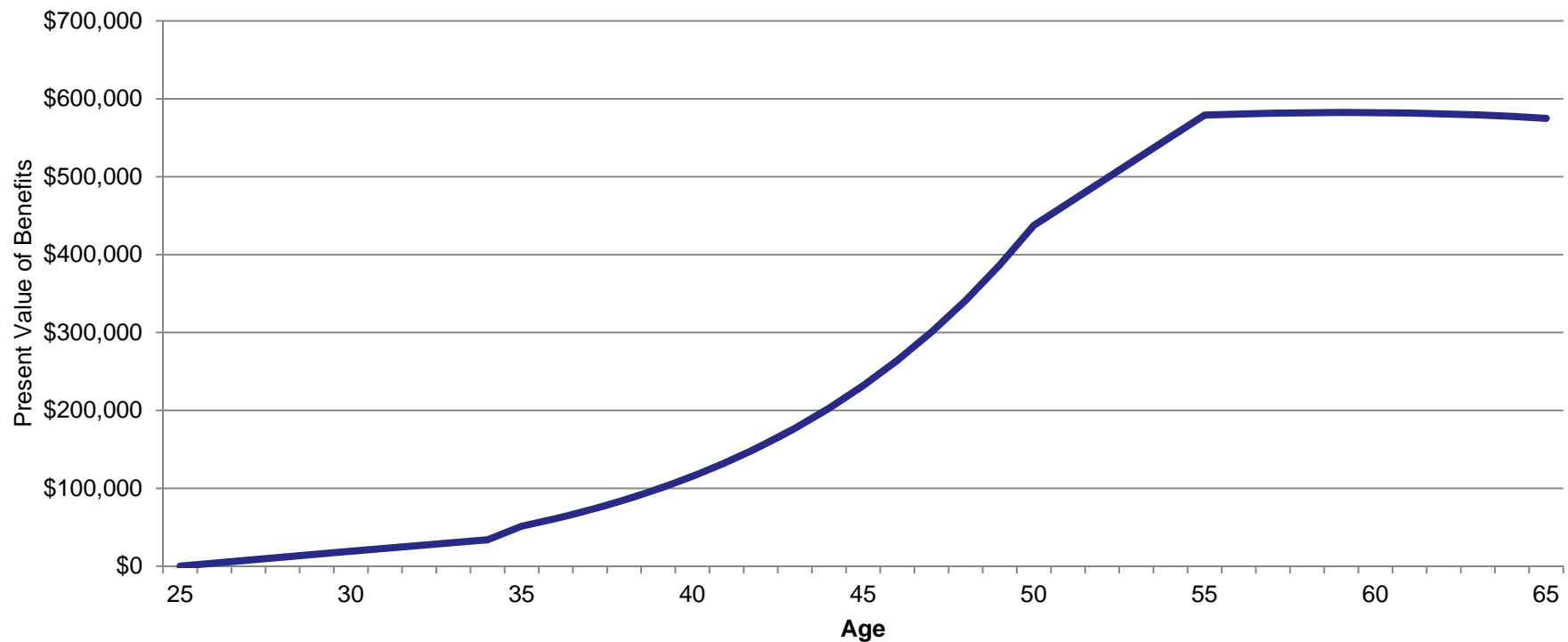
**Employee Contribution:** 10 percent of pay.

### **Other Notes:**

- COLAs are capped at 1.5 percent and only available when the plan is 80 percent funded.
- DROP is eliminated and annual benefits are capped at \$100,000.
- The Civic Council has also proposed reducing future benefit earnings for current employees.

## Retirement wealth accrual over a career under the Civic Council Proposal

The value of earned retirement benefits



Source: The Terry Group, 2013  
Analysis based on new employee entering at age 25  
and is based on plan assumptions.

— Civic Council



## Plan Parameters: Florida Retirement System Benefits for New Public Safety Workers

**Retirement Eligibility:** Age 60 or 30 years of service.

**Vesting Eligibility:** Eight years of service.

**Benefit Formula:** 3 percent

**Salary Calculation:** Final average salary based on past five years.

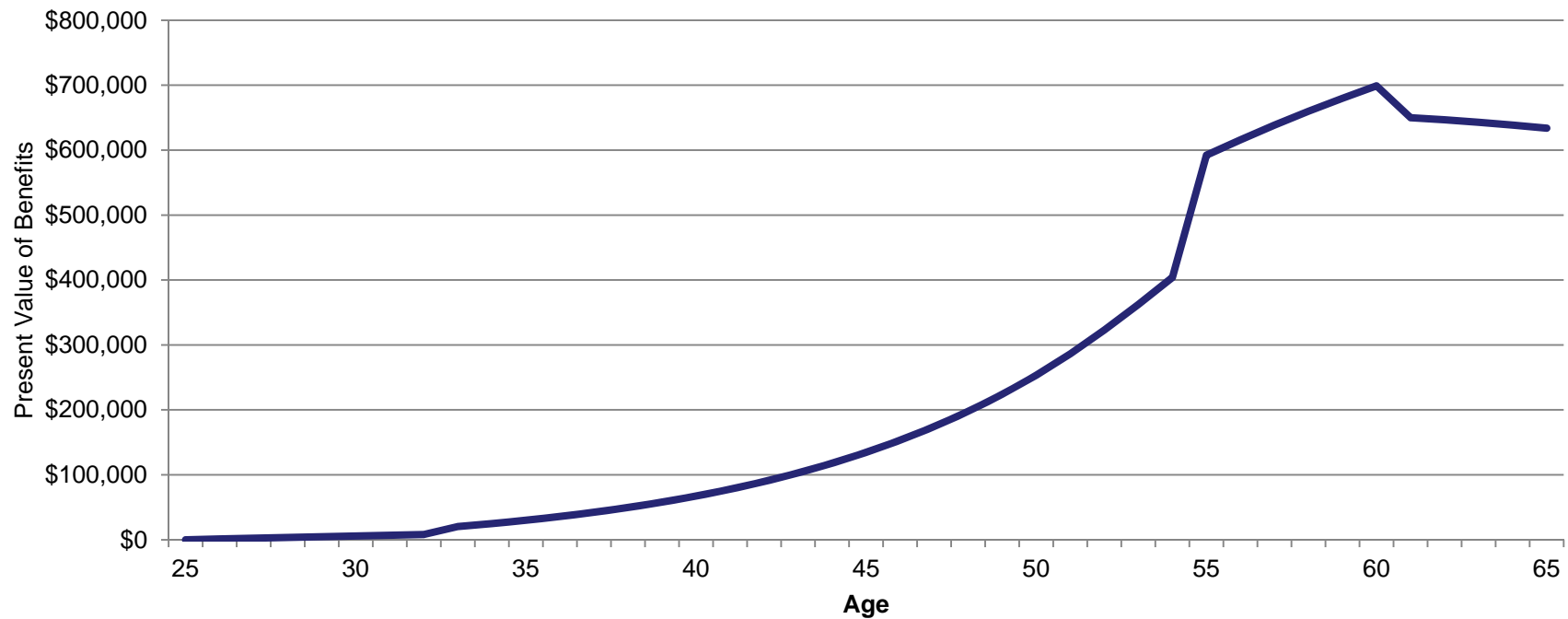
**Employee Contribution:** 3 percent of pay.

### Other Notes:

- Following recent reforms, employee contributions were raised to 3 percent, COLAs were eliminated, and retirement eligibility was made more stringent.
- Employee contributions for this plan are 3 percent of pay.
- Employees can access a DROP plan but employee accounts only receive 1.3 percent interest.

## Retirement wealth accrual over a career under the Florida Retirement System benefits for new public safety workers

The value of earned retirement benefits



Source: The Terry Group, 2013  
Analysis based on new employee entering at age 25  
and is based on plan assumptions.

— FRS

## Plan Parameters: Defined Contribution Plan

**Retirement Eligibility:** Age 60 or 30 years of service.

**Vesting Eligibility:** Five years of Service

**Pay Credit:** The employer puts in 10 percent of pay annually.

**Employee Contribution:** 10 percent of pay.

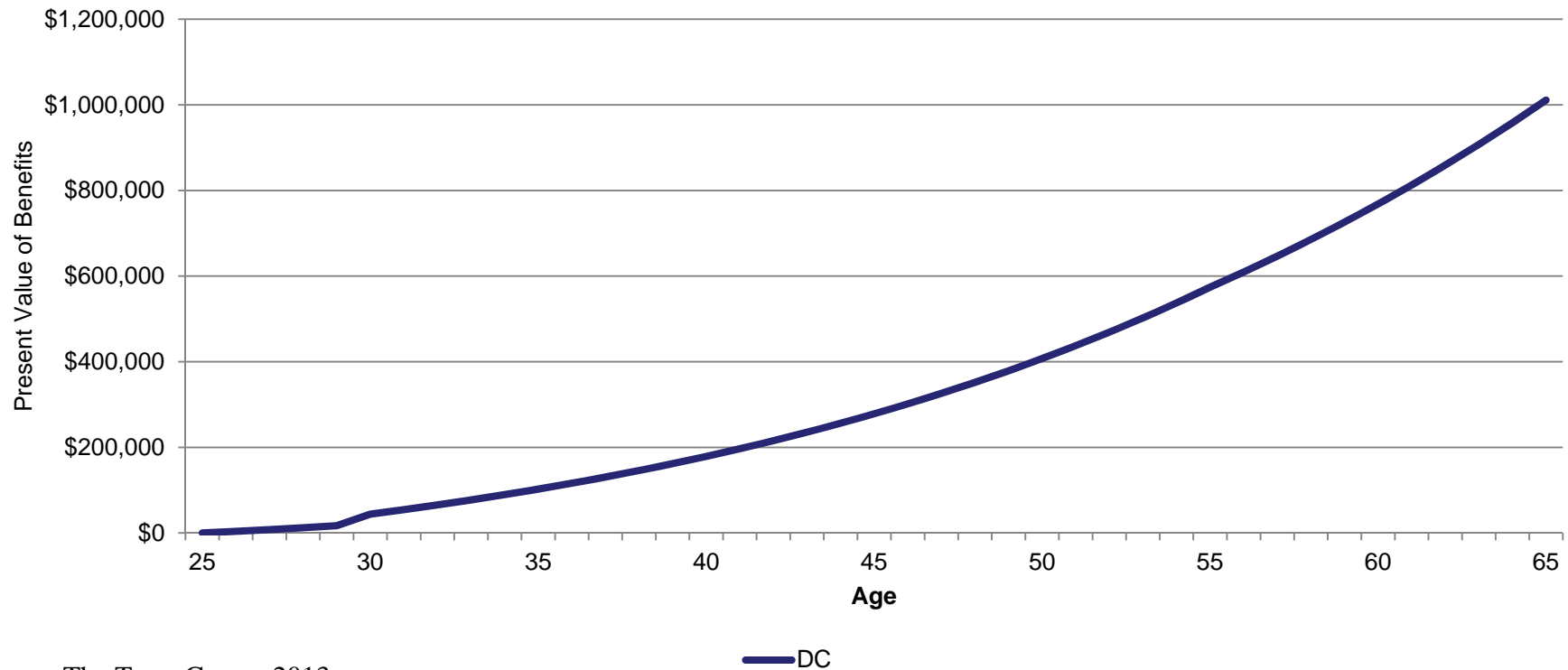
### Other Notes:

- In a defined contribution plan, employees bear all the risk. Employer costs are fixed at 10 percent of pay.
- A good defined contribution plan will include:
  - Low-fee, professionally managed investments that give employees a limited set of appropriate investment options.
  - Easy access to annuities so retirees are never at risk of running out of retirement savings.
- Benefit projections assumes worker accounts are managed by PFPF or equivalent and actuarially fair annuities are available at retirement. Benefit projections assume plan meets investment targets.



## Retirement wealth accrual over a career under a hypothetical defined contribution plan

The value of earned retirement benefits



Source: The Terry Group, 2013  
Analysis based on new employee entering at age 25  
and is based on plan assumptions.

## Plan Parameters: Hybrid Cash Balance Plan

**Retirement Eligibility:** Age 60 or 30 years of service.

**Vesting Eligibility:** Five years of service

**Pay Credit:** The employer puts in 10 percent of pay annually.

**Employee Contribution:** 10 percent of pay.

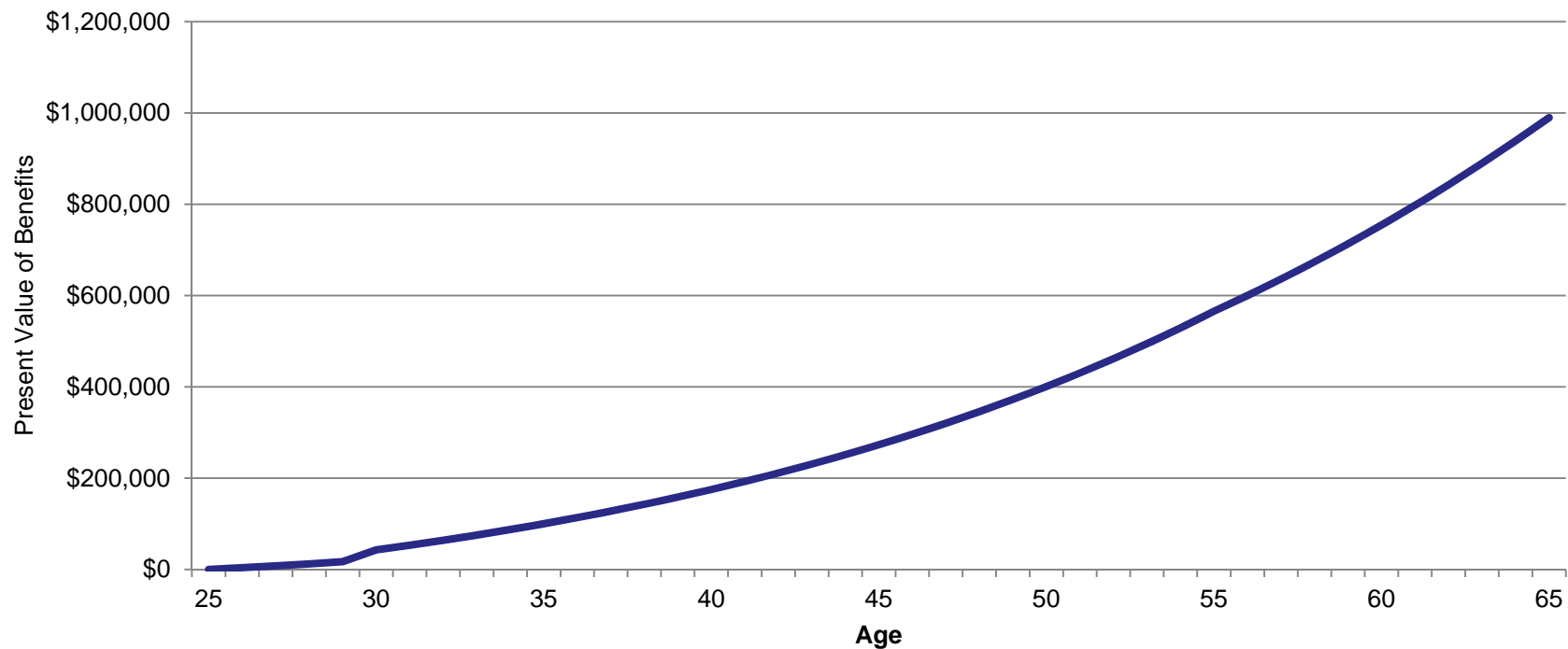
**Interest Credit:** 4 percent guarantee; employee accounts credited with 75 percent of returns above 4 percent based on a 5 year rolling geometric average.

### Other Notes:

- Cash balance typically share investment risks with employees; workers get a guaranteed minimum return and a portion of anything above that guarantee.
- The plan must offer annuities to retiring employees, this should be done at an actuarially fair rate.
- The interest crediting rules are projected to pay for themselves.
- Benefit projections assume plan meets investment targets.

## Retirement wealth accrual over a career under a hypothetical cash balance plan

The value of earned retirement benefits



Source: The Terry Group, 2013  
Analysis based on new employee entering at age 25  
and is based on plan assumptions.

— Cash Balance

## Plan Parameters: Stacked Hybrid Plan

**Retirement Eligibility:** Age 60 or 30 years of service.

**Vesting Eligibility:** Five years of service.

**Defined Benefit Formula:** 1 percent of final average salary per year of service.

**Salary Calculation:** Final average salary based on past five years.

**Defined Contribution Pay Credit:** 5 percent of pay from the employer, 10 percent of pay from the employee.

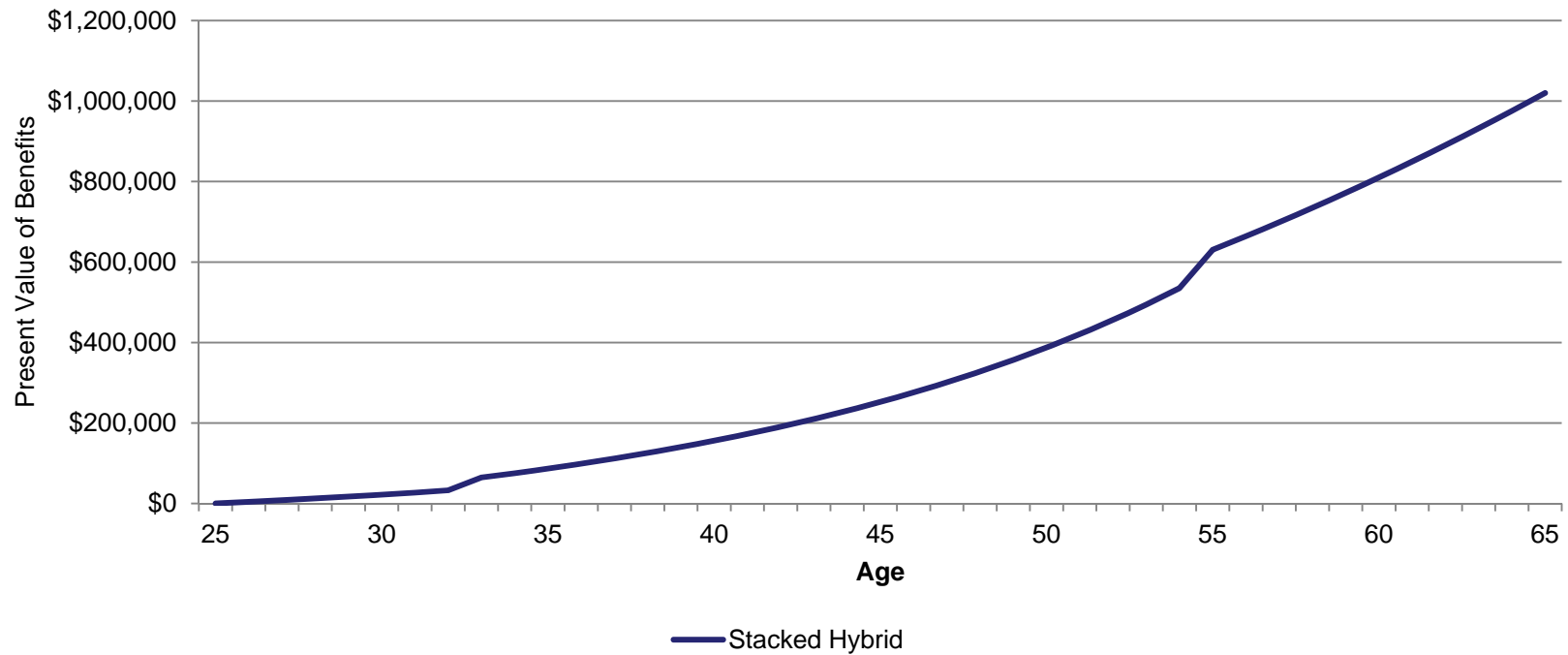
**Employee Contribution:** 10 percent of pay.

### Other Notes:

- Benefit is based on the defined benefit formula and the defined contribution account.
- The defined contribution account needs appropriate investment options and workers should have the opportunity to convert the benefit to an annuity.
- Benefit projections assume plan meets investment targets.

## Retirement wealth accrual over a career under a hypothetical stacked hybrid plan

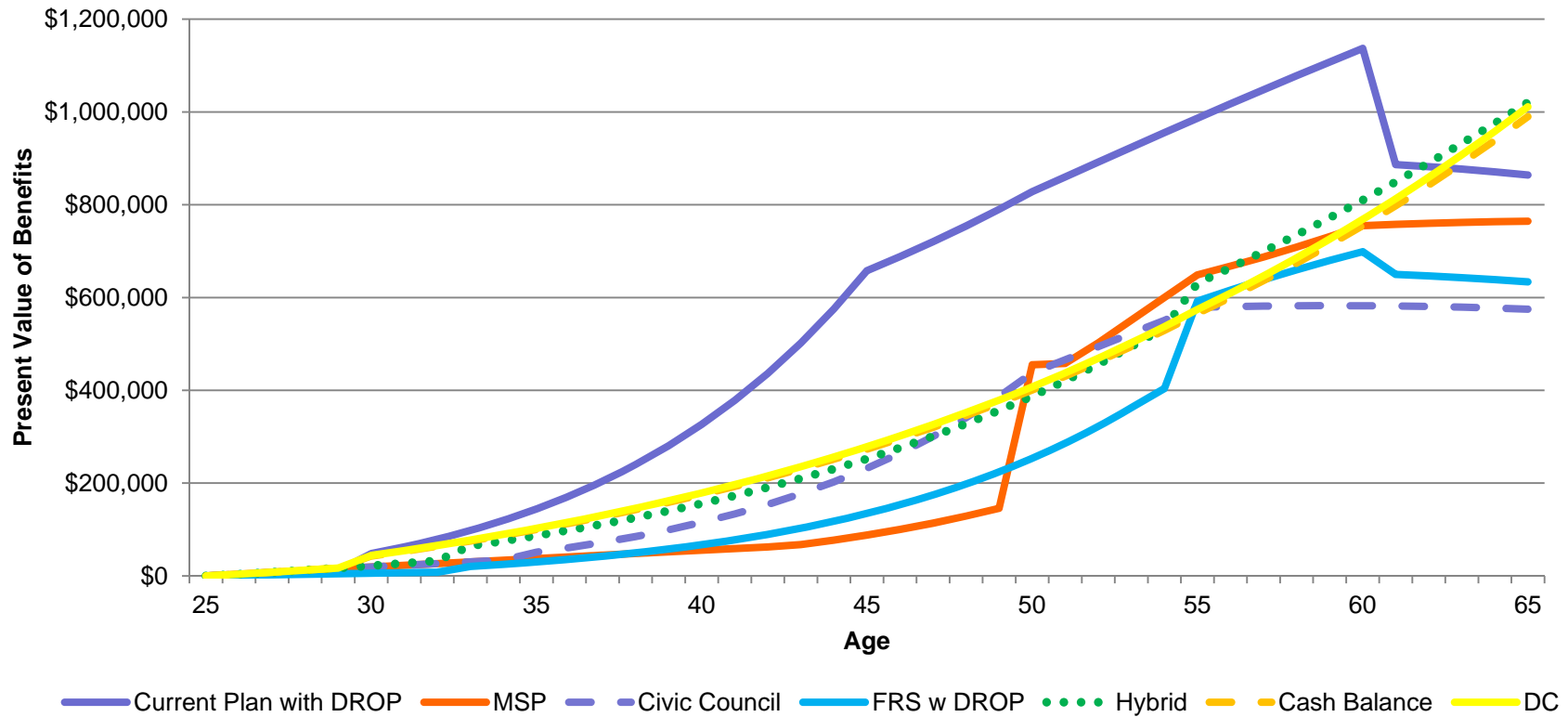
The value of earned retirement benefits



Source: The Terry Group, 2013  
Analysis based on new employee entering at age 25  
and is based on plan assumptions.

## Retirement wealth accrual for both the current and proposed plans

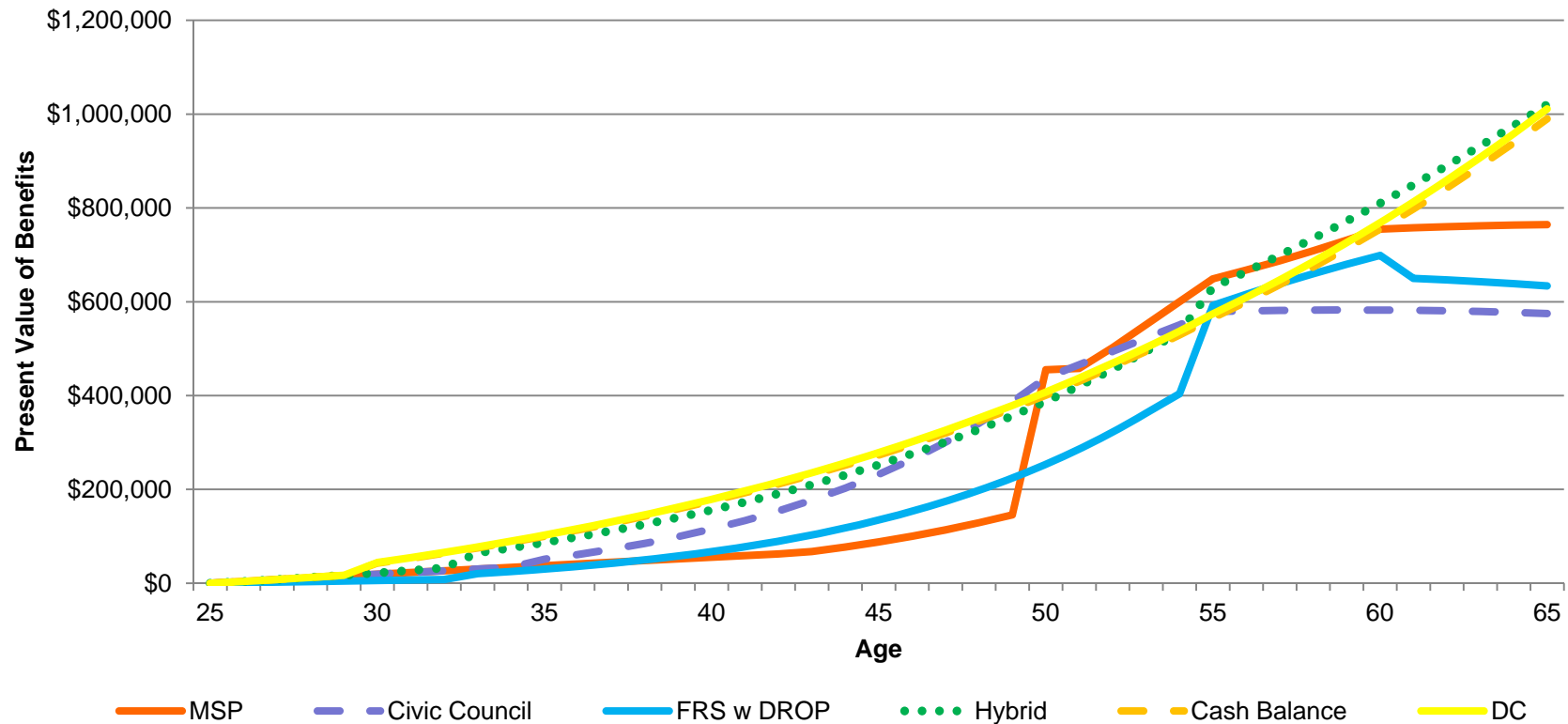
### The value of earned retirement benefits



Source: The Terry Group, 2013  
 Analysis based on new employee entering at age 25  
 and is based on plan assumptions.

## Retirement wealth accrual for proposed plans

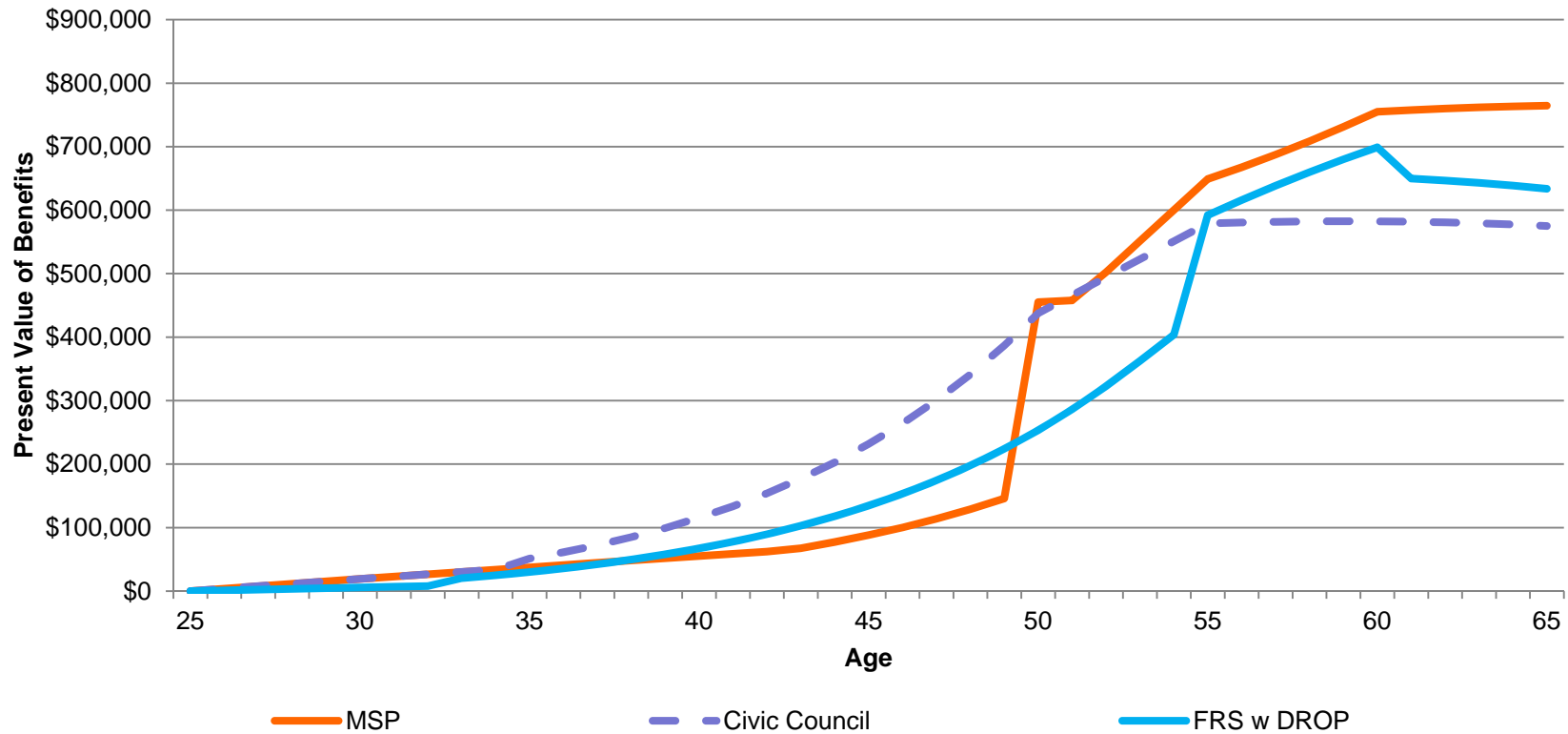
The value of earned retirement benefits



Source: The Terry Group, 2013  
 Analysis based on new employee entering at age 25  
 and is based on plan assumptions.

## Retirement wealth accrual for proposed Defined Benefit plans

### The value of earned retirement benefits



Source: The Terry Group, 2013  
 Analysis based on new employee entering at age 25  
 and is based on plan assumptions.



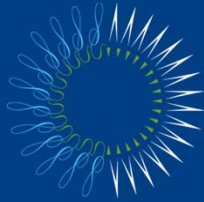
## **Plan Design for Jacksonville: Two Questions to Ask**

- What is the best way for Jacksonville to provide a retirement benefit for public employees in terms of both offering retirement security and giving the right workforce incentives?
- What plan design will be affordable, sustainable, and secure over the long-run?

## Jacksonville policy makers need to accomplish three main tasks:

1. Create a credible plan to reduce the funding gap over time in a fair way
2. Adopt a reformed retirement system that is affordable, secure, and sustainable
3. Ensure that the compensation being offered help the city recruit and retain a talented public safety workforce

*Different cities and states are pursuing very different solutions in an attempt to get to the same place: a fiscally-responsible, sustainable pension plan that can still help recruit and retain a talented workforce.*



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