REPORT OF THE JACKSONVILLE RETIREMENT
REFORM TASK FORCE

March 19, 2014

On August 21, 2013, Mayor Alvin Brown appointed seventeen persons to the Jacksonville Retirement Reform Task Force (the "Task Force"), whose mission was to examine the Jacksonville Police and Fire Pension Fund (the "Fund", or "JPFPF") and make recommendations concerning its future and the design of and funding for pension benefits for Jacksonville police and firefighters. The Task Force was an enlarged and reconstituted task force from that which had been appointed by the Mayor on July 3, 2013.

CALL TO ACTION

The stabilization of the City's employee pensions, especially the JPFPF, is the single most important issue facing the City today. Unless reform is accomplished soon, the City's quality of life will continue to decline because of the increasing burden that pension obligations will have on the City's financial resources. The Task Force calls city leaders to action to solve the pension crisis.

Leadership is crucial for implementing appropriate solutions. The Mayor, City Council President and members of the City Council, the JPFPF Administrator and its Trustees, and community leaders from Jacksonville's businesses and its nonprofit and civic sectors all have important roles to play. Even religious leaders are crucial for the solution of this problem, for ultimately it is a moral issue. What is our community life going to be like for the next generation? As citizens, we must be able to assure a sound financial foundation for Jacksonville so that we may meet our basic needs and partake in the "pursuit of happiness" that our country's constitutional documents enshrine.

The City of Jacksonville, like many other municipalities and most states, has long provided defined benefit pension plans for its employees. Jacksonville has adopted three such plans: one for its general employees, one for correctional officers employed by the Jacksonville Sheriff's Office and another for police and fire personnel. The latter is the JPFPF.

The funding of the JPFPF has become a significant part of the City's operating budget. In the FY 2000 budget, the City's JPFPF pension payment from its operating funds was a little over $32 million. In the FY 2008 budget, it had grown to $65 million; by FY 2012, to $90 million, by FY 2013 to $120 million, and in the City's current FY 2014 budget, it is $148 million. The total approved City operating budget for FY 2014 is $983,601,445, meaning that the "actuarially required contribution" ("ARC") for the JPFPF in FY 2014 amounts to 15.1% of the City's operating budget. When the ARCs for the other two City pension funds are added to the JPFPF's, the percentage of the annual City operating budget for required pension payments alone is 18.4%. (The City is legally required by State law to pay the full ARCs for all its pension funds.) By comparison the Library's portion of the budget is 3.4%, Public Works is 3.6% and Parks and Recreation is 2.6%.

The City's increasing annual pension obligations are crowding out funds for other needed community services, such as libraries, parks and road repair. In addition, there are fewer and fewer dollars available for paying salaries or funding capital needs, either directly or through capital financing, or economic development programs that can produce jobs. Moreover, the City is projecting a budget deficit for FY 2015 of almost $14 million, rising over the next few fiscal years to almost $68 million in FY 2018, the fiscal year in which the JPFPF's ARC would rise to more than $200 million. Obviously, the mounting pressure on the City's budget would translate into a steady decline in the community's quality of life.

The Task Force found that the JPFPF, as currently funded, cannot support the current level of retirement benefits of the men and women currently serving the public as police officers and fire and rescue personnel. The people of Jacksonville and their elected representatives must understand that the promises made to those men and women, and the City's financial position, are jeopardized by the underfunded status of the JPFPF.

The Task Force's analysis, outlined in this Report, illustrates that the 2012 JPFPF unfunded pension liability totaled *$1.7 Billion* ($1.64 Billion, according to a draft actuarial report of the JPFPF for FY 2013). That is a staggering sum. Nevertheless, the Task Force is hopeful that the people of Jacksonville can pay down this debt significantly over the next 14 years, and do so without further diminishing the capacity of the City of Jacksonville to operate its libraries and parks, support arts and culture and sports, and provide for public safety and other core services to children, elders and veterans.

Time is of the essence. In recent months, the ratings agencies have started to apply much more scrutiny to the status of public pension systems supported by debt-issuing municipalities. Just this month (March, 2014), the Fitch rating agency noted the City's "very high pension burden." Its adjusted funded ratio for all of Jacksonville's pension plans is very weak at 50.5%. (Jacksonville's funded ratios are even lower using Moody's adjusted methodology for analyzing municipal pensions.) According to Fitch, "[P]ension pressures have escalated rapidly [in Jacksonville] reflecting plan benefit structures (including an automatic 3% cost-of-living adjustment for all plans) and asset performance during the recession."

Without needed reform, it seems certain that Jacksonville is headed towards a ratings downgrade. Fitch anticipates resolving Jacksonville's Negative Outlook by the end of the calendar year and, "a downgrade of at least one notch is expected absent agreement on a pension deal that shows progress towards reducing the unfunded liability in a way that is affordable and preserves financial flexibility." The City can no longer postpone remedying the unfunded status of the JPFPF.

We know the people of Jacksonville to be honorable and expect that as a community we will together meet this challenge.

As far as pension design is concerned, the Task Force's recommendations in this Report call for no changes to the retirement income of those already retired. Those benefits are protected under the Florida constitution and by statute. The Task Force does call for sacrifices from *future* employees: specifically, increased employee contributions, longer years of service before collecting retirement income, increasing to five years the number of years to be used in determining the average salary for pension computation, reduced and delayed cost of living adjustments ("COLAs"), elimination of the deferred retirement option program ("DROP"), although the "BACK-DROP program is retained, and a limit on retirement income.

The Task Force's recommendations also call for sacrifice from *current* employees: specifically, a modest increase in employee contributions (most of which will only come once previous pay cuts have been restored); for those employees not eligible for DROP on the effective date of the recommendations, the annual interest guaranty of 8.4% would change to the Fund's realized rate of return, but not less than zero or more than 10%; reduction of the COLA for benefits earned after the effective date of the change, from a compounding 3%, to the rate of inflation as measured by the consumer price index, but not more than 1.5% annually; and, *only for those current employees with less than ten years' service on the effective date of the recommended reforms,* changing the number of years for computation of the average salary from two to five years for benefits earned after the effective date of the change (this change would only affect those who receive future salary increases), and delaying the COLA payable on benefits earned after the effective date of the change to a date that would be three years following retirement, but not earlier than age 55.

In addition, the Task Force calls for sacrifices from those of us who benefit from the service of police officers and fire and rescue workers. To reach the Task Force's intermediate target of an 80% funded ratio for JPFPF by 2028 (which represents an accelerated step towards reaching the ultimate goal of 100% funding, as required by Florida law), the people of Jacksonville are asked to contribute $200 million annually to the JPFPF. As noted above, the current fiscal year's contribution from the City's general fund totals $148 million. The Task Force recommends that the general fund contribution be capped at the current $148 million and that the additional dollars required be new dollars raised through a ½ percent sales tax increase (colloquially stated as a "half-cent per dollar" sales tax increase), or, failing that, an ad valorem tax increase of a little over one mil.

In addition to implementing reforms of JPFPF pension design and finding funds to increase the JPFPF's funding ratio to an intermediate goal of 80% and to an ultimate goal of 100%, as required by Florida law, comprehensive reform must also include changes to the governance of the JPFPF. The Report recommends several reforms addressing governance issues.

HISTORICAL CONTEXT

By statute, the City is required to fund, on a current basis, the amount attributable to benefits to be earned during a particular plan year by active participants (the "normal cost") and the annual amount of unfunded future obligations amortized over time. The "normal cost" is the estimated cost of the benefits earned by current employees in a one-year period. If the "normal cost" is consistently paid over a worker's career, and if the pension plan's actuarial and investment assumptions are accurate, that worker's pension will have been fully funded at his or her retirement. To the extent that the actual investment returns are less than the actuary's assumptions as to the anticipated rate of return (the "assumed rate of return"), funding is at a level less than required If other variances occur from the actuarial assumptions, then some portion of the workers' benefits will also become unfunded. In addition, benefit changes,

changes in assumptions and changes in actuarial procedures will also have an effect on the total actuarial liability and the portion of it that is unfunded. The colloquially discussed "unfunded liability" is known formally as the "unfunded actuarial accrued liability" or the "UAAL". The UAAL may be amortized over a period of time, but under Florida law, the maximum is 30 years.

The Fund's normal cost and UAAL are actuarially determined and the computations consider (i) the particular design of the pension benefits, (ii) the makeup of the present workforce, (iii) the assumed life expectancies of the participants in the plan as determined by mortality tables, (iv) the year-by-year experience of the workforce as compared to assumed demographic and economic assumptions which are periodically set through experience studies, and (v) the assumed and realized rates of return of the investments of the Fund. Adding the employer's normal cost to the required minimum amortized portion of the UAAL for a given year equals the "actuarially required contribution" or the "ARC" for that year. As an example, the JPFPF's ARC for the 2014 was just over $154 million. The $154 million ARC included a "normal cost" of $46 million and an amortized portion of UAAL of $108 million. The total payment of the ARC was made by paying $148 million from both the City's operating budget and an additional $6 million from the "Chapter Funds" allocated to the JPFPF under Chapters 175 and 185, *Florida Statutes* (which is a statewide tax on certain property insurance premiums). Chapter Funds are not included in the City's operating budget. There were also ARCs for the other pension funds of the City and those ARCs were paid with funds provided from the City's operating budget.

In FY 2000, the JPFPF's deficit, or UAAL, was approximately $124 million. In FY 2008, it increased to $798 million and in FY 2012 to $1.7 billion. At the same time, the JPFPF's funded ratio dropped from 87% in FY 2000 to 39% in FY 2013. These numbers are truly astounding. In FY 2000, the Fund was 87% funded; in FY 2008, 53% funded; and in FY 2012, 39% funded. *That is the lowest and most precipitous drop in funded ratio for any of Florida's large cities, despite the fact that every city in Florida – and for that matter in the country – experienced the same turbulent market conditions over that period of time.*

Funding Level of the Jacksonville Police and Fire Pension Fund

The Jacksonville Police and Fire Fund is just 39 percent funded, with a $1.68 billion pension debt.

	2012	2008	2004	2000
Assets	$1,078,907	$894,903	$727,955	$814,889
Liabilities	$2,762,977	$1,692,975	$1,222,355	$939,802
UAAL	$1,684,070	$798,071	$494,400	$124,913
Percent Funded	39%	53%	60%	87%

All dollar figures in thousands

Source: Actuarial Valuations of the Jacksonville Police and Fire Pension Fund

How did we get in such dire straits over such a short period of time? Frankly, a number of things went wrong in Jacksonville as far as its pension plan obligations are concerned. According to the 2009 Jacksonville Community Council ("JCCI") study investigating Jacksonville's financial condition ("Our Money, Our City: Financing Jacksonville's Future", at p. 26), the reasons included (i) lower investment returns than were assumed by JPFPF, (ii) investment decisions and policies, (iii) changes in actuarial assumptions that asymmetrically locked in market gains but smoothed market losses, (iv) increased benefits (notably adding cost of living adjustments, or "COLAs" which employed a compounded 3% annual rate to benefit payments) and (v) changes in payroll.

The JCCI report also identified previous funding decisions by the City as a factor in the substantial increase in the UAAL (for example, using funds from the JPFPF reserve account rather than funding from the City's operating budget), but the Task Force was advised and concluded that since the City had paid the ARC each year, the *source* of funding could not have affected the increase in the UAAL. Mayor Brown's Transition Team Pension Subcommittee report stated, at page 4, "The city's unfunded liability was primarily caused by three major contributors: 1) The use of inaccurate actuarial assumptions; 2) The addition of retroactive benefits; 3) The Bear Market."

It must be said that these problems are not unique to Jacksonville. A majority of the pension funds in the United States are underfunded, but the JPFPF is among the worst. Headlines in *The Florida Times-Union* (the "*Times-Union*"), *The Wall Street Journal* and other publications, have publicized the situation around the country. Most starkly, the City of Detroit's 2013 bankruptcy filing triggered both focus and concern not only in Jacksonville, but in cities throughout the United States.

APPOINTMENT OF THE TASK FORCE

With this backdrop, on May 28, 2013, at Mayor Brown's request, legislation was introduced before the Jacksonville City Council (the "City Council") by which he proposed a solution to the JPFPF pension crisis based on an agreement reached in federal court mediation proceedings in which the parties were Randall Wyse and other plaintiffs who are members/beneficiaries of the Fund, the City, and the JPFPF (the "Mediated Settlement Agreement" or "MSA"). The Fraternal Order of Police, Lodge 5-30, and the Jacksonville Association of Firefighters, Local 122 of the IAFF (the "Unions") also executed the MSA. The MSA recites that the Unions are the collective bargaining representatives, respectively, for all Jacksonville law enforcement officers and their ranked superiors, and all Jacksonville firefighters and their ranked superiors. In the MSA, the parties agreed to certain funding schedules for the City and to adjustments in pension design for new employees of the Jacksonville Sheriff's Office ("JSO") and the Jacksonville Fire Rescue Department ("JFRD"), which would result in lower benefits for such new employees. No changes in pension design were agreed to in the MSA which would affect current employees. The MSA also recommended an increase in the employee contributions to the pension fund from 7% to 9%, phased in over time.

On June 20, 2013, the Jacksonville Civic Council (the "Civic Council") wrote to the Mayor and William Gulliford, the President of the City Council, recommending that the proposed MSA be rejected and that other alternatives be considered. (The Jacksonville Civic Council is a group of 59 civic and business leaders committed to betterment of the City.) Shortly thereafter the *Times-Union* and the Jacksonville Regional Chamber of Commerce (the "Chamber") also recommended that the solutions proposed by the MSA be rejected. The *Times-Union*, through its editor, Frank Denton, also filed suit in Duval County Circuit Court to invalidate the MSA and moved to intervene in the federal proceedings in which the MSA was negotiated, based on alleged Sunshine Law violations and for other reasons.

On July 3, 2013, Mayor Brown appointed the initial task force, and it held an organizational and initial informational meeting on July 10. The Mayor charged it with evaluating the proposed legislation and making recommendations concerning it. However, before the task force could really begin its work, the proposed legislation was voted down by the City Council. The next scheduled meeting of the task force was cancelled.

In August, 2013, the Mayor decided to appoint the Task Force with a broader mission: to examine the JPFPF and its governance, policies, procedures, actuarial and investments and practices, together with the practices of the City in performing its funding obligations and oversight of the Fund. He envisioned and appointed a broad-based and experienced group to serve on the Task Force. Those persons were: Dr. Chester Aikens, a dentist and community volunteer involved in numerous community initiatives (*Note*: Dr. Aikens tragically died immediately following the December 5 meeting of the Task Force); Greg Anderson, Community Development Director of EverBank and chairman of the City Council Finance Committee; Charles C. Appleby, Chairman and CEO of Advanced Disposal Services; David A. Boor, vice president – tax, and treasurer of CSX Corporation; Carl Cannon, retired publisher of the *Times-Union*; Tad Delegal, attorney, whose practice is centered on employment law; Kirsten Doolittle, also an attorney whose practice is centered on employment law; Dr. Sherry Magill, president of the Jessie Ball Du Pont Fund; Robert L. Miller, Chief Financial Officer of Family Support Services of North Florida, Inc., and retired senior vice president of Regency Centers Corporation; Kelli O'Leary, executive vice president of HCI Group, with a particular expertise in human resources; Dr. William Rupp, CEO of The Mayo Clinic, Florida, and now chair of the Chamber; Robert T. Shircliff, business consultant and philanthropist; Gregory Smith, Bank of America market president and now immediate past chair of the Chamber; John F. Thompson, senior vice president and investment manager, The Forbes-Thompson Group of Wells Fargo Advisors, and chair of Mayor Brown's transition team's pension reform subcommittee; John F. Wilbanks, chief operating officer of Baptist Hospital System; Gwen Yates, former City Council member and former chair of the Board of Trustees of Florida State College at Jacksonville; and William E. Scheu, lawyer and shareholder of Rogers Towers, a Jacksonville law firm. Mr. Scheu was named by the Mayor to be the chairman of the Task Force. *Messrs*. Boor, Miller and Thompson served as the Task Force's subcommittee on pension design and funding.

The reconstituted Task Force held its first meeting on August 21, 2013, at which it received information from the Mayor, the JPFPF and others. Most of the meeting involved a presentation by John Mellott, who had chaired a similar effort by Atlanta to reform part of its pensions. He offered to present a proposal to the Task Force by which his group would provide assistance to the Task Force in its work. After subsequent investigation and negotiation by the Task Force Chair, it appeared that the fees for such services would approximate one million dollars, and would need to be raised from the private sector.

Coincidentally, and perhaps even providentially, the Task Force Chair received a proposal from The Pew Charitable Trusts ("Pew"), the John and Laura Arnold Foundation ("LJAF") and The MAEVA Group ("MAEVA") to provide financial, analytical, actuarial and other assistance to the Task Force, *pro bono*. The Task Force met on September 16, 2013, and received a presentation from Pew, LJAF and MAEVA. Following the presentation the Task Force voted unanimously to engage that assembled team. From the beginning Pew, LJAF and MAEVA have provided, on a *pro bono* basis, invaluable assistance to the Task Force and the Jacksonville community, and have helped the Task Force to reach its conclusions. It is fair to say that without this assistance, the Task Force would have been unable to do its work without significant expense and time. The Task Force is immensely grateful to Pew, LJAF and MAEVA for their work. The Task Force particularly appreciates David Draine, a senior researcher for Pew, and Jonathan Trichter, a principal at MAEVA, for their diligent work for the Task Force and their attendance at virtually all Task Force meetings. Copies of the many presentations made by *Messrs*. Draine and Trichter to the Task Force are included in the Appendix to this Report, which is posted on the City's Retirement Reform Website with this Report.

The Task Force also expresses its thanks to Mayor Alvin Brown and his staff, particularly chief of staff Chris Hand and treasurer Joey Greive; to City Council President William Gulliford; to the City's General Counsel, Cindy Laquidara and her staff, including special counsel James Linn; to John Keane, the Administrator of the JPFPF; to Sheriff John Rutherford; and to Fire Chief Martin Senterfitt; all of whom provided substantial assistance to the Task Force; and to Robert Dezube of Milliman, Inc., who presented actuarial analysis and commentary to the Task Force on behalf of the City. The Task Force especially expresses its gratitude and thanks to Carol Wells, Chris Hand's administrative assistant, for her thorough, timely and unselfish administrative assistance to the Task Force generally and to its individual members. Finally, the Task Force thanks the many citizens who attended its meetings and offered thoughtful feedback and recommendations during the Task Force's discussions.

Through March 19, 2014, the Task Force met 14 times, and its plan design and funding subcommittee met an additional 4 times. Members of the Task Force also attended meetings called by the City Council President and others. On November 5, 2013, the Task Force held a 3-hour town hall meeting at which suggestions and advice from the community were solicited and presented. At each meeting of the Task Force and the plan design and funding subcommittee, a period for public comment was provided. The Task Force at all times was subject to the requirements of the Sunshine law, so individual members could not meet privately to discuss issues before the Task Force.

Over its seven-month life the Task Force heard and discussed numerous proposals involving various aspects of the JPFPF, the City and the Unions. The Task Force quickly came to the conclusion that there were serious legal constraints that would affect its work. It also concluded that there were four main areas of concern that its recommendations should address: (i) governance; (ii) the JPFPF's investment authority; (iii) retirement pension benefit design; and (iv) reducing the UAAL.

This report addresses each of those four areas, but before discussing them it is very important to describe the legal context in which the pension issue is found, and the constraints that it places upon the City, the JPFPF, the Unions and the work of the Task Force.

LEGAL CONTEXT

The legal setting affecting the Task Force concerns six issues: (i) the governance of the JPFPF,(ii) the constitutional and statutory rights guaranteed to pension beneficiaries, (iii) the investment authority of the JPFPF, (iv) the applicability and enforceability of an agreement entered into by the City and the JPFPF in 2000 (the "30-Year Agreement"), (v) the effect of a decision reached by the Circuit Court in the lawsuit brought by the *Times-Union*/Frank Denton, and (vi) the potential for curing Jacksonville's pension crisis by filing bankruptcy.

Governance

To address governance issues it is first necessary to understand the history of the JPFPF and how its powers and authority arose.

1. Early History. In 1937, the Florida Legislature established the Police and Fire Department Pension Fund (Ch. 18615, Acts of 1937), and the Pension Fund for Employees of the City of Jacksonville (Ch. 18610, Acts of Florida). The administration of the two pension funds was vested in the Jacksonville City Commission, whose members ("or other officers which may succeed in the control of the organization of the Police and Fire Departments") were named the trustees of the police and fire pension fund. The members of the City Commission were also named the trustees of the general employee pension fund.

2. Consolidation. The 1967 Charter of the Consolidated City of Jacksonville (the "Charter"), in Chapter 18, continued the two pension funds established in 1937. Section 18.01 of the initial Charter (renumbered as Section 16.01 by the City Council in Ordinance 84-1307-754) provided that all officers and employees of the consolidated government employed after the effective date of the act "shall be" members of one of the two pension plans. Those pension plans were declared to be the pension system of the consolidated government, "unless otherwise provided by council." Chapter 67-1320, Laws of Florida, Section 18.01. Two years later, in Chapter 69-1172, Laws of Florida, the Florida Legislature repealed the language "unless otherwise provided by council." As enacted in 1969, Section 16.01 of the Charter granted and as it exists today Section 16.01 grants the City Council "*the authority to amend said retirement and pension system to provide a separate classification or classifications, including provisions relating to eligibility, contributions, required service, retirement age and benefits thereunder for officers and employees becoming members of said retirement and pension system after the effective date of this charter.*" (Emphasis added.) Section 16.03 of the Charter provides that "[t]he council shall have the power to amend any plans of former governments and to establish which officers of the consolidated government are responsible for the administration of the plans and the handling and investment of funds under such plans".

Until 1990, in the consolidated government of the City, a board of trustees administered the police and fire pension fund. The first such board, created by Ordinance 1968-0037, consisted of the Mayor, the Sheriff, the Tax Assessor, the Director of Finance and the Personnel Manager. Prior to the 1990 Legislation described below the City Council adopted different configurations for the Board of Trustees. Additionally, the City Council amended the plan dozens of times. From the foregoing it appears that in the City's consolidated governmental organization, the Council retained authority to make benefit changes and the Charter contemplates that it may do so.

3. <u>1990 Legislation</u>. In 1990, the Legislature added a new Chapter 22 to the Charter, creating the Jacksonville Police and Fire Pension Board of Trustees (Laws of Florida Ch. 90-442) (the "Board"). Section 22.04 of the new Charter provisions stated that the Board "shall have the power to *(a) Be the sole entity responsible for administering the Jacksonville Police and Fire Pension Fund.*" (Emphasis added.) Section 18.07(d) of the Charter, as amended, made the Jacksonville Police and Fire Pension Board an independent agency of the Consolidated City.

   Section 22.11 of the new Charter provisions stated that the Board "shall continue as an independent agency under the Charter of the City of Jacksonville." Section 22.04 also gave the Board the power to invest and reinvest the assets of the pension fund, sue and be sued, enter into contracts, employ and fix the compensation of any administrators, consultants, attorneys and other professionals and employees "as the board may require". Interestingly the legislation did not amend Section 16.03 of the Charter, leaving in the Council both the power to amend the pension system and the power to establish which officers of the consolidated government would be responsible for the administration of the plan or the handling and investment of funds under the plan.

   Rather than eliminate the City Council's power to amend the plan, the new Section 22.07, entitled "Amendatory Power," confirmed the City Council's Section 16.03 power to amend the plan. While the new Chapter 22 of the Charter grants to the Board "sole and exclusive" responsibility for "administering the pension plan," Section 22.07 (a) distinguishes administering from amending the plan, stating: "Nothing herein shall empower the board to amend the provisions of the pension plan without the approval of the Jacksonville City Council." Subsection (b) also confirmed the City Council's power to amend the plan, providing: "No legislation shall be adopted by the Jacksonville City Council altering the terms of the pension fund without said legislation having first been referred to the board for its consideration and comment. The board may, as it deems necessary, recommend legislative changes and pass those recommendations on to the Jacksonville City Council as ordinances." Sections 16.03 and 22.07 of the Charter each grant to and confirm in the City Council the power to amend the pension plan. Section 22.07 creates a new procedural requirement before the City Council can exercise its power: the City Council, prior to enacting plan amendments, must refer all proposed amendments to the Board for review and comment.

4. Election of Board. Section 22.02(a) of the Charter provides that the membership of the Board shall consist of five members, two of whom shall be residents of the City of Jacksonville appointed by the City Council, one of whom shall be a police officer elected by a majority vote of police officers who are members of the pension fund, one of whom shall be a firefighter elected by a majority of the firefighters who are members of the pension fund, and the last of whom shall be a person chosen by majority vote of the other four members (whose name shall be submitted to the City Council, which shall, *as a ministerial act*, appoint such person as the fifth member of the Board). Terms are four years, unless, in the case of Council appointed trustees, they are sooner replaced by the Council, at whose pleasure they serve; or, in the case of the firefighter or police officer trustees, sooner if they leave the employ of the City. Any Board member may succeed himself/herself, and there are no term limits. Section 22.02(d) of the Charter provides that "[T]he provisions of chapters 175 and 185, Florida Statutes, the provisions of s.286.012, Florida Statutes, and the provisions of ss.112.311-112.315 and chapter 112, part VII, Florida Statutes, and as the same may be amended in the future, shall apply to each member of the board."

   The JPFPF is a "local law plan" under Chapters 175 and 185, Florida Statutes. These are the state statutes that govern local police and firefighter pension plans that participate in the distribution of the state excise tax on property and casualty insurance premiums (commonly referred to as "chapter funds"). However, as noted below, the JPFPF has been determined by the State Division of Retirement to be "deemed to comply" with Chapters 175 and 185; thus, many of the statutory requirements do not apply to JPFPF.

   F.S. 175.061(1) (b) 2. and 185.05(1)(a) provide for a five member board of trustees similar to the JPFPF board. However, Section 175.061(b) also provides, "With respect to a board of trustees operating a local law plan on June 30, 1986, this paragraph does not permit the reduction of the membership percentage of firefighters, or of firefighters and police officers where a joint or mixed fund exists. *However, for the sole purpose of changing municipal representation, a municipality may by ordinance change the municipal representation on the board of trustees operating a local law plan by ordinance, only if such change does not reduce the membership percentage of firefighters, or firefighters and police officers, or the membership percentage of the municipal representation."* (Emphasis added.) Since Section 22.07 of the Charter provides that the Board continued its existence without a break in continuity, the Chapter 22 Board was operating a "local law plan" on June 30, 2006. While the membership has changed and while the body responsible for selecting membership has changed, the "board of trustees" has operated the fund for more than 70 years. It is the opinion of the Office of General Counsel ("OGC") that these changes did not create new boards, but, rather, they continued the Board with different members. The OGC opined that viewing the Board as a continuously operating board is consistent with the fact that the current pension plan is a continuation of the 1937 Plan. Following the OGC opinion, if the Board is a continuation of the past boards, then Section 175.061(b) permits the City Council to amend the composition of the Board by ordinance.

In a letter dated June 29, 2012, the Bureau Chief for Local Retirement Systems of the Florida Department of Management Services stated that the JPFPF was “deemed to comply” with Chapters 175 and 185 pursuant to F.S. 175.351(2) and 185.35(2), based on the original 1937 special act that created the pension plan. It is OGC’s opinion and that of its special counsel, Jim Linn, that as a “deemed to comply” plan, JPFPF is not bound by the pension board composition requirements of Chapters 175 and 185 (although counsel for the JPFPF some of the lawyers on the Task Force disagree with that opinion).

Assuming that the board provisions of Chapters 175 and 185 do not apply to the JPFPF, then Section 16.03 of the Charter supports the power of the City Council to amend the composition of the Board by ordinance. Section 16.03 expressly permits the City Council to amend the composition of the Board. Indeed, Section 16.03 permits the City Council to decide "which officers of the consolidated government are responsible for the administration of the [pension] plans." It is OGC’s opinion that nothing in Chapter 22 of the Charter takes this power away from the City Council; and nothing in Chapter 22 conflicts with this power. Further supporting the efficacy of Section 16.03 in the opinion of the OGC is the fact that the Legislature readopted both Section 16.03 and Chapter 22 of the Charter when it readopted the entire Charter in Chapter 92-341, Laws of Florida.

Section 3.01 may, however, limit the City Council's power to propose an amendment to the Charter as it relates to the Board. That section grants the City Council power to amend the Charter, but requires approval by voter referendum if the amendment "relat[es] to appointive boards."

There is some nonbinding authority that suggests that the Council’s amendatory power has been diminished. The issue of eligibility for the “Chapter Funds” under Chapters 175 and 185, Florida Statutes, is also relevant. In the aforementioned June 29, 2012, letter, the Bureau Chief for Local Retirement Systems of the Florida Department of Management Services opined that since the Legislature established the makeup of the Board by enacting the special act which created the JPFPF and established the Board, any change in the makeup of the Board would have to be approved by the Legislature. However, it is the opinion of the OGC that the Bureau Chief’s opinion ignores the fact that the Legislature also enacted the provisions of Sections 3.01(e), 16.03, 22.02(d) and 22.07 of the Charter, which provide for amendment of the Charter by the City Council. In the opinion of the OGC a reasonable construction of F.S. 175.061(b) is that in addition to the Legislature’s ability to amend the Charter, the City Council may, by ordinance, change the election procedure for the fifth trustee to provide for appointment of that trustee by the City Council (or by the Mayor with the joinder of the Council), with a confirming referendum by a majority of Jacksonville voters. In the end, the ability or not of the City Council to amend the make-up of the Board will require a careful review by

OGC of all relevant information in light of various canons of statutory construction. If the OGC were to conclude that the City Council has the authority to amend the make-up of Board, that legal conclusion would likely be challenged by the JPFPF or the Unions.

5. Use of Office of General Counsel. As noted above, Section 18.07(d) of the Charter defines the Board as an independent agency of the consolidated City government. Section 7.201 of the Charter establishes "a department of the City of Jacksonville to be known as the office of general counsel, which shall have responsibility for furnishing legal services to the city *and its independent agencies*…." Section 7.202 of the Charter provides: "The head of the office of general counsel shall be the general counsel who shall be the chief legal officer for the entire consolidated government *including its independent agencies*." It goes on to state: "*Any legal opinion rendered by the general counsel shall constitute the final authority for the resolution or interpretation of any legal issue relative to the entire consolidated government and shall be considered valid and binding in its application unless and until it is overruled or modified by a court of competent jurisdiction or an opinion of the Attorney General of the State of Florida dealing with a matter of state involvement or concern.*" (Emphasis added in all quotations.)

   The intention of the framers of the consolidated government was that the OGC would provide legal representation to all components of the consolidated government of the City and would resolve disputes and disagreements within the consolidated government, much like subsidiary corporations would yield to the view of the corporate parent for the welfare of the corporate whole. It was intended that the substantial costs and legal fees which could result from intra-City disputes could be substantially lessened if the OGC acted as arbiter, with the perspective of the City as a whole. It was not that conflicts would not arise; rather it was that subordinate conflicts ultimately would yield to the decision of the consolidated whole.

   On November 19, 1987, James Harrison, then the OGC, in a letter addressed to John Keane as the chairman of the Board, advised: "[t]he Office of General Counsel can no longer represent the Board of Pension Trustees of the City of Jacksonville, Police Officer and Firefighter Pension Fund. Chapters 175 and 185, Florida Statutes, creates relationships, which despite all good intentions, place our attorneys in either a present or potential conflict of interest." He went on to say: "I will not quote the rules relating to the Florida Bar. Suffice it to say, professional ethics require me to make this decision as being in the best interest of your Board and the City at this time."

   The Harrison letter may have overlooked the structure of the consolidated government of the City, particularly the provisions of Charter Sections 18.06 and 18.07, expressing the intent that the government's parts were one consolidated government, and Charter Sections 7.104, 7.201 and 7.202 providing that (i) the OGC shall provide legal services to the consolidated government and (ii) the opinions of the OGC would be binding on all components of the consolidated government, including its independent agencies. Four other persons who have served as the City's

> OGC (*Messrs.* Franklin, Delaney, Arnold and Rinaman) and the current OGC (Ms. Laquidara) have all indicated that the Harrison letter is incorrect and that the Charter provides for the representation of all agencies and departments of the City by the OGC and for the resolution of intergovernmental conflicts by the OGC without there being an ethical violation.
>
> While the Board, under Section 22.04(e) of the Charter, has been granted the power to employ and pay attorneys as the Board may require, it does not expressly eliminate the direction in the Charter that all agencies would utilize the OGC for their legal services. (However, Section 121.101(c) of Jacksonville's ordinance code (not the Charter) provides that the Board "may" use the Central Services of the City, "but it is not required to do so.") Substantial savings could be realized if the Board were required to utilize the OGC for legal services.

Constitutional and Statutory Rights

A recent Florida Supreme Court decision describes the constitutional and statutory limitations on making changes to pensions for current employees as contrasted with new employees. In *Scott v. Williams,* 107 So.3d 379 (Fla. 2013), which involved modifications to a state retirement plan, including eliminating a COLA, the Court held that prospective adjustments could be made, but not retroactive adjustments or those that affect pre-existing benefits. Noting F.S. 121.011(3)(d), part of the "preservation of rights" statute, which provides, in part: "the rights of the members of the retirement system… are declared to be of a contractual nature, entered into between the member and the state, and such rights shall be legally enforceable as valid contract rights and shall not be abridged in any way," the Court held that:

> the preservation of rights statute was not intended to bind future legislatures from prospectively altering benefits for future service performed…. and the elimination of the COLA for services performed after that date are prospective changes within the authority of the Legislature to make. The preservation of rights statute does not create binding contract rights for existing employees to future retirement benefits." *Id*. at 389.

Thus the elimination of a 3% COLA as applied to benefits for services to be performed after the effective date of the amendment was permissible; but the 3% COLA would continue to apply to benefits for services performed prior to the amendment's effective date. Since the Court held that there was no contract with respect to changes applying to future job performance, there also was no unconstitutional taking in violation of Article X, Section 6 of the Florida Constitution, which provides that "No private property shall be taken except for a public purpose and will full compensation therefor paid to each owner…." The Court also held that a prospective change did not violate Article I, Section 6 of the Florida Constitution, which provides, in part: "The right of employees, by and through a labor organization, to bargain collectively shall not be denied or abridged."

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The resulting context for the Task Force is that changes in pension design for new employees are permissible, but as to current employees, changes that reduce benefits are only applicable to benefits earned with respect to work and services performed after the effective date of the change. Thus, if the Task Force were to recommend the elimination or reduction of the COLA presently granted to current employees, the change could lawfully be applicable only to benefits earned with respect to future work. Benefits earned with respect to work performed prior to the effective date of the change would continue to be increased by the 3% COLA already granted. It should be noted that "contractual rights", such as those of the members of a retirement system described above, could possibly be retroactively modified or eliminated pursuant to a proper filing by the City for protection under the bankruptcy laws; but that is not a viable option, as discussed below.

Investment Authority of JPFPF

Under Section 22.04(b) of the City's Charter, the JPFPF Board (the "Board") currently has the power to invest and reinvest the assets of the Fund in any lawful investment as provided in the applicable provisions of Section 215.47, *Florida Statutes*, provided the investment is permitted in the written investment policy adopted by the Board as provided in Chapter 112, Part VII, *Florida Statutes*. The Board's investment authority, as enunciated in Section 215.47, *Florida Statutes*, is restated in the Appendix. The Board has adopted an investment policy, entitled the "Statement of Investment Policy (The Investment Plan)", approved by the Board on December 20, 2012 (the "Investment Policy"). A copy of the Investment Policy is also included in the Appendix. The Investment Policy includes, *inter alia*, investment policies, authorized classes of investments, asset allocation policies, portfolio guidelines, measurement standards and reporting policies. It also establishes duties and responsibilities for the Board's investment manager.

Section 22.02(d) of the Charter provides that prior to the adoption of any change in asset allocation or the introduction of a new asset class, the Board shall deliver to the City Council Finance Committee written notice of the time and place of the meeting of the Board at which the proposed change or introduction shall be considered. The Policy provides, in Section II., subsection I. that the effective date of any amendment to the Policy shall be the 31st calendar day following the filing of the amendment with the City, as contemplated by Section 112.661(16), *Florida Statutes*.

Section 22.04(b) of the Charter also provides that notwithstanding anything to the contrary in Section 215.47, *Florida Statutes*, investments in fixed real estate assets shall not exceed twenty percent (20%) of the total assets of the Fund, at cost.

The City Council is considering an amendment to Section 121.101 of the Ordinance Code to add a new section (f), which would provide that the Board would be authorized to invest in:

"any lawful investments as provided in applicable provisions of s. 112.661, 175.07 (***sic***), 185.06, (***sic***) 215.47, Florida Statutes, and 'alternative investments', provided that: (i) the investment is permitted in the written investment policy of the Board; and (ii) investments in hedge funds are prohibited.

For purposes of the proposed amendment the following terms have the following meanings:

(a) “Alternative Investments” means an investment by the Board in a private equity fund, venture fund, or distress fund or a direct investment in a portfolio company through an investment manager.
(b) “Alternative investment vehicle” means the limited partnership, limited liability company, or similar legal structure or investment manager through which the Board invests in a portfolio company.
(c) “Portfolio company” means a corporation or other issuer, any of whose securities are owned by an alternative investment vehicle or the Board and any subsidiary of such corporation or other issuer.
(d) “Portfolio positions” means individual investments in portfolio company in which the alternative investment vehicle in invested.

The City Council Finance Committee deferred its consideration of the amendment until the Task Force could provide its recommendations concerning the proposed changes.

The “30-Year Agreement”

On February 13, 2001, the City Council enacted Ordinance 2000-1164-E, which among other things authorized the execution of a Restated Agreement between the City and the JPFPF in which the City and the JPFPF settled certain disputes, implemented the addition of a COLA benefit for employees of JSO and JFRD, authorized the use of certain reserve accounts and the “Enhanced Benefit Account” into which the “Chapter Funds” (the State of Florida excise tax on insurance premiums) due the JPFPF under Florida Statutes, Chapters 175 and 185, Florida Statutes, and consolidated and restated other agreements concerning pension benefits and their funding. On April 8, 2003, March 9, 2004, and March 23,2006, the City Council enacted Ordinance No. 2003-303-E, Ordinance No. 2003-1338-E and Ordinance No. 2006-508-E, respectively, which amended the original Restated Agreement, which, as amended, is commonly known and referred to as “The 30-Year Agreement”. The stated term of the 30-Year Agreement ends on September 30, 2030.

The 30-Year Agreement continued or established the current pension design and funding for the Unions and the JPFPF. The current pension design established by the 30-Year Agreement is shown below:

<u>Plan Parameters: From 30-Year Agreement</u>

Retirement Eligibility**:** 20 years after joining the Police and Fire Pension Fund

Vesting Eligibility: 5 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 2 years

Employee Contribution: 7 percent of pay

COLA: 3 percent compounded annual increase

The 30-Year Agreement established a "City Budget Stabilization Account" (the "CBSA"), effective April 1, 2000, which was to provide funds that were to be used to help the City meet its funding obligations under the 30-Year Agreement. The Agreement also provided for the use of the "Chapter Funds" allocated to the JPFPF by the State of Florida from collections of the statewide insurance premium tax. The Chapter Funds were to be deposited in the CBSA, and, effective April 1, 2000, a portion of the funds were to be used to help the City meet its funding obligations under the 30-Year Agreement. The use of the CBSA was intended to be limited.

Today Chapter Funds from the CBSA are used as follows: contributions towards the normal cost of pension benefits of up to 4 percent of payroll are to be made from Chapter Funds as long as the Chapter Funds exceed at least 4.35 percent of payroll. Any amount beyond that is to be deposited into the Enhanced Benefit Account and is to be available to provide bonus pension payments or other benefit increases. In 2013, the JPFPF received $9,667,185 in Chapter Funds and deposited them into the CBSA. Of that, $5,238,887 was used to pay base benefits for that year, and the residual of $4,428,298 was deposited into the Enhanced Benefit Account to pay future enhanced benefits and an "annual retiree bonus". In 2013, the "annual retiree bonus" totaled $1,923,202. No other enhanced benefits were created or paid.

The undisbursed amounts now residing in the Enhanced Benefit Account total $27,647,091. In the MSA the City and the JPFPF agreed that the then current balance of approximately $20 million would be used to pay for a portion of the JPFPF ARC payable by the City.

It should be noted that under Section 106.08 of the Jacksonville Ordinance Code, benefits cannot be enhanced under any of the City's pension plans until the particular plan is at least 90% actuarially funded.

In 2013, Randall Wyse and other plaintiffs, who are firefighters employed by JFRD and members of the JPFPF, filed a Complaint in the United States District Court against the City and the JPFPF (the "Federal Litigation"). The Complaint alleges among other things that the 30-Year Agreement's terms and benefits were set through September 30, 2030, and cannot be modified. The Complaint further alleges that the collective bargaining agreements between the City and the Unions do not cover the JPFPF and employees of JFRD or JSO, and that the City's alleged attempts to engage in collective bargaining with respect to pension benefits covered by the 30-Year Agreement violated the agreement. The Complaint sought a declaration of rights with respect to the 30-Year Agreement and the entry of an order specifically enforcing the 30-Year Agreement and enjoining the City from utilizing the collective bargaining process *vis-à-vis* the Unions, the JPFPF and members thereof. The JPFPF filed a Cross-Claim against the City seeking similar relief.

The City denied most of the allegations of both the original Complaint and the Cross-Claim. Generally stated, it is the Plaintiffs' and JPFPF's position that the 30-Year Agreement is valid and enforceable throughout its term, and that pension benefits cannot be changed during that term. Generally speaking, it is the City's position that the 30-Year Agreement is invalid and unenforceable, and that pension benefits are the continuing subject of collective bargaining.

In an effort to settle their differences, the parties in the Federal Litigation agreed to mediate their dispute pursuant to the Federal Rules of Civil Procedure, which resulted in their agreement to the Mediated Settlement Agreement, or MSA, referred to above. The Unions also joined in the execution of the MSA.

As stated above, in June, 2013, the *Times-Union*, through its editor, Frank Denton, moved to intervene in the Federal Litigation based on alleged Sunshine Law violations and for other reasons. The Court denied the motion to intervene, but permitted the filing of a "friend of the court" brief on certain issues. In addition to its attempt to intervene in the Federal Litigation, the *Times*-Union, through Mr. Denton, filed suit in Duval County Circuit Court to invalidate the Mediated Settlement Agreement, also based on Sunshine Law violations and other reasons (the "State Litigation").

On December 31, 2013, Waddell A. Wallace, III, the state Circuit Judge before whom the State Litigation was pending, entered a Summary Final Judgment (the "Circuit Court Decision") holding that police and fire pensions are subject to collective bargaining and cannot be the subject of a separate agreement between the City and the Fund. Rather, pursuant to the Circuit Court Decision, matters concerning pension design must be negotiated in collective bargaining with the bargaining agents of the police and fire employees of the City, or their representatives.

The Circuit Court Decision did not explicitly invalidate the 30-Year Agreement, but the implication was that to the extent it sought to set pension benefits for the entire term of the agreement, it was unenforceable. The Circuit Court Decision enjoined the City and the JPFPF from conducting further mediation proceedings which involve, in the Court's judgment, negotiating pension benefits. The City and the JPFPF were ordered to advise the federal court in the Federal Litigation that they had been so enjoined, but the Circuit Court Decision recognized that because of the supremacy clause in the United States Constitution, if the federal court nevertheless ordered them to mediate outside the public eye, they would have to comply with the directives of the federal court. The Circuit Court Decision also enjoined the City and the JPFPF from meeting with the Unions or with each other to negotiate pension benefits without notice to the public and otherwise complying with the Sunshine Law.

A Motion for Rehearing of the Circuit Court Decision has been filed by the Fund, in which the City has joined. The Fund and the City have also filed Notices of Appeal; and Randall Wyse and other persons who were plaintiffs in the Federal Litigation have filed a motion to void the Circuit Court Decision.

It is possible that the Circuit Court Decision will be modified, reversed or vacated, which creates some procedural confusion for the Task Force.

Bankruptcy

Some Jacksonville citizens have suggested that the Task Force consider certain "debtor protection" remedies such as a declaration of financial emergency or reorganization proceedings under the United States Bankruptcy Code. Detroit is the most commonly suggested example.

The declaration of municipal bankruptcy is an emergency measure and has been used as a last resort by cities that are distressed and have no alternatives. Municipalities entering bankruptcy, while few and far between, have been thrown into periods of extreme uncertainty that significantly hinder their operations and ability to maintain core governmental services at current levels, receive credit from their vendors and access capital markets. Bankruptcy is therefore not in the best interest of Jacksonville residents nor is it a realistic remedy for the City's problems. In addition, there are formidable substantive and procedural requirements of the Bankruptcy Code that Jacksonville would be unable to satisfy given its current stable financial condition and its capacity for additional revenue.

Nevertheless, in order to make the community aware of the limitations of the bankruptcy remedy for Jacksonville, the Task Force had legal research performed to learn in general terms the requirements of the Bankruptcy Code as applied to municipalities (the consolidated City of Jacksonville also being a county):

> In order for a municipality to file a Chapter 9 bankruptcy, it must prove insolvency, obtain the state's approval and prove it negotiated in good faith, or alternatively, show that it became impracticable to do so. The following are some criteria a municipality should be prepared to show when filing a Chapter 9 bankruptcy petition:
>
> - The municipality has made efforts to obtain additional funds to pay obligations by making reasonable reductions in spending and that further spending cuts would be counterproductive;
>
> - The municipality is proposing adequate use of taxation to help it meet its payment obligations and raising taxes any further would be counterproductive;
>
> - The municipality's rejection of obligations to fund pensions is reasonably done, with reasonable replacement contracts for current employees and minimal retroactive impact on already-retired employees;
>
> - The municipality's plan will pay residual available cash to unsecured labor contract rejection claims and the municipality is proposing to pay all that it can reasonably afford to pay to its unsecured creditors.

For the foregoing reasons the Task Force concluded that a Chapter 9 bankruptcy is neither a realistic nor helpful alternative for the City of Jacksonville and its citizens.

RECOMMENDATIONS OF THE TASK FORCE

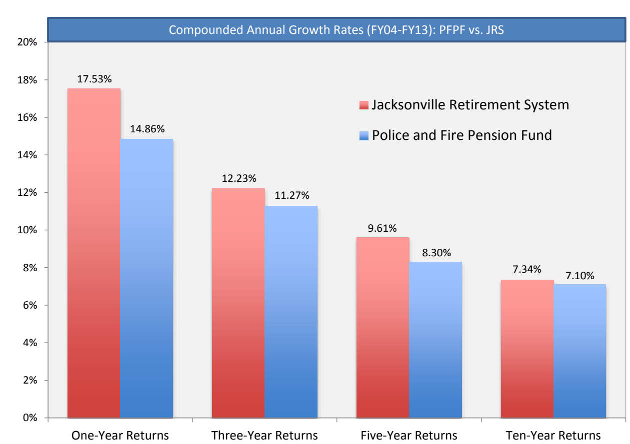
Having reviewed the context in which the Task Force finds itself, this Report now turns to specific recommendations. The recommendations focus on four areas of concern: (i) governance, which includes recommendations for the revision of the 30-Year Agreement, (ii) the JPFPF's investment authority, (iii) retirement pension benefit design; and (iv) reducing the UAAL. The first two and fourth areas of concern can be reformed by agreement of the City and the JPFPF, upon action by the City Council, the Mayor and the Board of Trustees of the Fund, which the Task Force strongly urges. Because of the Circuit Court Decision, and subject to its finality, the Task Force's recommendations as to pension design are recommendations to the City as positions the City should advance in the collective bargaining process.

<u>Governance Reforms</u>

The JPFPF is governed by a five-member board of trustees. Two of the trustees must be residents of the City of Jacksonville and are appointed by the City Council. One trustee must be a police officer elected by a majority vote of the police officers who are members of the JPFPF. Another must be a firefighter elected by a majority vote of the firefighters who are members of the JPFPF. The fifth trustee is chosen by a majority of the other four trustees and the name submitted to the City Council, who appoints that person as a ministerial act.

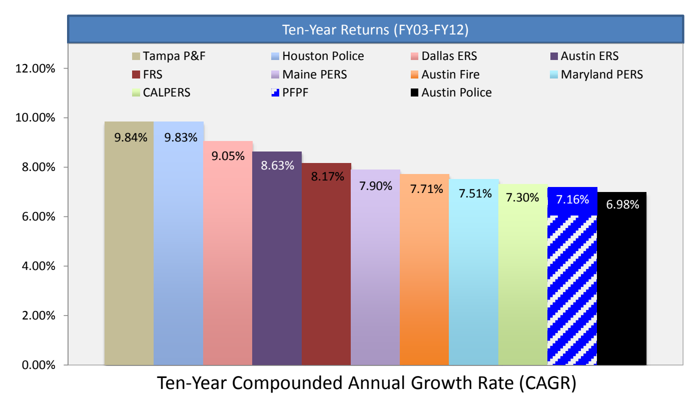
The Board utilizes the services of an investment manager who advises the Board on its investment policies and decisions, and who implements those decisions. The investment manager's duties and responsibilities are enunciated in the Board's Investment Policy, as noted above. The Board does not utilize an investment committee as does the Florida Retirement System. Task Force members have experience with other organizations which use investment committees in addition to investment managers, and they believe that the use of an investment committee is a "best practice". It is the opinion of the Task Force that a volunteer investment committee consisting of knowledgeable investment and financial professionals would be helpful to assuring sound financial and investment decisions by the Board.

In recent periods the JPFPF's investment returns have lagged the Jacksonville General Employees' Pension Fund, which has comparable asset allocations to those of the JPFPF's. JPFPF performed in the middle of the pack compared to some other public pension funds that MAEVA was able to find return data over matching time periods.



Sources: Summit Strategies Group PFPF 2013 Flash Report, 30 September 2013; Summit Strategies Group JRS 2013 Flash Report, 30 September 2013

Note: The Jacksonville Retirement System jointly manages the assets of the General Employees Pension Plan and the Corrections Officers Pension Plan.



Note: These public plans all have assets > $500mm and 9/30 reporting periods; returns are taken from public disclosures as of 9/30/2012.

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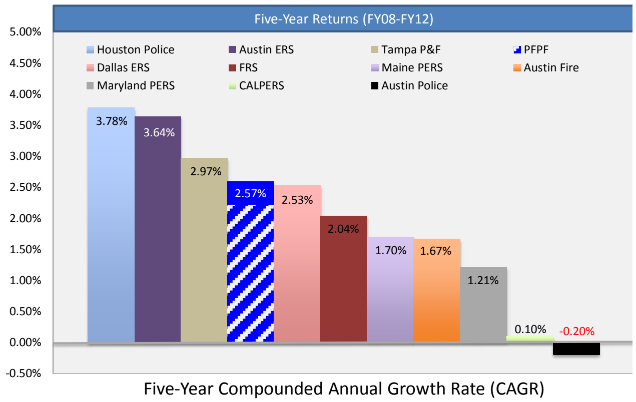
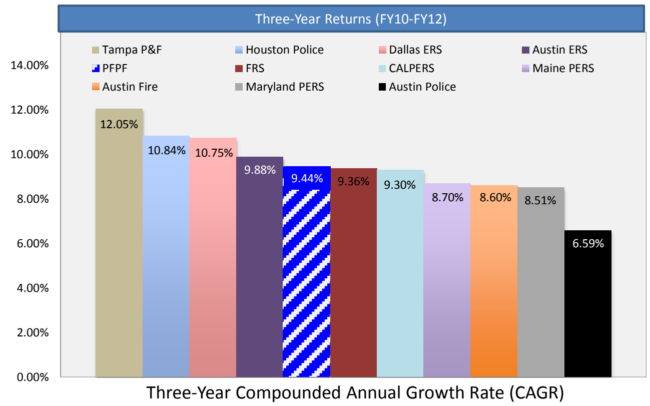


Note: These public plans all have assets > $500mm and 9/30 reporting periods; returns are taken from public disclosures as of 9/30/2012.



Note: These public plans all have assets > $500mm and 9/30 reporting periods; returns are taken from public disclosures as of 9/30/2012.

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A presentation to the Task Force also revealed that the JPFPF relies on largely active rather than passive investment strategies for its equity investments. Active investing may bear more risk and, in the case of the JPFPF resulted in higher investment management fees. For example, the presentation showed that the JPFPF's active management of equity investments was 83% of the Fund's equity assets and compared unfavorably with those of the Florida Retirement System and other pension funds.

A Comparison of Active % Passive Equity Management						
	Jacksonville PFPF (Recommended Targets)		**Florida Retirement System**		**CalPERS**	
	Active	Passive	Active	Passive	Active	Passive
Equities	83.4%	16.7%	51.1%	48.9%	31.0%	69.0%

Sources: Summit Strategies Group Memo Dec 20, 2012; FRS Staff; CalPERS Facts at a Glance January 2013 (p. 4)

The implementation of the JPFPF's investment policies resulted in professional service fees and administrative expenses equal to 74 and 78 basis points as a percentage of assets in 2012 and 2013, respectively, as compared with 30 basis points in 2011 for those items for the Florida Retirement System (the 2011 calendar year being the latest available from Florida Retirement System at the time).

A Comparison of Total Plan Fees: PFPF vs. FRS			
	PFPF (FY13)	**PFPF (FY12)**	**FRS (CY11)**
Professional Services Fees	$5,937,000	$5,745,347	N/A
Administrative Expenses	$3,265,154	$2,547,264	N/A
Total Fees	$9,202,154	$8,292,611	$376,721,095
Assets (Beginning of Year)	$1,173,771,828	$1,116,370,870	$126,579,719,608
Fees as Percentage of Assets	78 bps	74 bps	30 bps

Sources: PFPF 2012 Annual Report (p. 4) and document supplied by PFPF: Attachment Detail for Page 6, Item 4; Florida Retirement System 2011-2012 Annual Report (pp. 24 and 27)

All-in costs for the FRS Defined Benefit Plan include:

1. Investment management costs, including those related to externally managed assets and internally managed assets
2. Overlay costs (forex, asset allocation programs, etc.)
3. Oversight, custodial and other costs (staff salaries, direct expenses, overhead, etc.), trustee and custodial services, consulting and performance measurement costs, audit costs, legal expenses and other asset-related costs (benefits administration costs, actuarial valuations fees, etc.)

The Task Force believes that if the City is going to provide substantial additional funds on a voluntary basis so as to reduce the UAAL over an accelerated period, the City should have a greater say in the governance of the JPFPF. The Task Force has been advised that the City Council is addressing this by asking the Florida Legislature to amend the Charter to provide for participation by the Council in more than a nominal way in the selection of the fifth JPFPF trustee. However, the Task Force believes that because Jacksonville's government is a "strong mayor" government with the mayor as the chief executive officer of the City, the mayor is an important stakeholder. It would therefore be better for mayors to participate in naming the persons who govern the JPFPF. Consequently the Task Force favors the fifth trustee being appointed by the Mayor and confirmed by the City Council. The process being suggested by the City Council leaves mayors out. In any event, changing the manner of election, and the qualifications, would require an amendment to the Charter, which, in the case of amendments affecting the JPFPF, can only be done by the Florida Legislature alone or by the City Council with a subsequent ratification by Jacksonville voters in a referendum. The Task Force concludes that if the Legislature refuses to amend the Charter to provide more accountable governance, the City Council should do so, asking the voters to approve any amendment by referendum.

The JPFPF presently maintains ethical standards and disclosure requirements for its advisors. The Task Force believes that it is appropriate to state publicly and incorporate into the Ordinance Code strong ethical and disclosure standards so that policymakers and the public can know what those standards are and can expect them to be followed.

As noted above, the Charter gives the JPFPF the power to employ attorneys and other consultants. All of the other independent agencies and boards of the City, except the Jacksonville Transportation Authority, use the OGC for their ordinary legal services. The Task Force believes that such should be the case with the JPFPF, recognizing that the JPFPF has a definite need for quality legal advice in the pension field.

Finally, the Task Force agrees that the 30-Year Agreement is too lengthy and should be terminated and comparable agreements incorporated into a new "2014 Agreement" which would be monitored and enforced by a respected community leader until the JPFPF attains an 80% funded ratio. The other governance recommendations should be permanent improvements. The

Task Force's endorsement of the pension design and funding obligations as recommended below are contingent upon the governance of the JPFPF being changed as contemplated by the Task Force's recommendations. Attention should be given by policy makers to the whole report of the Task Force and to the entire package of recommendations, not to individual parts.

Recommendations for governance reforms include:

1. Financial and Investment Advisory Committee. The Jacksonville Municipal Code (the "Ordinance Code") should be amended to require the JPFPF to appoint a financial and investment advisory committee (the "Financial Advisory and Investment Committee") of five (5) persons who will be charged with advisory oversight to the JPFF Board on financial matters, actuarial practices and assumptions, investment strategy and policy, and the selection of outside financial services providers, including investment managers and advisors. Financial Advisory and Investment Committee members will serve in a volunteer capacity and be financially sophisticated professionals who bring expertise to the Fund's actuarial needs, fiscal operations and investment practices. Criteria for service will include knowledge of and experience and familiarity with portfolio and/or pension fund management, institutional investment and fiduciary responsibilities. Members of the Financial Advisory and Investment Committee must be residents of Duval, Nassau, St. Johns, Baker or Clay County, Florida. Financial Advisory and Investment Committee members will be nominated for service by the Board and confirmed by majority vote of the Jacksonville City Council. The term of office will be three years, with the possibility of two additional consecutive three-year terms. The initial terms will be staggered, with two persons to serve initial terms of two years and three persons to serve initial terms of three years. The Financial Advisory and Investment Committee shall annually elect a chair and secretary from its members. The Board shall provide administrative support to the Financial Advisory and Investment Committee.

   Financial Advisory and Investment Committee members shall be deemed to be fiduciaries of the JPFPF and will be required to undergo periodic fiduciary training as required by the Board and, together with members of the Board, shall submit to the proper authority the "Form 1" annual public conflict disclosure statements as do members of other public agencies and boards. Any business organization or affiliate thereof that is owned by or employs a member or a spouse, child or sibling of a member of the Financial Advisory and Investment Committee shall not directly or indirectly contract with or provide services for the investment of JJPFPF assets during the time of such member's service on the Financial Advisory and Investment Committee or for two (2) years thereafter (unless such potential conflict is fully disclosed to all Trustees of the JPFPF as well as to all existing members of the Financial Advisory Investment Committee and all such Trustees and committee members who have no apparent conflict in the matter unanimously approve and agree that the JPFPF will not be adversely impacted by such contract or services and that the allowance of such contract or services together with service by the Committee member or potential Committee member are in the best interest of the JPFPF).

For general strategy matters (*e.g.*, actuarial practices and assumptions, asset allocation, accounting determinations, risk management, actuarial assumptions, etc.) the Financial Advisory and Investment Committee will provide advice and recommendations to the Board, which shall receive and act upon such advice and recommendations as the Board, in its fiduciary capacity, shall determine. For the selection of individual investment managers, the Financial Advisory and Investment Committee will work with the JPFPF's professional staff to rank all potential asset/investment managers and recommend particular selection(s). Following its review the Financial Advisory and Investment Committee shall make its recommendations to the Board. The Board will then make its decision(s) taking into account such recommendations and other information which is available to the Board. For the selection of other financial professionals, including actuaries, the Financial Advisory and Investment Committee will furnish advice to the Board following such processes as may be determined with respect to the particular selection. The Financial Advisory and Investment Committee's work will be subject to Sunshine and Public Records Laws.

2. <u>Ethics, Certification and Disclosure Requirements for Investment Managers and Advisors</u>. The City and the Board intend to assure that investment managers and advisors employed by the JPFPF will reflect the highest ethical standards and investment performance, and that they will report regularly to the Financial Advisory and Investment Committee and the Board on matters within their engagement. Consequently: any investment manager or advisor of the JPFPF who has discretionary authority for any investment of the JPFPF shall agree to certify and/or disclose annually to the Financial

Advisory and Investment Committee and to the Board, no later than the January 31 following the previous calendar year, that:

<u>Certifications:</u>

(a) The investment manager or advisor serves as a fiduciary to the JPFPF, and all investment decisions made by the investment manager or advisor on behalf of the JPFPF are made in the best interests of the Fund and not made in a manner to the advantage of such investment adviser or manager, other persons, or clients to the detriment of the JPFPF;

(b) Appropriate policies, procedures, or other safeguards have been adopted and implemented by such manager or advisor to ensure that relationships with any affiliated persons or entities do not adversely influence the investment decisions made on behalf of the JPFPF;

(c) The investment manager or advisor is not the subject of a claim or litigation brought by a present or former client or by a regulatory agency asserting that such investment manager or advisor has breached its fiduciary responsibilities, or, if such be the case, disclosing the particulars of each such claim or litigation;

(d) A written code of ethics, conduct, or other set of standards, as submitted to the Financial Advisory and Investment Committee and the Board and acceptable to them, governs the professional behavior and expectations of owners, general partners, directors or managers, officers, and employees of the investment adviser or manager, has been adopted and implemented, and that such standards are effectively monitored and enforced; and

(e) Policies of the JPFPF concerning prohibited business relationships among family members and other related parties have been complied with.

Disclosures:

(f) Any known circumstances or situations that a prudent person could expect to create an actual or potential conflict of interest, including specifically (i) any material interests in or with financial institutions with which officers and employees conduct business on behalf of the JPFPF, and (ii) any personal financial or investment positions of the investment manager of advisor that could be related to the performance of an investment program of the JPFPF over which the investment advisor or manager has discretionary investment authority on behalf of the JPFPF; and

(g) All direct or indirect pecuniary interests that the investment manager or advisor has in or with any party to a transaction with the JPFPF if the transaction is related to any discretionary investment authority that the investment manager or advisor exercises on behalf of the JPFPF.

3. Use of Office of General Counsel. While the Charter gives the JPFPF the authority to employ separate counsel, the JPFPF should ordinarily use the Office of General Counsel of the City (the "OGC") for its legal needs. The JPFPF should consult with the OGC should it find that the JPFPF needs additional or separate counsel for specific purposes, including the nature of the work and the fee arrangement. The JPFPF and the OGC have consulted concerning the need for specific pension and retirement-related advice, and the OGC has indicated that she concurs with the engagement on such matters of Klausner, Kaufman, Jenson and Levinson ("Special Counsel"), who are currently counsel to the JPFPF. The OGC has further indicated that she is familiar with and concurs with the fee arrangement that the JPFPF has with the Special Counsel. The OGC and the Special Counsel will consult regularly to assure that the legal needs of the JPFPF are being competently and efficiently handled for a reasonable fee. The Task Force also recommends that the OGC research and issue a binding opinion pursuant to Section 7.202 of the Charter concerning the powers of the JPFPF to employ counsel and the JPFPF's responsibility under the Charter to utilize the OGC for its legal needs.

4. Selection of JPFPF Board Members. The terms of Trustees of the JPFPF should be as provided in Section 22.02(a) of the Charter. Presently the City Council appoints two Trustees, one Trustee is elected by the fire and safety members of the JPFPF, one Trustee is elected by the police members of the JPFPF, and the fifth Trustee is elected by

majority vote of such four Trustees. The Task Force recommends that the selection process be modified in the Charter to provide for the appointment of the fifth Trustee by the Mayor with the approval of the City Council.

5. Qualifications for Council-appointed Trustees and the Fifth Trustee. Persons appointed to serve as Trustees of the JPFPF by the Mayor and City Council should be persons with professional financial experience and/or public pension experience, governance experience, institutional investment experience, community experience and wisdom, or comparable professional training, knowledge, and expertise.

6. Actuarial Standards, Transparency and Disclosure. The assumed annual actuarial rate of return should remain at 7.0% through the term of the "2014 Agreement", defined below, unless otherwise agreed by the City and JPFPF based on sound actuarial practices, or as otherwise required by applicable law. An actuarial valuation of the JPFPF should be performed by the JPFPF's actuary annually, as of October 1 of each fiscal year. The annual actuarial valuations should be completed and delivered as expeditiously as possible to the Board, the Financial Advisory and Investment Committee, the City's Director of Finance and to the City Council Auditor promptly upon completion but in any event the JPFPF shall complete and deliver such analyses and reports no later than 120 days after the end of each fiscal year, provided the City has responded promptly to requests made by the JPFPF for information from the City that is necessary for the preparation of such valuations. Actuarial analysis and reporting by the JPFPF will utilize the following standards in addition to other standards governing its work:

   a. Annual ARC calculations based on most recent actuarial assumptions;
   b. Alternative funding scenarios based on variable investment performance in addition to the base case, that extend to future years and incorporate volatility;
   c. The latest "experience studies" prepared by the JPFPF's actuary;
   d. Consistency in actuarial methods;
   e. Accrual method: Entry Age Normal (EAN);
   f. Annual normal cost disclosure; ***Note: it is now likely that since there will be two tiers of benefits if the Task Force's recommended design is implemented, the normal cost should be broken out for each tier.***
   g. Actuarial practices will be consistent from year to year unless changed through an "experience study" or decision of the Board, with advice from the Financial Advisory and Investment Committee, or unless necessary for compliance with applicable laws or regulations;
   h. Unfunded liabilities will be amortized as separate annual bases over closed 30-year periods or less, unless otherwise required by law; and
   i. Clear and transparent disclosure of actuarial and financial matters, including distributing to City's Chief Financial Officer and City Council Auditor, and prompt posting on the Fund's website, the JPFPF's quarterly investment return reports showing results both gross and net of investment fees and with comparisons to assumption and benchmarks of the JPFPF, and to results of comparable pension funds.

In addition to the foregoing regarding the standards for actuarial and financial studies, on or before 120 days after the end of each fiscal year of the Fund, currently September 30 of each year, commencing with the end of the 2014 fiscal year of the JPFPF, the Board should prepare annual financial statements and submit them electronically or as otherwise agreed to the Mayor, City Council President, City Director of Finance, City Council Auditor, and the Treasurer of the JPFPF; and, on or before March 15 of each year, to the Florida Department of Management Services (the “Department”) in format(s) prescribed by the Department. The financial statements will:

j. Be in compliance with the requirements of the Government Accounting and Standard Board's Statement No. 67, Financial Reporting for Pension Plans and Statement No. 68, Accounting and Financial Reporting for Pensions, using the mortality tables and generational projections by gender most recently available from qualified actuarial sources. If yet unaccepted updates also are available that suggest longevity improvements beyond accepted tables, then such updates shall be used in lieu of accepted tables so long as such usage remains acceptable within GASB requirements and is permitted by applicable law;
k. Report funding status, contribution rates and expected normal cost of new benefits earned using both the current assumed rate of return on investments and the greater of 5.4% or an assumed discount rate that is 200 basis points less than the Fund's assumed rate of return; and
l. Provide information indicating the projected assets, liabilities and actuarially required contributions to the Fund over the next 30 years based on the Fund's latest valuations and actuarial assumptions.

In addition to the above information, the JPFPF should also make available on a timely basis on its website prior actuarial studies and reports in order that accurate comparisons can be made, minutes of its meetings for the past 3 years on a rolling basis, and copies of all reports or studies commissioned by the JPFPF that are matters of public interest, including experience studies and investment performance reports.

7. <u>Selection of Future Administrator/Chief Investment Officer</u>. The selection of any future Plan Administrator/Chief Investment Officer of the JPFPF should be governed by a professional process subject to Florida law in which the candidate will be selected using the City Employee Services Department’s search and selection processes, and, if necessary, utilizing the assistance of an executive search firm retained by the Board. A salary and benefits survey should be conducted prior to advertising for the position in order to establish a compensation level comparable to funds of similar size and complexity to the Fund. In addition to the requirements of applicable law, candidates will be required to have a minimum of five years of pension administration or institutional investment experience, expertise in the oversight of investment portfolios, and a degree in finance, economics, accounting or a related area of study from an accredited university, or comparable training and experience. Comparable experience directing the activities of a state or local public pension plan will also be considered. As agreed in the MSA, candidates who are CPAs or who have a JD, MBA or CFA degree will be preferred.

8. Future Administration of the JPFPF. Upon the selection of the next Administrator/Chief Investment Officer of the JPFPF, the aggregate compensation of the JPFPF's Administrator/Chief Investment Officer shall be determined in accordance with the market analysis of comparably-sized public pension plans provided for in recommendation 7 above. The City and/or JPFPF shall assure that any future Administrator and/or senior management employee shall be placed in the City General Employees' Pension Fund. The JPFPF's current Senior Staff Pension Plan will be frozen as of the close of the pay period immediately preceding August 15, 2014, and following that date no further benefits will accrue under the Senior Staff Pension Plan. Benefits will be distributed to Senior Staff Pension Plan participants after closure of the Plan as if such participants had been enrolled in the Florida Retirement System Special Risk Plan, or by the purchase of annuities as permitted by law.

9. Revision of the 30-Year Agreement. The City and the JPFPF should agree that the 30-Year Agreement will be terminated and a new agreement entered into (herein referred to as the "2014 Agreement"). The 2014 Agreement should provide that the agreements made in the 30-Year Agreement as to the funding obligations of the City and the employees and JPFPF will be continued, as modified by the recommendations of the Task Force; and the 2014 Agreement should incorporate the recommendations of the Task Force therein. However, the governance recommendations of the Task Force should be accomplished permanently by amendment to the Charter and/or Ordinance Code, as appropriate, and should not be incorporated into the 2014 Agreement. To the extent there is a conflict between the provisions of the 30-Year Agreement and the recommendations of the Task Force, such recommendations shall control. The 2014 Agreement shall terminate on the date upon which the JPFPF fund assets reach a funded ratio of 80%, that is, the actuarial value of assets divided by the actuarial accrued liability equals 80% or more (the "Agreement Termination Date").

   Because of the Circuit Court Decision, unless it is reversed or modified, the 2014 Agreement will not be concerned with the Task Force's recommendations concerning pension benefits for police and fire employees.

   The 2014 Agreement shall retain the provisions of the 30-Year Agreement concerning the funding obligations for the JPFPF, and shall incorporate the recommendations of the Task Force that concern funding the unfunded actuarial accrued liability (including the contributions required of the City).

   In order to provide for the enforcement of the 2014 Agreement and increased transparency, in the 2014 Agreement the City and the JPFPF shall agree, *inter alia*, that until the Agreement Termination Date the performance of both the City and the JPJFPF under the 2014 Agreement shall be monitored and enforced by a special master (the "Master") whose appointment will be requested of the United States District Court before whom the Federal Litigation (defined above) is pending. The Master will examine and certify on a quarter-annual basis whether: (i) the City is paying its contributions to the Fund or on its behalf on a timely basis in accordance with the terms of the 2014

Agreement; (ii) whether the Financial Advisory and Investment Committee is performing the functions for which it was created and whether its recommendations of the Task Force are being received and acted upon by the Board in the manner contemplated by the 2014 Agreement; (iii) to the extent that the JPFPF's investment performance is at variance with actuarially assumed returns or with the investment performance benchmarks established, net of fees, for such investments, whether the Financial Advisory Investment Committee has provided reasonable explanation as to the investment actions, if any, that will be taken in consideration of such variability; (iv) whether the City and Board are each exercising transparency in the conduct of their affairs concerning the Fund and its administration; and (v) such other matters as may be reasonably requested by either the City or the JPFPF, or as may be deemed necessary by the Master.

The City and the JPFPF have agreed that they will request the United States District Court to appoint the Honorable Harvey E. Schlesinger, United States District Judge, as the initial Master and that his successor(s), if any, will be person(s) of comparable experience, temperament and community respect. It is intended that reports shall be made to the Master on a quarter-annual basis, in public proceedings, and that copies of such reports shall be made available to the public at large promptly upon filing. It is also intended that for jurisdictional and enforcement purposes the Federal Litigation should continue until at least the Agreement Termination Date.

10. Return to Collective Bargaining. Unless the Circuit Court Decision is modified or reversed, the determination of retirement benefits for police and fire employees shall immediately be resumed through the collective bargaining process as defined in Chapter 447, Florida Statutes, and other applicable law. If the Circuit Court Decision is modified or reversed, the pension benefits set forth in the 30-Year Agreement, as modified by the recommendations of the Task Force, shall be incorporated into the 2014 Agreement for its term, and it shall provide that collective bargaining of police and fire pension benefits shall recommence upon the Agreement Termination Date, unless such modification or reversal requires otherwise.

11. Consultation among Parties. The City and the JPFPF should consult on an ongoing basis related to their performance under the 2014 Agreement, public records, open government issues and other matters. Senior representatives of each should meet monthly to discuss matters of importance to either, and both parties should proceed in a spirit of good faith and cooperation. In that regard, the parties should make available to each other on a continuing basis, all information that is necessary to assure their mutual understanding and success. The City and the JPFPF should endeavor to work harmoniously to enforce their respective obligations hereunder, under the 2014 Agreement, and applicable Charter, statutory and Ordinance Code provisions, and to avoid obstruction of their respective rights.

12. Expression by Charter and Ordinance. The City and the JPFPF should agree to articulate the recommendations of the Task Force by supporting and promulgating the 2014 Agreement and by supporting and promulgating appropriate revisions to the Charter and

Ordinance Code, as the case may be that will accomplish their recommendations of the Task Force.

13. Application to General Employees and Correctional Officers Pension Plans. While the General Employees' Pension Plan and the Correctional Officers Pension Plan are not within the purview of the Task Force's charge, the Task Force suggests that the recommendations set forth in Sections 1 (the Financial Advisory and Investment Committee), 2 (ethics and disclosure requirements) and 6 (standards for actuarial analysis and reporting), of this Governance section should be considered by the City for application to those pension plans.

Investment Authority Reforms

The Task Force discussed the current investment policies and authority of the JPFPF as set forth above. The members of the Task Force felt that its mission was not originally considered to include the consideration of the JPFPF's investment authority, but that an evaluation could be expertly conducted by the Financial and Advisory Committee that the Task Force recommends as a JPFPF governance improvement. The Task Force recommends that the City Council defer its consideration of the expansion of the investment authority of the JPFPF until the Financial Advisory and Investment Committee can weigh in on the subject and make recommendations to the Board and to the City Council.

After reviewing the City Council legislation, the Task Force makes the following observations:

1. The reference to F.S. 175.07 should be to F.S. 175.071. There is no F.S. 175.07.

2. As to the authority to invest in real estate, Charter Section 22.04(b)(2) contains a 20% limitation for real estate investments. While the Task Force encourages the City Council to seek the advice of the Financial Advisory and Investment Committee concerning whether investments in real estate should be permitted, a similar limitation should be included in the legislation in order that the Ordinance Code does not conflict with the Charter.

3. There needs to be a definition of "hedge fund" in the legislation so that it is clear to the City Council, the JPFPF and the public as to what specific types of investment the legislation is prohibiting.

Pension Design Reforms

The Task Force found it critical to validate assumptions before quantifying and projecting the impact of alternative plan designs, funding solutions or retirement benefit issues.

The Task Force recommends 7.0% as the overall long-term rate of investment return to be expected; however, to fully understand the cost of taking on investment risk, a 5.4% rate of return should be used when quantifying cost or affordability issues for the City.

Selecting an appropriate assumed investment return is the single most important assumption affecting the economics of planned retirement benefits. The Task Force recognized that reliance upon too high a rate can have a very significant impact on costs and funding requirements as investment returns compound over the working and retirement life of the employee. Pew estimated based upon the JPFPF's asset allocation and investment assumptions what probability could be assigned to long-term investment returns based upon plan assumptions. The 7.0% investment return assumption used by the JPFPF is a 50th percentile scenario. Thus, when assuming 7.0% returns, there is a 50% chance the investments will earn less and a 50% chance they will earn more (a flip of the coin in common parlance). Pew estimated a 5.4% rate of return would amount to a 75% confidence level, again based on the Plan's own assumptions. In other words, instead of a 50-50 probability of success, a 5.4% assumed rate of return would have a 75% chance of achievement. It was the Task Force's conclusion that this risk/reward ratio was much more suitable to rely upon. Of course any assumption is not a guarantee; the Task Force's intent was to lower the risk of falling short, but it cannot eliminate it.

In offering a defined benefit plan, the City agrees to take on an adjustable rate obligation. The City and the JPFPF expect the Fund's long-term returns to average 7.0%, but the City, not the JPFPF, bears the full risk if the returns are less. Using 5.4% as an assumed rate of return for cost estimates and for planning future contributions allows the City to lower the likelihood that investment returns may not perform as expected. It also causes the City to appreciate that there is a higher cost associated to attain lower investment risk.

The Task Force understands that the median expectation, or 7.0%, is a common practice used by public pensions for financial and regulatory reporting of actuarial results and accumulated obligations. The Task Force recommends that 7.0% should be retained as the actuarial assumption used to compute the ARC and for actuarial reporting by the JPFPF of its funded status.

There is also public investment commentary today that suggests investment returns of the last 30 years may overstate returns going forward. On the other hand, there also are public arguments that such concerns may be too pessimistic. The Task Force discussed whether an investment return lower than 5.4% should be considered. A lower return estimate would further assure obligations are properly funded; however, there also may be some immediate costs from too conservative a view. As earlier contribution requirements become more onerous, the City may struggle to fulfill other essential City needs; pressure to increase taxes may hamper economic growth or concentrate sacrifice today with surpluses realized by later generations, a generational inequity. The Task Force believes a 5.4% assumed rate of return for contribution purposes addresses a reasonable range of lower return outcomes, even though it does not assure the most severe scenarios would be addressed. It would also balance generational sacrifice more equitably.

<u>The Task Force recommends projecting mortality rates to consider future improvements</u>

As actuarially accepted mortality tables are updated, the trend has been to recognize longer life expectancy. Failing to project longer life expectancy understates the likely true cost of benefits promised and can increase the funding required when estimates are later revised. The

Task Force recommends that the most recent available standards always should be used in the actuarial analysis and that pension costs be estimated using projections of future mortality increases.

The Task Force used projections and data that reflect the latest accepted actuarial tables, RP2000, Scale AA. Other scales (BB) and methods (projecting generational improvements) have been proposed but are not yet accepted or adopted. The Task Force estimates that if longevity is later found to be 3 years greater, then it would increase normal cost by less than 10%. This sensitivity was not sufficient to alter the conclusions otherwise reached in the current tables.

<u>Expected future salary levels & other key assumptions were accepted by the Task Force</u>

Experience studies indicate assumed salary growth rates, assumed rates of employee withdrawal, expected retirement dates and impacts of the DROP program on overall cost are acceptable.

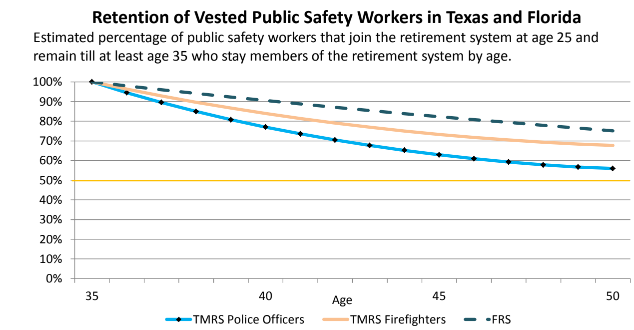
The Task Force recommends that a defined benefit plan be retained so long as proper governance and oversight is instituted and benefit levels can be sufficiently reformed.

The Task Force considered alternative benefit plan structures including a defined benefit (“DB”) plan, a defined contribution (“DC”) plan and hybrid approaches that combined aspects of both defined benefit and defined contribution. The Task Force noted that the City and employees could share investment risk in a DC plan, and that employees could have greater ownership and flexibility in such a structure as well. In adopting a DC plan, the City’s cash requirements and costs are much more predictable. Investment returns no longer impact the City’s annual funding. Mortality and other unknowns no longer have to be predicted. Employees can retain ownership of savings when changing employers and can select the style in which their savings will be invested. But while the City may benefit from greater control over its cost and funding requirements by adopting a DC plan, in moving from a DB plan the City also would abandon some areas where it may be inherently better suited to manage retirement risk for JSO and JFRD personnel.

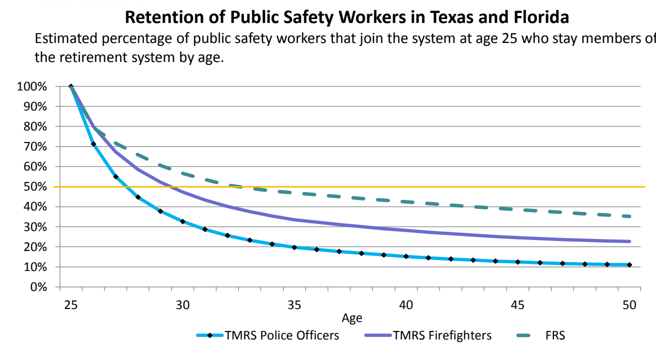
The investment expertise and oversight available for the City to apply to investment performance management brings resources more difficult for individuals to find, or as a practical matter, to find time to deploy in their private DC Plan account. Additionally, the ability and discipline to take risk and suffer through market swings may be greater at the collective resource level of the City than within the risk tolerance of any individual DC account. Employees may be more prone to lose an appropriate long-term focus in reaction to short-term fear or a desire to chase recent market returns.

Sheriff John Rutherford and Fire Chief Martin Senterfitt also saw a move to a DC plan as significantly adverse and likely to affect hiring and retention capabilities. They also found the characteristic of the current DB plan that defers some benefit accrual to later years in a career is helpful in supporting retention objectives of the JSO and JFRD.

Both the Sheriff and the Fire Chief expressed strong reservations about going to a DC plan or even considering a hybrid arrangement. They saw a DC plan as far less understood by employees. As a result, they testified that such a benefit would be perceived as less competitive with surrounding counties and jurisdictions in Florida that continue to offer DB plans. Sheriff Rutherford in particular was adamant that a hybrid structure similarly would adversely impact both hiring and retention. The charts below show competing jurisdictions' plans and retention rates comparing Texas (DC plan statewide), JPFPF and the Florida Retirement System.



Analysis based on new withdrawal assumptions for public safety workers in the Texas Municipal Retirement System and the Florida Retirement System. There is not enough information presented in either retirement system's documents to understand what drives these differences.



Analysis based on new withdrawal assumptions for public safety workers in the Texas Municipal Retirement System and the Florida Retirement System. There is not enough information presented in either retirement system's documents to understand what drives these differences.

Sheriff Rutherford also emphasized the need to consider issues that accompany higher employee turnover. Beyond the disruption that turnover brings to any organization, the Sheriff testified that for JSO officers the initial training costs are quite high, particularly in specialty units. Additionally, injury rates are highest for JSO officers in their first five years of employment.

<u>The Task Force found that certain factors additionally limit the practical ability of the City to fully abandon a DB structure.</u>

The City previously elected to opt out of Social Security and as a result the only guaranteed and predictable retirement annuity provided to JSO and JFRD employees arises from the City's retirement plan. This was primary in the Task Force's decision to rule out moving solely to a DC plan structure, but it did allow consideration of a hybrid combination of DC and DB plan elements.

The Task Force considered a Social Security-linked model. Because Social Security benefits are weighted to lower salaries and investments are in low-return, low risk instruments, moving to Social Security would be expected to raise costs for both the employee and the City beyond those reasonably necessary to provide a comparable benefit. Everyone would pay more and the employee would receive less. Additionally, the penalties for early retirement dates and the lack of control over future Social Security changes limited the desirability of such an approach. (Social Security does not allow non-disabled employees to begin receiving Social Security benefits prior to attainment of age 62). In regard to retirement age, the Sheriff noted that concern with the ability of officers to meet minimum desired levels of physicality typically

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begins at age 50, thus 55 and perhaps 60 was seen as the latest desired age for many JSO positions.

The Task Force also considered the possible movement of all employees to the Florida Retirement System ("FRS"). The Task Force understands such a move would require the approval of FRS along with the satisfaction of FRS's requirement that the City first fully fund the existing $1.7 billion unfunded liability that has accrued. Upon such full funding, the City could seek the FRS to consider a transfer all the fund's future pension payment and investment obligations to the FRS. Because FRS benefits also are offered to employees as retirement benefits in addition to Social Security, a move to FRS also may suggest the City would prospectively consider entering prospective employees in the Social Security system. The FRS alternative was not seen as a practical solution to consider further at this time.

<u>To better understand how a hybrid structure shares investment risk among the City and employees, the Task Force examined how costs would be impacted for a DB plan in comparison with a hybrid plan where returns expected at 7.0% actually earn only 5.4%. The Task Force found the savings to the City from sharing risks with employees though a hybrid structure at this range of investment returns were not sufficient to overcome other issues that would accompany the adoption of a hybrid plan structure.</u>

In the following series of tables, normal costs of alternative plan designs are compared. In order to be helpful to the reader, the Report includes some definitional concepts to reduce the need for the reader to go back and forth in the Report. For example, "normal costs" generally represent the greater retirement benefit over the employee's retirement period earned by the employee as a result of one more year of employment. The normal cost is expressed as a percentage of the annual base salary for that employee. Thus, retirement normal cost represents an annual employment cost in addition to salary and other benefits earned by the employee. "Chapter Funds" are the portion of the statewide insurance premium tax allocated to the JPFPF.

Various plan designs also are included in the following tables. These are as follows:

- "MSA" – The "Mediated Settlement Agreement", which was upon by the Mayor and the JPFPF, and joined in by the Unions. This agreement modified retirement benefit and contribution levels of new employees, affected contribution levels of existing employees but did not adjust the benefit levels earned by existing employees.

- "Existing Baseline Benefits" – The benefit levels as currently in force. They do not reflect a reduction for the MSA or for any of the other proposals.

- "Revised MSA" - The proposal announced by the Mayor at the Task Force meeting on January 21, 2014, and expanded the terms of the original MSA by proposing benefit levels and further contribution changes for existing employees.

- "Task Force Adjusted Revised MSA" - The final recommendations of the Task Force for current employees, which makes no changes to the benefit levels prospectively proposed for new employees in the original MSA. It adopts the changes for existing employees proposed by the Mayor in the Revised MSA, but makes further benefit changes for employees who have less than 10 years of service at the date of enactment to more closely align existing employees' benefits with those of new employees.

The Task Force first considered benefit design and compared a hybrid plan for new employees with the benefits they otherwise would have received in the MSA benefit structure. The DB element of the hybrid plan used the 5 year average final salary and an annual accrual rate of 1%, which is lower than the 2.5% proposed in the MSA. For the DC plan element, the employee would contribute 10%, as is proposed today in the MSA, and the City also would provide a 4% contribution or match in exchange for a lower DB benefit accrual.

Where investments are assumed to earn 7.0%, the hybrid plan would be nearly 3% more expensive at the subtotal funded by the City's operating budget plus "Chapter Funds" (11.9% vs. 9.1%). This higher cost to the City where 7.0% is earned is appropriate because the City also avoids risk for the DC portion of the benefit if lower investment returns occur. That risk for the DC element is borne by the employee.

Table 1		
Normal Costs at 7.0% Investment Return (*New Hire* employees)		
	MSA	Hybrid
City	5.1%	7.9%
Chapter Funds	4.0%	4.0%
Subtotal	9.1%	11.9%
Employee	9.9%	9.9%
Total	19.0%	21.8%

When a lower investment return of 5.4% is considered, the comparable MSA plan's cost is revealed as 18.4% as noted in Table 2 below. Thus, the lower investment return nearly doubles the expected cost funded by the City and Chapter Funds to provide the same retirement benefit. In the hybrid arrangement, the cost not borne by the employee rises only to 15.8%, thus an annual normal cost that is 3% lower than the MSA in this situation. Additionally, the cost of the Hybrid plan across the 7.0% and 5.4% return outcomes falls within a narrower band that varies from 11.9% to 15.8%, respectively, while the annual normal cost of a fully DB plan of the MSA for new employees would range from 9.1% to 18.4%. In turn, the portion of the investment risk shifted by the City to the employee in a hybrid plan would then be taken on by the employee, whose benefits earned would have both fixed and variable elements.

Table 2		
Normal Costs at 5.4% Investment Return (*New Hire* employees)		
	MSA	Hybrid
City	14.4%	11.8%
Chapter Funds	4.0%	4.0%
Subtotal	18.4%	15.8%
Employee	9.9%	9.9%
Total	28.3%	25.8%

Adopting a hybrid plan for new employees would make employer costs more predictable but it would require abandoning the MSA benefit structure previously jointly adopted by the agreement between the City and JPFPF. It also would trigger the employment concerns voiced by Sheriff Rutherford and Chief Senterfitt. As a result, the Task Force determined that pursuing a hybrid structure would not be worthy at this time, especially if overall negotiated outcomes still can be successfully achieved without litigation.

The reduced impact that a hybrid plan is expected to produce at lower investment returns is in part attributable as well to the significant reduction in normal costs achieved by the joint undertaking to design the MSA for new employees. If investment returns are 5.4% rather than 7.0%, the MSA still significantly raises normal costs to 18.4% in Table 2 above, but that result is significantly less than had benefit reforms not been achieved. In Table 3 below, the existing subtotal of City and Chapter Funds-funded normal costs for the baseline benefits would be 47.0%.

Table 3		
Existing Baseline Benefits - Normal Costs		
	7.0% Investment Return	5.4% Investment Return
City	25.1%	43.0%
Chapter Funds	4.0%	4.0%
Subtotal	29.1%	47.0%
Employee	6.8%	6.8%
Total	35.9%	53.8%

The Task Force recommends that the benefit levels proposed for new employees in the MSA be adopted.

The Civic Council earlier recommended benefits for new employees as proposed in the MSA should be lowered in order to reach a total normal cost of 20%, shared equally by employee contributions and by employer funding and the use of Chapter Funds when measured at an investment return of 7.0%. The Civic Council did not have 7.0% computations available and thus relied upon its internal estimates of what the MSA produced. Current actuarial estimates at 7.0% indicate the MSA will achieve a normal cost and a sharing of cost that should fall within targets recommended by the Civic Council (Table 1).

The hybrid plan provides a further data point for assessing reasonableness of the MSA, as well. The hybrid plan represents a benefit structure created afresh to be reasonable, cost efficient and a practical starting point to create a wholly new prospective retirement plan. The MSA remains slightly more expensive than the hybrid arrangement if returns fall short of investment targets, but the MSA also ultimately retains features preferred by the Sheriff and the Fire Chief for its greater attractiveness to employees and for addressing the competitive job pool in which the JSO and JFRD must compete.

In examining the competitive marketplace, the Task Force found it difficult to directly compare benefits across jurisdictions because of the multitude of assumptions and plan elements that vary. The table available to the Task Force showed that the MSA would provide a significant benefit level that appeared competitive with other Florida cities. The table is included in the Appendix. The Task Force found that the MSA provided a significant benefit level for comparison with alternatives, as its terms addressed age, retention and other operational considerations cited as important by Sheriff Rutherford and Chief Senterfitt, and it represented an outcome already agreed to in a collaboration of perspectives.

The Task Force recommends the prospective benefits for current employees be revised to adopt changes proposed in the revised MSA as well as additional benefit changes that will further align existing and new employee benefits.

The Task Force appreciates the work by the City and Mayor in developing the Revised MSA proposal, which makes a significant reduction in long-term cost by reducing the impact of Cost of Living Adjustments ("COLA") for prospective benefits to a rate comparable to that provided to new employees. As a result, COLAs for current employees for benefits earned after these recommendations go into effect would be tied to the inflation index used for Social Security but would be capped at a rate of 1.5%. The Task Force recommends the changes to employee contributions, to the DROP program and to the COLAs in the Revised MSA be adopted.

The Task Force also examined further changes to reform long-term costs and align benefit levels for prospective services more closely among current and new employees. The additional Task Force recommendations beyond the revised MSA, *to apply only to prospective benefits earned by current employees having less than ten years' service with the City,* are:

1) The determination of final average pay should use the final 60 months of salary, with the understanding that in no event would the amount so determined be less than what the amount equal to the final 24 months of pay as of the implementation date would have been.

2) COLAs should not be payable on benefits earned *prospectively* until a date that is three years following retirement, but in any event not earlier than age 55.

A comparison of the expected normal costs for the Revised MSA with these further Task Force changes along with the normal costs for the other benefit arrangements are as noted for each assumed rate of return in Tables 4 and 5, which follow on the next page below.

Table 4								
Estimated Normal Costs of Alternative Benefit Proposals at 7.0% Investment Return (50% confidence)								
	Existing Baseline	Task Force Adjusted Revised MSA		Revised MSA	Stacked Hybrid Plan			
	All employees	Current employees		New employees	DB element	DC element	Total
Funding Source		< 10 Yrs	> 10 Yrs				
City	25.1%	12.0%	14.1%	5.1%	3.9%	4.0%	7.9%
Chapter Funds	4.0%	4.0%	4.0%	4.0%	4.0%		4.0%
Subtotal	29.1%	16.0%	18.1%	9.1%	7.9%	4.0%	11.9%
Employee	6.8%	9.7%	9.7%	9.9%		9.9%	9.9%
Total	35.9%	25.7%	27.8%	19.0%	7.9%	13.9%	21.8%

Table 5							
Estimated Normal Costs of Alternative Benefit Proposals at 5.4% Investment Return (75% confidence)							
	Existing Baseline	Task Force Adjusted Revised MSA		Revised MSA	Stacked Hybrid Plan		
	All employees	Current employees		New employees	DB element	DC element	Total
Funding Source		< 10 Yrs	> 10 Yrs				
City	43.0%	24.0%	27.0%	14.4%	7.8%	4.0%	11.8%
Chapter Funds	4.0%	4.0%	4.0%	4.0%	4.0%		4.0%
Subtotal	47.0%	28.0%	31.0%	18.4%	11.8%	4.0%	15.8%
Employee	6.8%	9.7%	9.7%	9.9%		9.9%	9.9%
Total	53.8%	37.7%	40.7%	28.3%	11.8%	13.9%	25.7%

Note: The format of the foregoing tables was requested by the Task Force and the data presented was estimated by Milliman to reflect the estimated incremental cost impact of various further changes by the Task Force beyond those directly modeled by Milliman or the City's actuary. Confidence levels are not the work of Milliman. Additionally, these tables may not be appropriate for other purposes and Milliman assumes no liability for use of this data by other parties who may receive this report or information. Milliman further recommends that third parties be aided by their own actuarial analysis in reviewing this information.

The Task Force noted that the annual normal cost of recommended prospective benefits for current employees in the Revised MSA, even including the further adjustments recommended by the Task Force, will still remain higher than the normal cost for future services of new employees for reasons other than age of the populations. As noted in Table 5, the prospective cost for current employees funded by the City and Chapter Funds, depending upon existing years of service, ranges from 28.0% to 31.0%. This benefit level still exceeds the comparable cost for new employees of 18.4%. Such an outcome is nevertheless recommended by the Task Force and reflects its expectation that all Task Force recommendations be accepted as a package. Thus, these higher benefit levels may provide a possible compromise solution to what ultimately must be a collaboratively agreed upon process of shared sacrifice between the City, its taxpayers and current JSO and JFRD personnel.

To summarize the foregoing, the Task Force recommends the following pension design for new and current employees:

Recommended Changes for New Employees

New employees would enter into a final average salary defined benefit pension plan, based on the following parameters which were agreed on in the Mediated Settlement Agreement.

Normal Retirement: Age 62 or 30 years of service
Early Retirement**:** 25 years of service
Vesting Eligibility: 10 years of service
Benefit Multiplier Per Year of Service:

- 2.5 percent with 30 or more years of service
- Between 25 and 30 years of service: 2.5 percent, reduced by an early retirement factor
- 2 percent with fewer than 25 years of service

Final Average Salary: Last 5 years
Employee Contribution: 10 percent of pay
COLA:

- Begins after three years in retirement
- Indexed to the Consumer Price Index
- Cap of 1.5 percent

Other Notes:

- DROP is replaced with a Back-DROP plan that does not include a guaranteed return.
- Annual benefits are capped at $100,000 or 75% of final average salary.

Recommended Changes for Current Employees

Current employees would have the following changes to their benefits and employee contributions based on the Task Force's recommendations. Police officers and firefighters who are already retired and their beneficiaries would experience no changes.

- Increasing employee contributions—Employee contributions should immediately increase from 7 to 8 percent of pay and then subsequently increase to 10 percent following salary increases to make up for recent pay cuts.

- Changing the interest guarantee in the DROP program—For current workers not eligible to enter the DROP program at the time of implementation, DROP accounts will credit employees with the actual returns generated by the JPFPF, with a floor of 0 percent and a ceiling of 10 percent.

- COLAs applied to benefits for current employees that have not yet been earned. Benefits based on service through the date of implementation will continue at their present rate (3 percent annually in retirement, compounded), but benefits based on service following the date of implementation will receive a COLA benefit rate equal to the lower of CPI or 1.5 percent.

In addition, the Task Force recommends that with respect to current employees with less than ten years' service to the City, to be applied *only* to prospective benefits for service after the implementation date:

1) The determination of final average pay should use the final 60 months of salary, with the understanding that in no event would the amount so determined be less than what the amount equal to the final 24 months of pay as of the implementation date would have been.

2) COLAs should not be payable on benefits earned *prospectively* until a date that is three years following retirement, but in any event not earlier than age 55.

Recommended Funding Solutions for the Payment of the UAAL

The Task Force recommends that the City annually contribute the greater of $200 million or the ARC until the Plan becomes 80% funded, which is expected approximately 13 years after increased funding begins. This contribution level is intended to contribute more than the projected ARC amounts over that time period and to identify a contribution level that would be stable should investment returns fall to as low as 5.4%. This $200 million contribution amount is in addition to continuing a contribution of premium taxes, also known as chapter funds as agreed in the MSA, including the one-time $20 million payment in the first year following implementation and the payments for each year as contemplated by the MSA.

The Task Force recommends a level payment funding plan to address the UAAL and new benefits.

Without a level funding approach, the existing funding forecasts require the City to steadily increase contributions each year. Contributions currently at $148 million will in the future continue to rise ultimately reaching over $400 million by FY 2036 even if the assumed 7.0% rate of return can be achieved over the long-term.

The Task Force determined a key concern in evaluating pension benefits offered employees and retirement plan structures was assuring that any final recommendations must be affordable and sustainable when considered with the need to address existing underfunding as well. In this regard, the Task Force requested an atypical analysis to examine funding costs, which was to consider what level payment would be required to fully fund both the existing underfunded obligation as well as all new prospective benefits that would be earned over that recovery period. By examining level funding, affordability became clearer. Inherent in this approach was a decision by the Task Force to not assume inflation would solve affordability issues for the City. In that regard, budget revenues available to meet pension needs were not assumed to perpetually grow in availability by an amount equal to or even because of an inflation projection. Simply put, the Task Force asked what fixed dollar amount must be paid over the full funding period for targeted benefit arrangements and the UAAL to be addressed?

The Task Force recommends the adoption of an actuarial method that amortizes gains and losses over a closed 30-year period based on separate annual bases. For the current unfunded liability, this will have the result of extending the period over which the unfunded liability must be paid off and will allow level funding to be adopted at a lesser contribution level than had a shorter amortization been used. This closed 30-year period is still consistent with sound actuarial practice.

The Task Force considered the existing actuarial practice that requires gains above and losses below the assumed investment rate of return to be fully addressed in contributions by no later than 2036. An alternative approach, as is recommended, would take each year's new gains and losses as a layer, and amortize each layer over a future 30-year period.

There are sound reasons to consider either approach. One argument in favor of the City's existing system is it requires more immediate and significant contributions to make up existing short-falls since the period to do so is shorter. But as a methodology going forward, it also becomes less feasible as each year's variance gets amortized on an increasingly shorter period remaining until 2036. That eventually becomes unworkable. The actuaries noted an approach over 30 years would extend the required period to address the unfunded liability to 2042 in lieu of 2036, but that was both a valid and accepted practice.

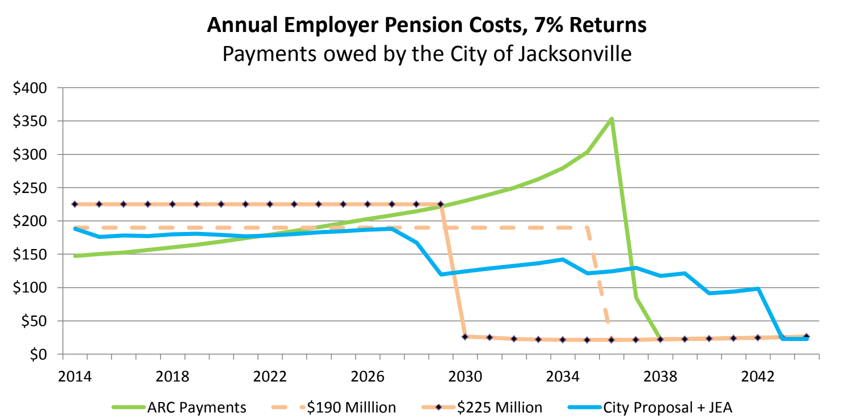
The Task Force determined that since it would be recommending contributions at levels set in consideration of only 5.4% investment returns, and since it would be recommending level payments that would accelerate funding significantly beyond minimum amounts, then adopting the longer amortization methodology would not only be a more suitable method, but it also would contribute to a prudently balanced outcome overall.

The Task Force found that a large initial contribution could provide value through ongoing investment earnings but it did not significantly lower the level funding amount that would be required.

The Task Force examined modeling of one-time up-front payments and found that such contributions reduce level payments by only a small percentage thus sizeable level payments will likely be required. With a 7% investment return, an $800 million initial contribution reduced annual level contributions required by $70 million, which provides some sense of scale. With a 5.4% investment return assumption, a greater upfront payment would be required to have the same annual reduction impact. The real value of such initial payments is creating significant value through the compounding of ongoing investment return over time.

In evaluating level contribution requirements, the investment return assumption again remains extremely significant.

Pew examined what the City's contributions would be prospectively both to pay new benefits as they are earned and to pay down the existing UAAL. Pew did this while taking into account the existing actuarial assumptions, where all gains and losses are amortized by 2036 (not an ongoing 30-year amortization approach). In this scenario, investments are assumed to 7.0%, and a contribution level of approximately $190 million a year would be required:



Source: The Terry Group, 2014
City Proposal figures were provided by Milliman

Millions of Dollars,
Not Adjusted for Inflation

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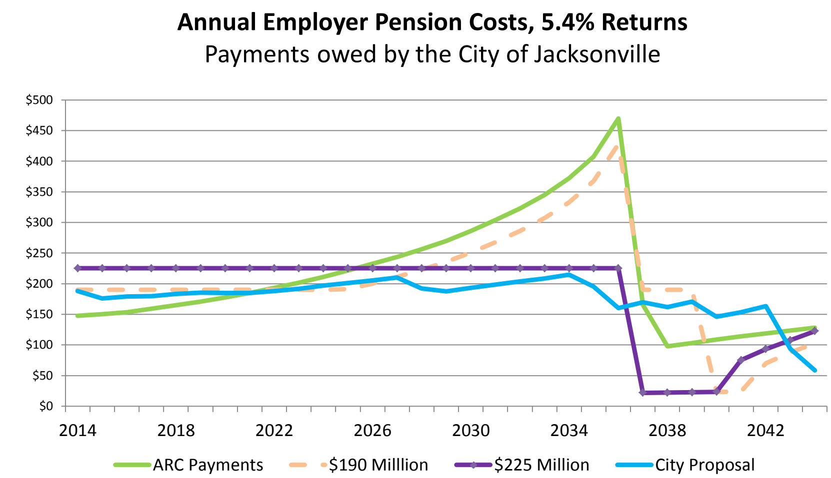
Pew conducted another contribution scenario where investments are assumed to be a lower 5.4%. At this assumed rate of return, the level contribution of $190 million is not sufficient and climbs over time to exceed $400 million at its highest level.



Source: The Terry Group, 2014
City Proposal figures were provided by Milliman

Millions of Dollars,
Not Adjusted for Inflation

The Task Force recommends $200 million as the level payment to be targeted

The Task Force then examined funding scenarios that included not only addressing the UAAL and new benefits assuming that the revised MSA for existing employees and the MSA for new employees were prospectively implemented, but that also allowed the annual 30-year method of amortization to be used. Thus, gains and losses are allowed to be fully recovered as late as 2042. If only 5.4% were assumed to be earned, then about $200 million a year would be sufficient as a level payment amount even at this lower investment return assumption, and the JPFPF would reach 80% funding by approximately 2035 with gradual reductions in payment amounts thereafter.

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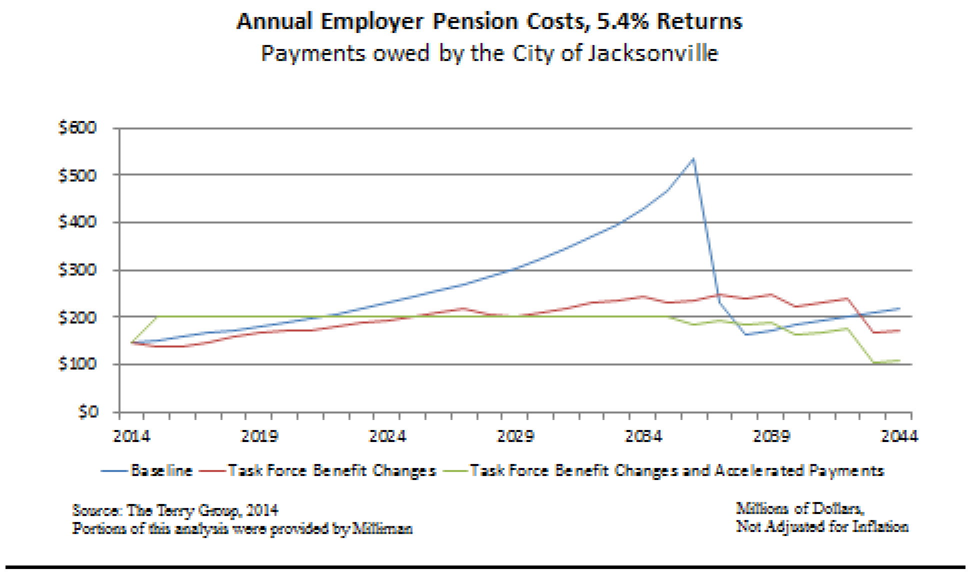
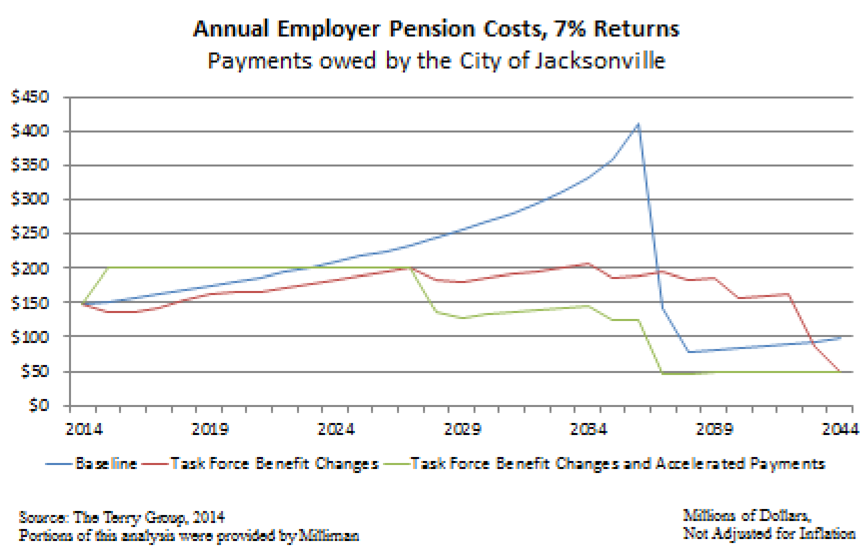


In the event that 7.0% investment returns are consistently earned, then, according to the Pew chart below, the UAAL and the new retirement service obligations would be 80% funded by 2027, or within 13 years after initiating level contributions of $200 million.



The Task Force recognizes that the use of $200 million requires funding levels in excess of the approximately $148 million that is being currently funded through the City's operating budget. This higher level of contribution is established because of the Task Force's goal of reasonably avoiding further funding surprises from volatile investment returns and to responsibly move forward to address the existing UAAL. To some extent this strategy also is dependent upon investment returns in the next several years remaining adequate so that efforts to establish accelerated funding balances are not offset by larger declines in invested plan assets. It also results in savings approximating $1 billion in gross undiscounted amounts, as shown in the Pew chart below. The first column for total cost reflects the cumulative dollar amounts of all contributions forecast in the chart for the period 2014 through 2044. Not all scenarios are equivalent as they leave the City in alternative states of UAAL, but they present a sense of impact on a gross dollar basis. The cost impact differs at 7.0% or 5.4% because the level of return earned by the investments impacts the expected contributions. The columns that are inflation-adjusted reflect the incremental impact of the changes but also assume contributions have a lesser value just due to the expectation of paying in future inflated dollars.

	Projected Contributions from 2014 through 2044			
7% Actual Returns	*Current Policy Baseline*	*Task Force Recommended Benefit Changes*	*Task Force Recommended Accelerated Payments*	*Recommended Benefit Changes and Accelerated Payments*
Nominal Dollars				
Projected Contributions	**$6,117**	**$5,222**	**$5,737**	**$4,346**
Savings	**$0**	**$896**	**$381**	**$1,772**
Inflation Adjusted (assuming 2.5% inflation)				
Projected Contributions	**$4,348**	**$3,693**	**$4,159**	**$3,324**
Savings	**$0**	**$655**	**$189**	**$1,024**
5.4% Actual Returns	*Current Policy Baseline*	*Task Force Recommended Benefit Changes*	*Task Force Recommended Accelerated Payments*	*Recommended Benefit Changes and Accelerated Payments*
Nominal Dollars				
Projected Contributions	**$7,819**	**$6,217**	**$7,660**	**$4,346**
Savings	**$0**	**$1,601**	**$159**	**$3,473**
Inflation Adjusted (assuming 2.5% inflation)				
Projected Contributions	**$5,353**	**$4,269**	**$5,285**	**$4,170**
Savings	**$0**	**$1,084**	**$68**	**$1,183**

Recommended benefit changes do not include the additional reductions towards workers with less than 10 years of services as those changes were not modeled. Actual savings under the full recommendations would thus be greater.

Source: The Terry Group, 2014
Portions of this analysis were provided by Milliman

$ in Millions of Dollars

<u>Annual funding at the $200 million level should continue until the JPFPF is at least 80% funded and monitored and enforced as part of the 2014 Agreement recommended above.</u>

Why 80%? The JPFPF should target reaching 100% funding. However, this 80% funded milestone is an appropriate time to determine if the accelerated contribution levels established using 5.4% investment return assumptions need to continue, or whether the plan asset levels might be sufficient to return to contributions to levels more consistent with simply making the actuarially required contribution, likely determined using a 7.0% assumption. The City too, while needing to aggressively address current underfunding, does not want to continue making contributions greater than the ARC for longer than appropriate as it both risks reaching an overfunded status and it continues to set a priority for pension sacrifice that might more appropriately be funded over a longer period. The Task Force, in working with Pew and the actuaries determined that 80% was an appropriate threshold to pause and reestablish a prudent funding plan from that point forward with the understanding that the JPFPF will need to reach a 100% funded ratio in a reasonable time frame.

The funding status for actuarial purposes is measured using actuarial asset values, which can vary from actual fair market values because of the smoothing of gains and losses over a longer time period for actuarial purposes. It is the Task Force's intent that the 80% milestone would be measured based on the JPFPF's smoothing formula that the Task Force understands is permitted under Florida law: smoothed by averaging the mark-to-market returns over the preceding 5 years with a minimum floor equal to 80% of market value, and a ceiling equal to 120% of market value, and using the 7% actuarial assumption for the return on investments, unless that assumed rate of return is changed by agreement of both the City and the JPFPF as a result of sound actuarial practice or if required by law. It is also the Task Force's expectation that such liabilities would incorporate recent plan experience updates and should be challenged to assure the estimates also consider the latest available information on mortality and other assumptions.

The Task Force recognizes too that fair market values could result from a boom or bubble that on a long-term basis could be too optimistic. It is for this reason that gains are brought in more slowly for actuarial reporting. Certainly too, once an 80% funding status is reached, prudent funding decisions will need to be made based upon a consideration of all the facts and circumstances at that time. Once an 80% funded status is achieved, required ARC contributions will fall below the $148 million that the current ARC requires, but if the JPFPF funding ratio again drops below 80%, the JPFPF and City policymakers must not delay in restoring that ratio to that level. The Task Force recommends that contributions in excess of the ARC must again be made as necessary to assure that a minimum funding ratio of at least 80% is quickly achieved at all dates in the future as well as today.

Funding Sources

In considering how to fund the contributions to accelerate the payoff of the substantial UAAL, the Task Force considered several options, including (i) pension obligation bonds, (ii) contribution to the JPFPF of "lazy" real estate assets of the City, (iii) further cuts to the City's operating budget, (iv) a proposal of the Mayor to utilize savings suggested may be available in the JEA budget, particularly if JEA employees were transferred out of the City's General Employees' Pension Fund into a new retirement plan to be negotiated by JEA, (v) increasing ad valorem taxes, and (vi) utilizing a discretionary sales surtax that is available for fire rescue services and facilities.

The Task Force considered the use of pension obligation bonds whereby the City would borrow and then transfer the proceeds to the JPFPF. The benefit of such a transaction arises from the arbitrage that would be gained by the expected ability to borrow at fixed rates much lower than the long-term investment return that would be earned. Proponents also saw pension bonds as a lower cost replacement for a debt-like unfunded obligation that currently grows each year by the difference in investment returns actually realized and the assumed investment return of 7.0%. They suggested that since a contribution would be made in any event, the economic question was whether that contribution should be accelerated by incurring interest. There were many public comments to the Task Force against the added risk of a debt-funded approach. There was concern that unfunded liabilities initially extinguished by debt proceeds could return if asset values declined leaving the City with even greater debt than if the additional proceeds had not been borrowed. Concern was also expressed that such an approach could concentrate the investment of the funds over too short a time period, resulting in excess reliance upon the market's value within a relatively narrow period. Additionally, since the time when the pension bond recommendation was first considered, many of the economic drivers supporting confidence in that approach have waned. Some of the lowest interest rates in decades have now begun to move up and the City's current borrowing cost is estimated to be in excess of 5% for pension bonds, which are taxable debt instruments. Additionally, the appreciation of the equity market in 2013 has driven equity values to record highs. Given all these considerations, the Task Force rejected using pension bonds as a funding solution at this time.

The Task Force does not believe that transferring City real estate to the JPFPF to reduce the UAAL would work. In the first place, the JPFPF would be taking on substantial development risk without having a sufficient track record in successfully developing real estate, especially complex projects. Further, it is not clear to the Task Force that conveying properties on the basis of ad valorem tax assessment values (as proposed by the JPFPF to the City Council) would realize for the City the actual value of the properties transferred. Next, making a substantial real estate transfer large enough to shift the unfunded liability would leave the JPFPF with an insufficiently diversified asset base with excessive exposure to the Jacksonville real estate market. Finally, the City's "Lazy Asset Survey", which is still underway, suggests that there is not enough surplus real property to make a substantial reduction in the UAAL. Even if there were $100 million in surplus real property, it would only be a one-time reduction that would only reduce a small fraction of the UAAL. If the development risk led to deterioration in value, the one-time reduction would be reversed. The Task Force suggests that if there are "lazy assets" that they be disposed of using a "R.F.P." process where experienced real estate developers and investors could be invited to bid in a competitive process for the asset(s). In that way the price could be maximized and the risks of development would be borne by the developers and not the City. The cash proceeds of sale could be used to pay down the UAAL in addition to payments by the City from the operating budget. One additional note raised by MAEVA was that if the City contributed real estate assets to the JPFPF, the JPFPF and ultimately the City would be adding to the ordinary investment risk the expectation that Jacksonville as a market would not have a down turn. The economic well-being of the City itself, and its ability to attract businesses and growth, would be a factor in whether the particular real estate performed or not. To the extent the City underperformed, so would the JPFPF. Since the City ultimately bears the economic risk of the UAAL, a downturn in Jacksonville's economy would "double down" on the bet on surplus real estate if conveyed to the JPFPF. In other words, *local* real estate investments are never a good diversification of a public pension fund's assets.

The Mayor presented to the Task Force a proposal to work with the JEA to achieve approximately $40 million per year in pension and expense savings and have the JEA contribute such savings to the City for use in paying down the UAAL over a 14-year period. The proposal has received wide publicity. While the Mayor insists that there would be no need for the JEA to increase its rates, and would not add significant burden to the JEA's finances, the JEA board chair, Mike Hightower, and JEA CEO Paul McElroy testified to the Task Force that such may not be the case. The proposed pension savings would take decades to be fully realized and the JEA would need to find a way to make the annual payments in the interim. It appears that the Mayor and the JEA have not finalized and agreed upon the proposal. Without an agreed upon proposal, the Task Force believes that it is not a present solution as a funding source for the reduction of the UAAL. It is the Task Force's belief that if the City and the JEA ultimately reach an agreement in the future, the City Council can then consider the proposal as a potential funding source for the City's needs, including pension payments. At present it is too early to base substantive recommendations on the JEA proposal.

The Task Force considered recommending that the City Council increase the franchise fee payable to the City by the JEA for the use of certain rights of way from the present 3% to 6%, which would produce an additional $40 million dollars in annual revenue to the City. However there are certain legal issues involving the franchise fee which would make such a recommendation problematic. Moreover, such an increase would be borne by JEA customers only and would not be as broad based as either an ad valorem tax increase or an increase in the sales tax, discussed below.

The Task Force evaluated the possibility of recommending that the City Council increased the ad valorem millage rate to raise the additional $50 million the Task Force believes is necessary to accelerate the payment of the UAAL. The City has sufficient taxing capacity, and the millage rate remains relatively low when compared to most larger-population counties in Florida and in the northeast Florida area.

However, the Task Force feels that increasing the ad valorem millage rate is not as good a solution as taking advantage of an available discretionary sales tax. A sales tax would be broader based when compared to the property tax. Also, it would be paid not only by Jacksonville residents but residents in surrounding counties who purchase goods and services in Jacksonville, and by tourists visiting the City.

The Task Force also feels that it is very important to assure as best we can as a community that once the revenue source is identified and utilized, that the City Council and Mayor continue to bind that revenue source until the UAAL is reduced as recommended by the Task Force (that is, until the funding ratio of the JPFPF reaches at least 80%). If policymakers are permitted to back away from a credible and sustainable funding plan in years to come, the UAAL funding ratio will continue to remain low, and the City will continue to be responsible for a high UAAL. The Task Force feels that the sales surtax can be levied for a specified period and the City Council would find it hard to repeal once the community has approved it. Needless to say, community will needs to be brought to bear on the Mayor and Council to make sure they stay committed to the course of restoring the JPFPF's financial strength so that police and fire employees are assured that their pensions will be there when needed and so that taxpayers don't face the same problem in years to come.

For the foregoing reasons the Task Force recommends that the City use the discretionary sales tax surtax available to counties under F.S. 212.055(8) (the "Surtax Statute"). Under the Surtax statute the City is empowered to enact up to an additional one per cent ($0.01 per $1.00) sales surtax. It is estimated that the full one percent surtax would generate an additional $136 million per year for the City. The revenues generated by the surtax must be used for fire rescue services and facilities, but those revenues would free up an equivalent amount of money from the City's ad valorem tax budget which could be used to fund the City's pension obligations. It is noteworthy that the Surtax Statute specifically requires a reduction of the City ad valorem tax budget by an amount equal to the annual revenues received from the surtax, and that the imposition of the surtax must be approved by vote of the citizens in a referendum to be placed on the ballot by the City Council. There are also requirements for approval by other communities participating with the City in interlocal agreements for fire and rescue services, and sharing of the revenues with them.

The Task Force observes that a one half of one percent (or half-cent per dollar) surtax would raise approximately $68 million dollars, which is $18 million more than the additional $50 million recommended by the Task Force for accelerating the payment of the UAAL. It has been presented to the Task Force that the General Employees' Pension Plan also has a substantial UAAL, so the additional $18 million could be used to accelerate the reduction of that deficit.

Given the requirements of the Surtax Statute, the Task Force recommends that in the budget process for the 2014-15 budget year, which begins on October 1, 2014, the City Council increase the millage rate to generate additional revenue in the approximate amount of $68 million (the amount estimated to be produced by a half-cent surtax). With that legislation the City Council should also adopt an ordinance levying a one-half percent (half-cent per dollar) surtax under the Surtax Statute, and place the levy on the ballot in November, 2014, for consideration by the voters. The surtax should have an expiration date of at least 14 years, but to provide some margin of error, the expiration date should probably be 20 years. In effect, the voters would have a choice as to whether they preferred the additional revenue to be generated by the levy of the sales surtax or by the increase in the ad valorem millage rate. If they vote in favor of the surtax levy, it would begin January 1, 2015, and be added to the 2015-16 budget once the 2015 surtax revenues have been received and apportioned. (<u>Note</u>: this is one year later that the 2014-15 budget year for which the ad valorem millage had been increased.) In the 2015-16 budget the ad valorem tax portion of the budget would be required by the Surtax Statute to be reduced by the amount of 2015 surtax received. There would be one year of overlap in which both taxes would be in effect, but that one year would be needed to pay down the first installment of the accelerated payments of UAAL, and ultimately at the back end would reverse the overlap.

On the other hand, if the voters rejected the surtax, the ad valorem millage increase would continue and be the source of the payments for accelerated reduction of the UAAL. Both cases assume that the community would bring its will to bear on the City Council and Mayor to continue the payment of the UAAL. The enforcement mechanism in the 2014 Agreement would be a good tool to cause that to happen, because in the 2014 Agreement the City should agree to the funding levels recommended by the Task Force, and Judge Schlesinger could see to it that the City lives up to its word.

CONCLUSION

The changes contemplated by the Task Force's Recommendations would require approximately $50 million of additional revenue from the City in the short-term; but over the next thirty years, the changes are estimated to save in excess of $1.7 billion. Part of this comes from reducing the benefits offered to new employees, part comes from changes to current employee benefits, and the remainder comes from paying down the UAAL faster. If the proposed changes are implemented, the JPFPF is expected to reach an 80% funded ratio in 2028, rather than in 2033. Achieving that result at the earlier date will result in substantial savings to the City, and without doing so a spike in the required pension contributions required of the City will seriously impact every aspect of the City's finances. Current retirees will not have any changes to their existing benefits, new workers will realize the plan previously agreed upon between the City and the JPFPF in the MSA, and prospective benefits earned by current employees will have changes directionally closer though still more remunerative than those of new employees and also reflective of changes made to current employees in the Florida Retirement System.

The Task Force urges that its Recommendations be considered as a complete package and not be jeopardized by piecemeal negotiation. The Report as a whole has been adopted by unanimous vote of Task Force members, although a few individual points were not unanimous. The entire Task Force believes that the willingness of the City to provide additional funds to the JPFPF should be conditioned upon the willingness of the JPFPF and its members to share the burden of pension relief going forward. The taxpayers should not be expected to make significant sacrifices if police and fire personnel are not willing to do so.

As stated in the Report, leadership is crucial for implementing appropriate solutions. The Mayor, City Council President and members of the City Council, the JPFPF Administrator and its Trustees, and community leaders from its business, civic, nonprofit and civic sectors all have an important role to play. Even religious leaders are crucial for the solution of this problem, for it ultimately is a moral issue. What is our community life going to be like for the next generation? We must be able to assure a sound financial foundation for our citizens so that they may live in this community with their basic needs met, and with the ability to enjoy the "pursuit of happiness" that our country's constitutional documents enshrine.

The Task Force is grateful to all those persons and organizations that have provided such exceptional expertise and resources to the Task Force in this effort. The Task Force also expresses its gratitude in advance to the residents of the City of Jacksonville who will be asked to make pension reform possible. The members of the Task Force thank the citizens of Jacksonville for permitting them to serve on their behalf.

Respectfully submitted,

RETIREMENT REFORM TASK FORCE

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*Dr. Aikens tragically died on December 5, 2013, immediately following a Task Force meeting. His contributions to the work of the Task Force were substantial, and the Task Force grieves for his family and for the Jacksonville community in the loss of this fine man.

**Greg Anderson, as a member of the City Council, fully participated in the work of the Task Force, but abstained from voting on any proposal affecting or related to pension design. His vote on the Report as a whole does not include his taking of any position on any aspect of pension design.