POLICE AND FIRE PENSION FUND

ONE WEST ADAMS STREET, SUITE 100
JACKSONVILLE, FLORIDA 32202-3616

"We Serve. . .and We Protect"

Phone: (904) 255-7373
Fax: (904) 353-8837

April 18, 2017

Lori Boyer, Council President
Office of the City Council
117 W Duval Street, Suite 425
Jacksonville, FL 32202

Thank you for the opportunity to review and comment on Ordinances 257 and 259.

The Board of Trustees of the Police and Fire Pension Fund is given the responsibility of commenting on any proposed ordinances concerning our Pension Fund. Section 121.104 of the City Charter and section 22.07 of the Code require that any proposed legislation concerning our Pension Fund be presented to our Board of Trustees for review and comment. Likewise, section 121.104 of the Charter requires that recommendations and comments from the State Division of Retirement accompany proposed pension ordinances before the last public hearing is held on the proposed ordinances. We look forward to receiving those from the state. We understand that the City administration has submitted the City administration's proposals and the actuarial impact statement that we approved on April 10th to the state.

We realize that the Council is not bound by our comments and recommendations but we have taken this responsibility seriously. We hope that you will recognize the hard work and good faith that we have put into meeting your legislative schedule and seeking the advice of our trustees, professional advisors and staff. We also hope that you will give great weight to our expertise in administering a pension plan that must be well-funded and actuarially sound to protect the retirement security of our police officers and firefighters in their most vulnerable years.

The City-wide pension reform legislation affects all City workers and the City's overall finances. Our focus in these comments is limited, as it must be, to the retirement security of our current and retired firefighters and police officers. Under the fiduciary standards of the Florida Protection of Public Employee Retirement Benefits Act, our Board's sole duty is to act in the best interests of our members' retirement security. The overall costs and benefits of the pension reform package to the City, its workers, their unions, and the taxpayers are for others to evaluate. Our duty is only to our members and retirees. Our comments and recommendations only apply to how these two ordinances affect the security of their promised pension payments.

Our first comments will be on the overall pension reform proposal as it affects our Pension Fund. Then we will comment on and make recommendations for the two specific ordinances that you have referred to us.

THE OVERALL PENSION REFORM ARRANGEMENT

As Mayor Curry said, the pension reform arrangement replaces one revenue stream with another. In 2015, our Board and the City agreed in both our 2015 Pension Reform Agreement and the federal court consent decree that the City would endeavor to make additional payments of $350 million dollars to our pension fund over the next 13 years. As shown in the attached 30 Year Projection from the Board's actuary, those additional contributions, if made, would have lowered our unfunded liability each year and brought our Pension Fund to over 100% funded in 2035, 18 years from now (page 4.)

Under the proposed ordinances, those additional payments anticipated in the 2015 Agreement and Consent Decree will be replaced by a portion of the pension surtax, but starting in 2030. Because of the delay in receiving those surtax revenues, our unfunded liability expressed in expected market value of our assets will increase each year until 2032, when it will begin to decrease. Our Pension Fund will not reach 100% funding until 2060, rather than in 18 years.

As said in the iconic Fram filters commercial, "You can pay me now or you can pay me later." Of course, our Pension Fund would prefer to be paid more now, as anticipated in the 2015 Agreement and Consent Decree, so our pension fund will be fully funded by the time that most of our current members will have retired. As the date of full funding is pushed out 25 more years by 2017 pension reform, we just want you to realize the increased uncertainty and risk of achieving a fully funded plan by then.

That being said, we also acknowledge that pension reform brings higher benefits to our Group II members. Equalizing their benefits with those of Group I brings significant benefit to them and makes it easier for us to administer the Pension Fund. Increasing their benefits brings added liability to our Pension Fund that was not anticipated when the 2015 agreement and consent decree were reached. While the current pension reform proposal may take longer to pay off those liabilities than we'd prefer, we recognize that the City has given us both a plan and a revenue stream to pay our debts to our members and retirees.

The pension reform package also closes our defined benefit plan to new hires at the close of this fiscal year. While we believe that a defined benefit plan provides the best retirement security, that was not our decision to make. We respect the collective bargaining process between the City and the unions that, without our involvement, made this decision. Our only comment is to echo the warning that we received from our actuary. Eventually, as our cohort of active members age and get closer to retiring, we will be unable to tolerate the current level of investment risk and our investment policy will become more conservative. This is the same as an individual's decision as she or he gets older to shift personal investments to less risky investments. With the reduced risk tolerance of a mature closed plan also comes reduced investment returns, and thus eventually higher City contributions. This will be a slow and gradual process that will likely not need to begin immediately, but we do want our warning to be on record. This is faced by all closed pension plans everywhere.

Council should also be aware of the added long-term costs of increasing our unfunded liability and extending our date of full funding by 25 years. The added liability means added interest costs, as our unfunded liability increases by 7% each year (our assumed rate of investment return) to compensate for lost investment earnings.

We want to assure you that we are ready, willing and able to administer and operate whatever pension plan you enact. We have an experienced, devoted, educated and committed group of five volunteer trustees who oversee our experienced, devoted, educated and committed staff and professional advisors. We are no longer in the pension benefits design business. We will faithfully and to the letter administer the pension plan that you enact. We hope that you will favorably consider our following recommendations to help us do that for you and for our members.

THE PENSION SURTAX – ORDINANCE 2017-257

This ordinance implements the pension liability surtax imposed by the City's voters. Once it is imposed, state law permits the City to reduce its annual contribution to our Pension Fund by a 30-year amortization of the present value of the surtax.

VALUATION OF SURTAX REVENUE

In our actuarial impact statement approved April 10th, our Board accepted the City's determination that the surtax revenue would grow by 4.25% per year. The General Counsel told our Board that, for a variety of reasons, his opinion was that for the purposes of creating an impact statement and later creating our annual Actuarially Determined Employer Contribution (ADEC) payment, we were obligated to accept and apply the City's determination of the surtax growth rate. To best determine the value of this surtax to our Pension Fund, we'd engaged Dr.

John Pertner, a Registered Municipal Advisor Representative of GAPublic Solutions in Orlando, to project the growth of the surtax through 2060. His report, projecting a 3.34% growth rate, is attached. Because of the General Counsel's opinion, the Board chose to accept the City's projection of 4.25%.

The Board was uncomfortable with the difference between Dr. Pertner's and the City's projections. However, it took some comfort from the assurances from Finance Director Weinstein and General Counsel Gabriel that the City's projection would be reviewed annually. The proposed ordinance permits, but does not require, such an annual review of the projection. It also does not specify that the projection will be based upon any historical data (as does state law require that our pension fund project payroll growth using 10 years of data) or that the method of projection be the same each year (as does the City charter require that our Pension Board's annual actuarial valuations utilize consistency in methods). Thus we request and recommend the following change to section 776.105(b)(2) of Ordinance 2017-57:

RECOMMENDATION: 776.105(B)(2): The present value shall be calculated assuming 4.25 percent growth per annum in the proceeds of the surtax, <u>which shall be reviewed and set by Council by October 31, 2018 and by each October 31st of each subsequent fiscal year using consistent methods and the compound average growth in surtax revenue for the previous ten years.</u>

This proposed change does not require the Council to change the projection; only to review it.

<u>ACTUARIAL DISCLOSURES</u>

The actuarial impact statement approved by the Trustees on April 19th was prepared by the Pension Fund's new actuaries, Gabriel, Roeder & Smith (GRS Retirement Consulting), the largest governmental actuarial firm in the U.S. The statement contains several disclosures that are not usually found in actuarial impact statements: they comment on the reliance on the City's projection of the surtax revenue, the use a payroll growth assumption greater than zero for a closed fund, the 30 year amortization for the entire net unfunded liability, and whether current pension costs will be transferred to future taxpayers (see pp. 4 and 5.) Each of these items is required by a specific provision of state law and the opinion of the General Counsel and this is so recognized by the actuary in his impact statement.

Both the Florida Constitution and the City Charter require that the pension fund be maintained on a sound actuarial basis. Our position, based upon the advice of the General Counsel, is that it is sound actuarial practice to follow state law and the City Charter and the actuarial practices and assumptions prescribed therein.

GASB REPORTING AND CAFR VALUATIONS

We have been advised by Finance Director Weinstein and our actuary that the valuation and recognition of the surtax revenue in our annual actuarial valuations and our impact statement may differ from the manner in which they are valued and recognized by our auditors in our annual audit and by your auditors in your GASB disclosures and CAFR. We add this comment just to bring it to your attention now.

PENSION BENEFIT AND FUNDING CHANGES – ORDINANCE 2017-259

The benefit changes and increased worker contributions provided in the new collective bargaining agreements are enacted by this ordinance. The additional City funding provided in the 2015 Pension Reform Agreement and Consent Decree is repealed, to be replaced with the surtax revenue, a minimum annual City payment, and City payments needed to preserve our Pension Fund's ability to pay benefits ("liquidity") as we await the surtax revenue starting in 2030.

LIQUIDITY PAYMENT

Because the Pension Fund's anticipated assets and funding level will decrease (compared to the assets expected under the 2015 Pension Reform Agreement and Consent Decree) while its payments to retirees will increase (as our members continue to retire), the Pension Fund's liquidity could be impaired. Our liquidity can be further impaired by adverse market events reducing the value of our assets, as shown in the "stress test" projections in our actuary's 30-year Projections, attached. Our actuary has warned us that a severe market downturn could cause large additional City payments ($100M or more) to maintain liquidity in such situations. Both Dr. Pertner and our actuary have warned us that recessions and market downturns will occur several times during the next 43 years until our pension plan is expected to be fully funded.

Section 121.113(b)(4) of the proposed ordinance provides for an additional City contribution if our liquidity falls below an unspecified ratio. Based upon the advice of our Executive Director and our actuaries as to the amount we need to pay our bills, we

RECOMMEND: that the liquidity ratio in section 121.113(b)(4) be at least 7.0 (to prevent the Fund's liquidity to be reduced further below the current woefully low level of 7.0), and that this liquidity ratio be more specifically defined as the net market value of assets in the Pension Fund (net of the DROP accounts and other reserve accounts) divided by the total benefit payments paid in the most recent fiscal year.

MINIMUM PAYMENT

Section 121.113(b)(5) of the proposed ordinance provides for a minimum City payment to our pension fund each year This minimum payment will use extraordinary actuarial gains to accelerate the payment of our unfunded liability as well as provide a minimum income to our Pension Plan if needed after the surtax expires. Any amounts paid by the City to maintain liquidity will be credited towards this payment. It is our understanding that this means no matter what happens in a given year relative to actuarial assumptions, earnings, the actuarial determined employer contribution, etc..., the Board will receive a minimum payment of an amount to be specified. Based upon advice of our Executive Director, we

RECOMMEND: that the minimum annual payment in section 121.113(b)(5) be $125,000,000 (based on the actuary's 30-year projection using the 4.25% Surtax Growth Rate and the 1.25% Growth Rate assumptions).

"SUBJECT TO ANNUAL APPROPRIATION"

Both the liquidity payment and the annual minimum payment are described in the proposed ordinance as being "subject to annual appropriation." This, in our view, makes the payments optional with each year's Council deciding whether to make the appropriations so vital to our Pension Plan's liquidity and funding.

Under the proposed pension reform, our liquidity and our funding ratio will decrease until the surtax revenue arrives in 2031. The liquidity and annual minimum payments are crucial to our continued operation and soundness. To assure the flow of these minimum amounts that we need, we

RECOMMEND: that the phrase "subject to annual appropriation" be deleted from sections 121.113(b)(4) and (5).

DETERMINATION OF USE OF STATE PREMIUM TAX REBATE INCOME FOR ADDITIONAL BENEFITS

Sections 121.114(a)-(d) prescribe the use of certain funds now in internal Pension Fund accounts and those premium tax rebate funds received from the state in the future. The four subsections require that these funds be used for the "legal use" of our firefighter and police officer members, "as determined by the legally recognized bargaining unit[s]."

The intent of these subsections is to permit the firefighter and police unions to decide how these funds will be allocated among their members. The unions will decide what benefits will be bought with this money and who will receive them. The proposed ordinance does not specify any procedure, method or deadline by which the unions will make these determinations or how they will be presented to, recognized by, and administered by our Pension Fund.

Deciding upon and designing pension benefits is no longer a function of our Board of Trustees. Our job is to administer the pension benefits agreed upon by the City and the unions in collective bargaining that result in an ordinance enacted by Council. Other than informing the unions and the City of the amount of money available for these benefits and making our actuary available to cost out any proposed use of these funds, we should not be involved in the creation of any additional pension benefits. Enacting benefit plans could subject our Board to litigation from retirees or members who are dissatisfied with the plans created by the unions or the procedures that the unions followed to create them. Rather than presenting their benefit plans to our Board, the unions should present the benefits they've decided upon to the City to be adopted as a pension plan amendment by City Council. Therefore, we

RECOMMEND: that the following underlined phrase be added to subsections 121.114(a),(b),(c) and (d):

"….as determined by the legally recognized bargaining unit <u>and thereafter adopted by ordinance by the City Council.</u>"

<u>ASSURANCES AND EFFECT ON 2015 PENSION REFORM AGREEMENT AND CONSENT DECREE</u>

The viability of this 2017 pension reform and of our Pension Plan depends upon our assured receipt of the surtax revenue, the annual minimum payment, and the liquidity payment when it is needed. These are the income streams that replace those anticipated by the 2015 Pension Reform Agreement and Consent Decree. Thus, we have recommended deleting the words that make the liquidity and minimum annual payments "subject to appropriation." We also need assurance that the pension surtax will not be repealed or reduced between now and the time our pension plan becomes fully funded (now estimated to be 43 years in the future.)

Also, the proposed ordinance repeals the funding provisions contained in the 2015 Pension Reform Agreement and the Consent Decree. Our pension fund is a party to both the agreement and the consent decree. The consent decree requires annual reporting to the federal court on compliance with its terms. Whether legally required or not, both that agreement and the consent decree should be amended to reflect 2017's pension reform as a substitute for 2015's pension reform.

This Council may not wish or be able to bind future City Councils. However, regardless who sits on City Council, our need to receive the funding promised under 2017 pension reform continues each and every month. We will need these payments until we are fully funded so that we'll have the money needed to pay the last surviving retiree or beneficiary her or his last pension payment. To go forward with our now-delayed goal of full funding, we need assurances that the payments promised in Ordinance 2017-257 and 259 will be made or that the funding in the 2015 Pension Reform Agreement and Consent Decree (that is replaced by these ordinances) will be provided. Thus we

RECOMMEND: that the 2015 Pension Reform Agreement and Consent Decree be amended to include the provisions of this 2017 pension reform as a substitute for the pension funding provisions contained therein.

CONCLUSION

Our Board of volunteer trustees has spent over seven hours of formal meeting time plus additional review and study time by each trustee reading and analyzing these proposals. Our professionals and staff have spent weeks preparing their reports for our analysis and for our meetings. This is not a task that we undertook lightly or without careful thought and deliberations.

We encourage the Council to likewise carefully, prudently, and deliberately analyze and understand all aspects, implications and effects of this far-reaching proposal. 2017 pension reform will affect the financial security of our Pension Fund, its members, our retirees, our taxpayers, and our City government for decades to come.

After pension reform is considered and enacted by City Council, we will be left with the task of administering it. While appreciating the increased benefits for our members, we will be faced with a decreasing funded ratio and an increasing unfunded liability until mid-century. Our goal of 100% funding will be deferred for another 25 years. We acknowledge that it is the task of the City administration, the unions, and this City Council (and not our task) to balance the needs for enhanced benefits, adequate pension funding and the City's other financial priorities. We only ask that the 2017 pension reform be backed with promises, not just plans and projections, so that we can administer our pension plan on a sound basis.

We face considerable challenges in administering and financing our Pension Plan with the reduced resources made available under 2017 pension reform. With our six recommendations above, we seek only assurances from this Council that the City is committed to providing us with the contributions that we need to keep things going until the surtax revenue begins to flow and our progress towards full funding resumes.

Lt. Chris Brown Trustee	Richard Patsy Trustee, Board Secretary
Willard Payne Trustee	William Scheu Trustee
Lt. Richard Tuten III Trustee, Board Chairman	Timothy H. Johnson Executive Director – Plan Administrator

Cc: Dr. Cheryl Brown
Members of City Council
Margaret Sidman
Bob Sugarman
Jason Gabriel
Pete Strong
John Pertner