Remarks to the Jacksonville Retirement Reform Task Force — Funding Sub-Committee

David Draine
The Pew Charitable Trusts
1/2/2013

January 2, 2014

This presentation to the Sub-Committee on Funding of the Jacksonville Pension Task Force will cover two topics:

1. Projecting the cost of paying for Jacksonville's pensions under the status quo and potential reform packages.

2. Assessing risks facing the Jacksonville Police and Fire Pension Fund.

1. Projecting the cost of paying for Jacksonville's pensions under the status quo and potential reform packages.

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.

Modeling Jacksonville Pension Costs

We looked at projected costs to the city of Jacksonville for the Police and Fire Pension Fund.

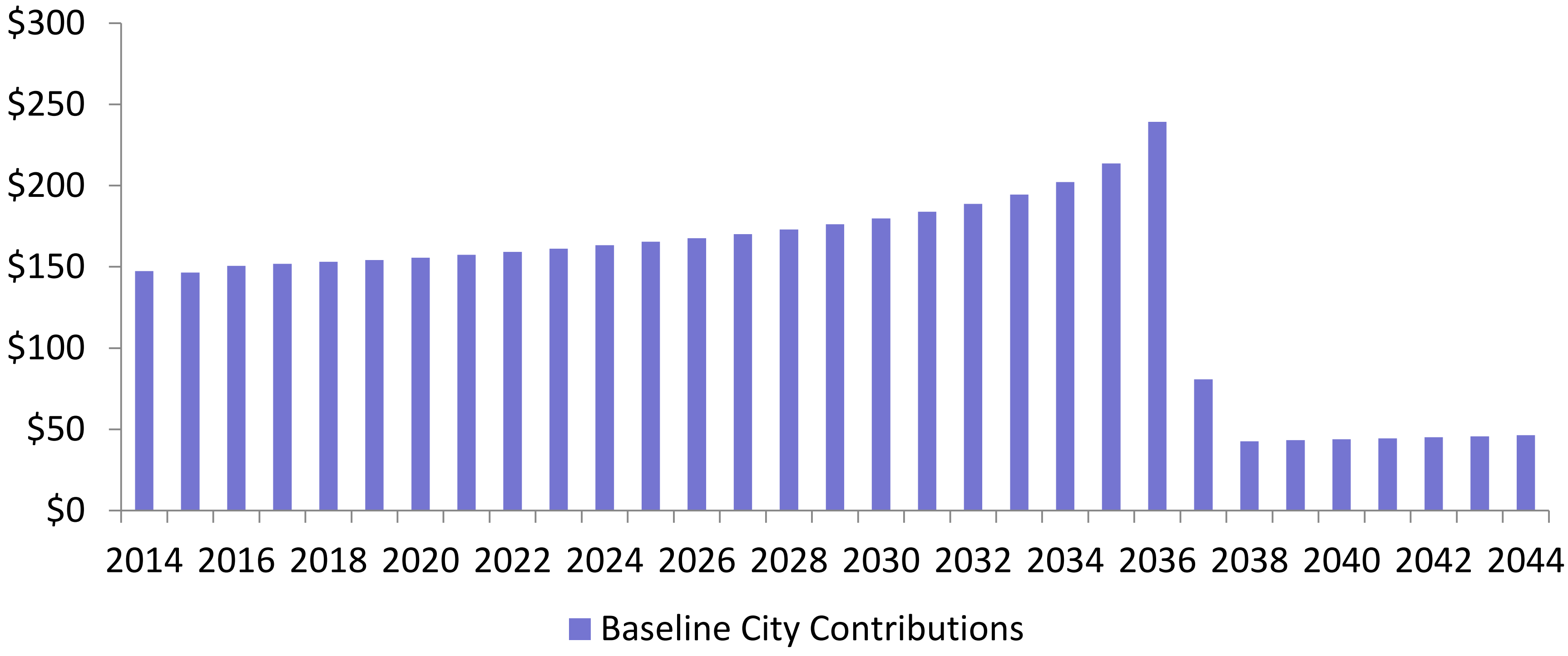
Unless otherwise stated, we use the same plan assumptions used by the Fund. We use an assumed 7 percent rate of return for the discount rate.

These figures show city costs and do not include the inflows from the use of Chapter Funds.

Costs and savings are measured over a 30 year period and all dollar values are expressed as 2014 dollars.

Annual Employer Pension Costs
Baseline

Payments owed by the City of Jacksonville.



Millions of Dollars,
Adjusted for Inflation

Source: The Terry Group, 2014

Changing Benefits for New Hires

Changing benefits for new hires will take a while for the City to realize substantial savings.

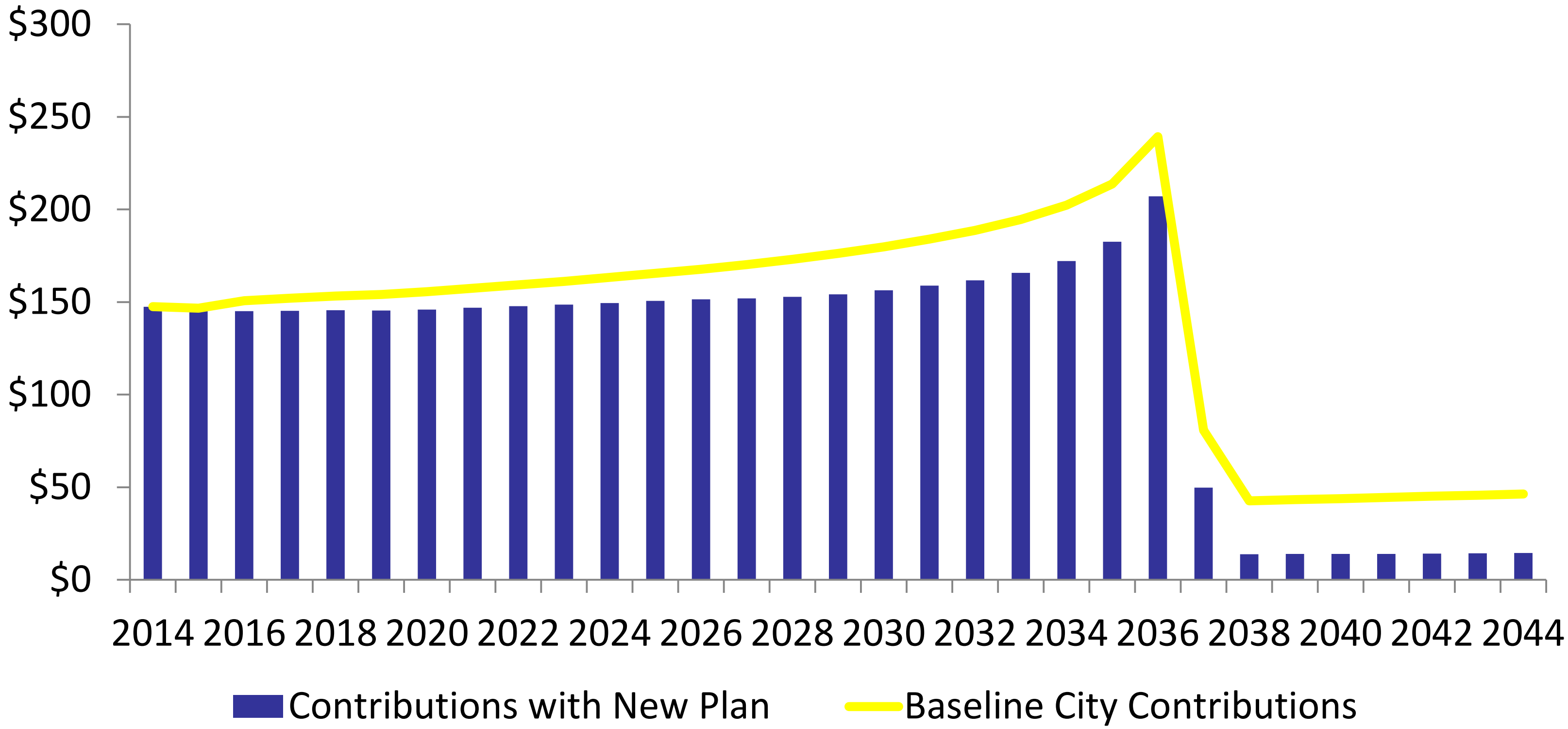
However, over the long-term, the proposed changes for new workers can reduce costs significantly over the medium- and long-term.

We modeled changing newly hired workers to a plan with 10 percent projected employer normal costs. We also included increasing employee contributions for both new and current workers to 10 percent of pay.

Switching new employees to a plan with 10 percent employer normal cost is projected to save Jacksonville more than $620 million in 2014 dollars over the next 30 years.

Annual Employer Pension Costs
10 Percent Employer Cost Plan for New Workers

Payments owed by the City of Jacksonville.



Source: The Terry Group, 2014

Millions of Dollars,
Adjusted for Inflation

Potential Funding Plan

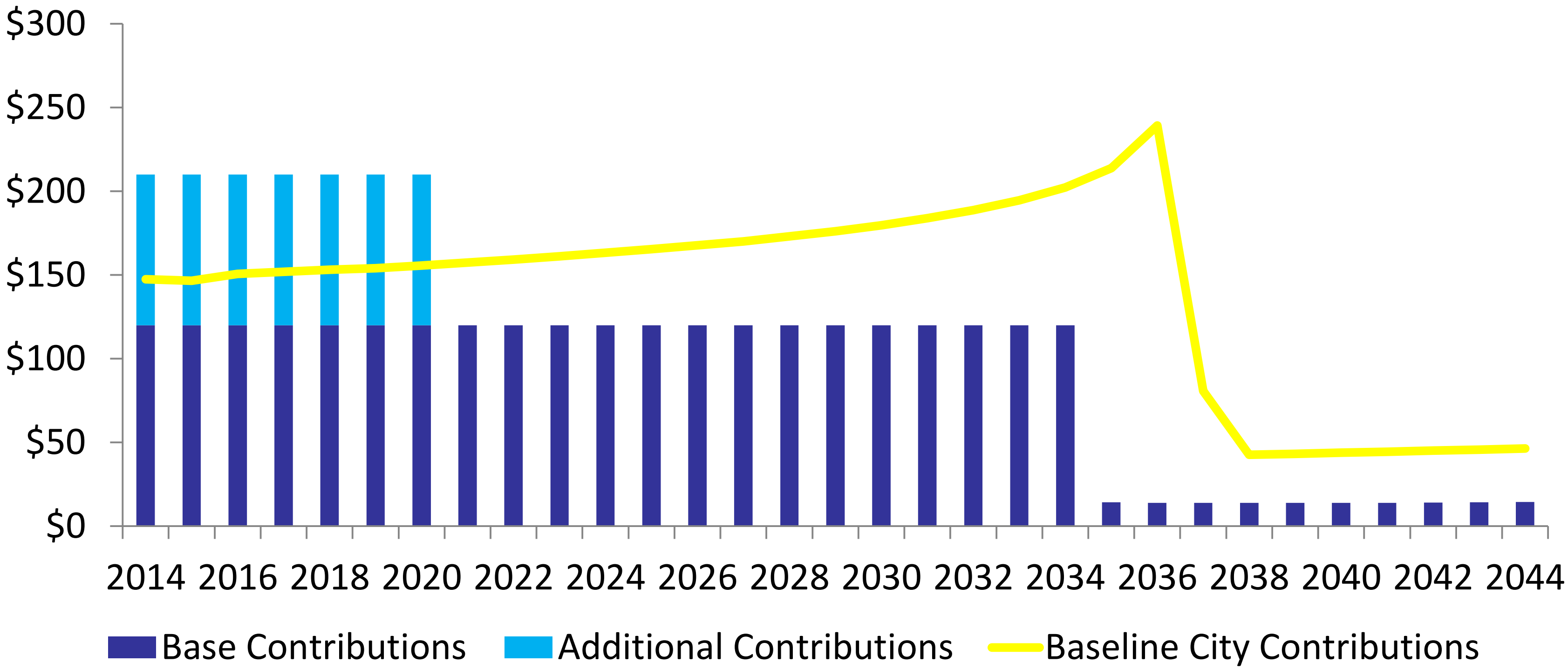
The Jacksonville Pension Taskforce has asked that we model a potential funding approach for Jacksonville to see whether it was sufficient to fund the Police and Fire Pension Fund.

Task force members suggested that a stable funding stream with $120 million coming from the city budget and $90 million coming from a separate funding source would be affordable. We modeled this along with a 10 percent normal cost plan for new hires and 10 percent employee contributions.

In the short-term this would cost $410 million more as initial contributions would be higher for the first seven years but over the remaining 23 years Jacksonville would save $1.48 billion, for a total savings of a little over $1 billion. In addition, the plan would be fully funded sooner.

Annual Employer Pension Costs
Potential Funding Plan

Payments owed by the City of Jacksonville.

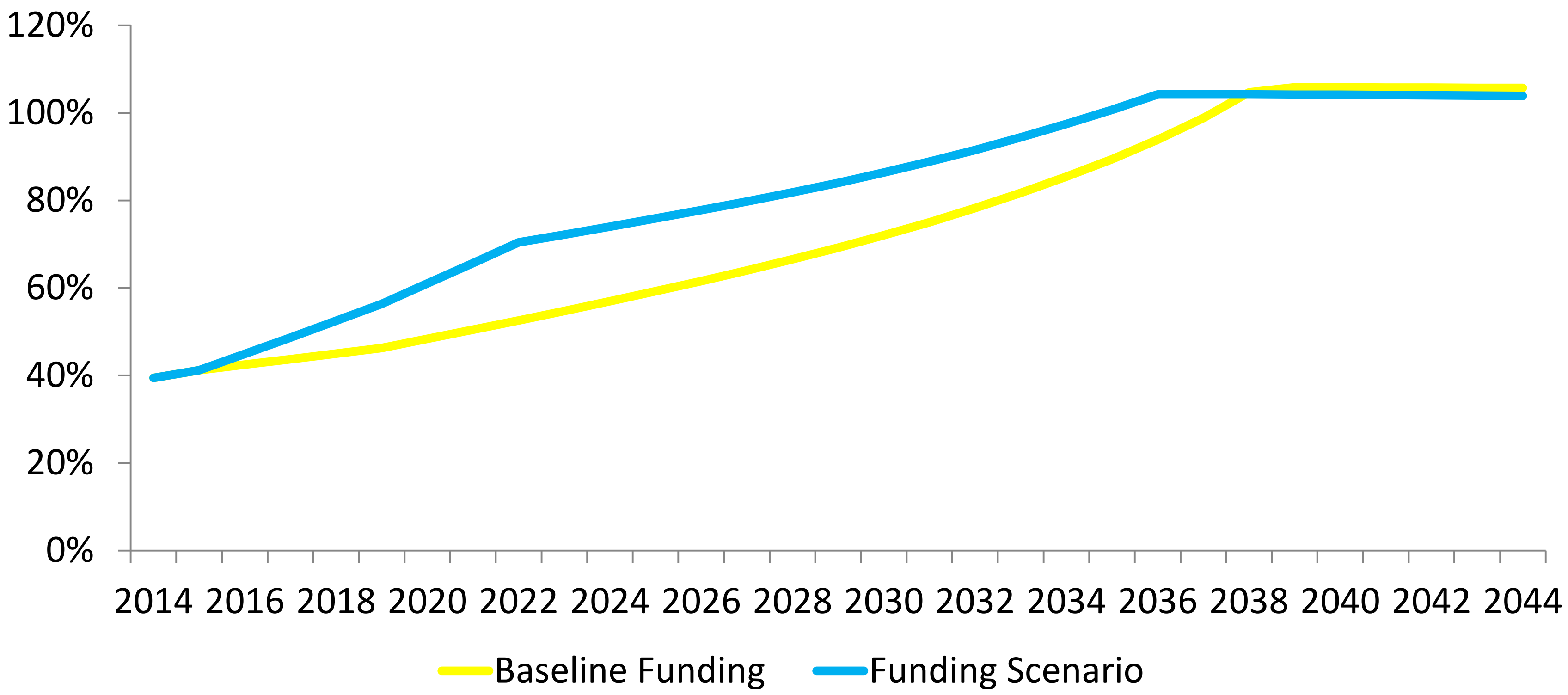


Millions of Dollars,
Adjusted for Inflation

Source: The Terry Group, 2014

Plan Funding Over Time

Percent of plan liabilities matched by assets



Source: The Terry Group, 2014

2. Assessing risks facing the Jacksonville Police and Fire Pension Fund

Investment Returns and Pension Funding

Investment returns are the single largest actuarial risk facing state and local pension plans—investment returns vary substantially in the short-term, have a major impact on assets and liabilities, and are not easily predictable over the long-term.

Many plans, including the Jacksonville Police and Fire Pension Fund, have seen their liabilities shoot up as they have changed their assumed rates of return. This acknowledges costs up-front and reduces the risk of underperforming investment returns going forward.

Risks include the possibility of both losses and gains—long-term investment returns might over perform the assumed rate of return.

Investment Returns Scenarios

Plan Assumptions: The Jacksonville PFPF gets 7 percent returns.

25th Percentile Scenario: Plan returns are 5.4 percent (costs rise by $936 million).

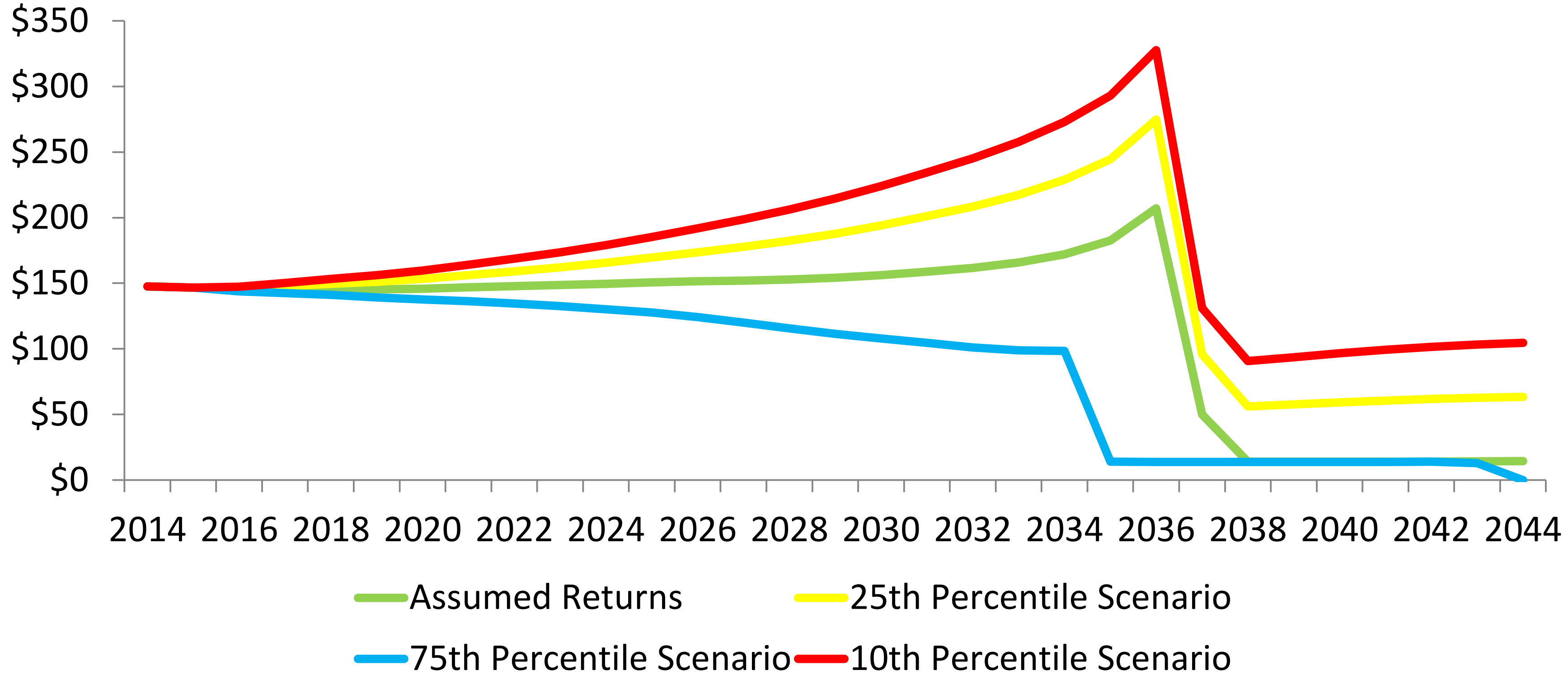
75th Percentile Scenario: Plan returns are 8.7 percent (costs drop by $962 million).

10th Percentile Scenario: Plan returns are 3.9 percent (costs increase by $1.7 billion)

We model costs and funding levels over time for each funding scenario. The models include a new plan with 10 percent employer cost for new hires and 10 percent employee contributions.

Annual Employer Pension Costs
Different Return Scenarios

Payments owed by the City of Jacksonville.

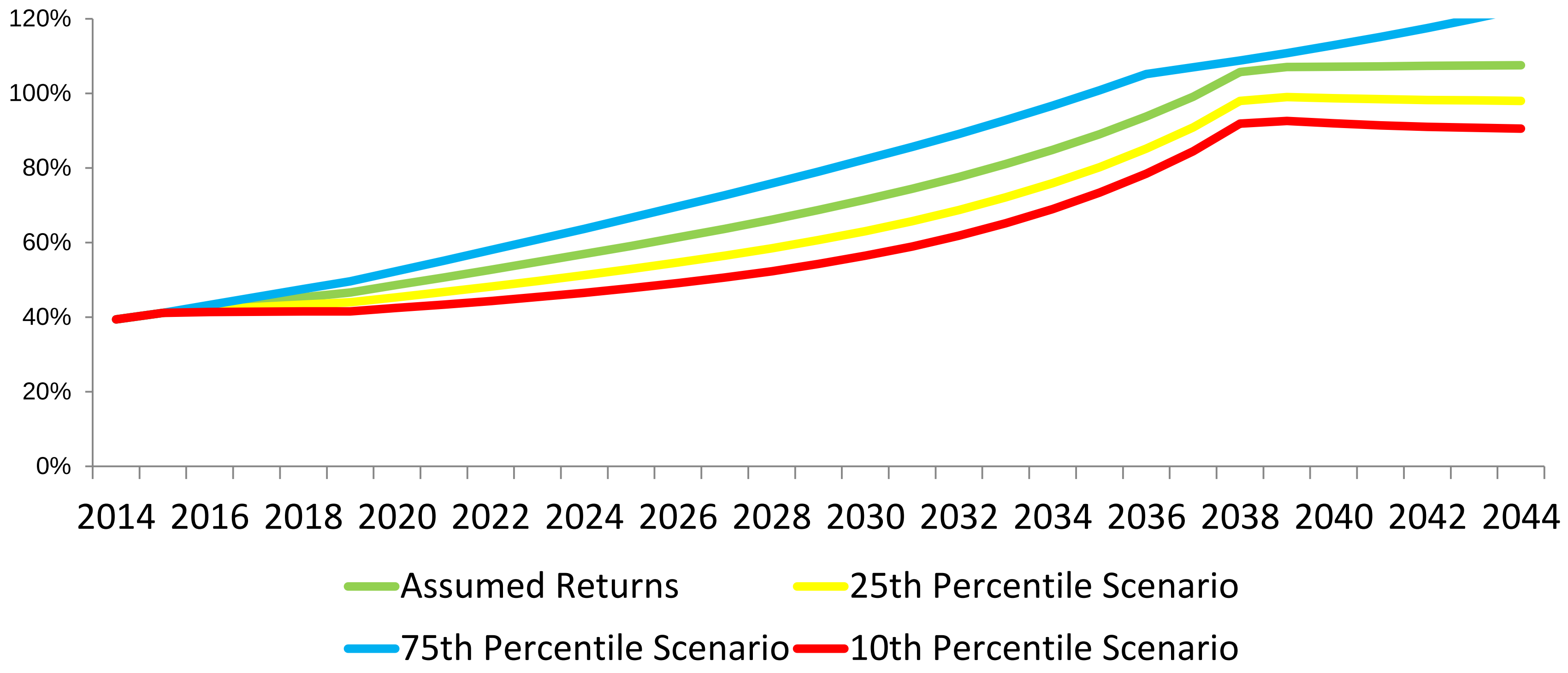


Millions of Dollars, Adjusted for Inflation

Source: The Terry Group, 2014

Pension Plan Funding
Different Return Scenarios

Percent of Plan Liabilities Matched by Assets



Source: The Terry Group, 2014

Other Actuarial Risks

Beyond investments, there are four other significant actuarial risk factors.

- **Longevity:** If public safety workers live longer than expected, costs will go up as the plan will need to pay out benefits for longer. To better plan for longevity increases, the plan mortality table should be adjusted to include future increases in life spans.

- **Inflation:** If inflation is higher than expected then it will be easier for the plan to make its investment targets and revenues will be expected to grow faster than benefit payments.

- **Salaries:** If salaries grow faster than expected then costs will go up; recent salary freezes in state and local governments have resulted in pension plan savings.

- **Withdrawal Rates:** If workers leave the workforce faster than expected early in their careers, the pension plan will experience an actuarial gain.

David Draine
Senior Researcher
ddraine@pewtrusts.org
(202) 552-2012

January 2, 2014