Florida Pension Plan Closure: 2021 Legislative Session Issue Redux

FREA Conference, 5.26.21

Ash Williams, Executive Director and CIO, FL SBA

For reference, here is a link to the March 9, 2021 SBA Trustees meeting in which Governor DeSantis asks for background and my perspective on the Senate proposal to close the FL Pension Plan to new members https://thefloridachannel.org/videos/3-9-21-florida-cabinet-meeting/. For tomorrow's discussion, I would like to revisit the same points made as they expose the inadequacies of the narrative offered by Senate pension closure advocates. Following is an outline of these points; I will then hand off to Dan for his framing of the DB vs. DC issue nationally and the comparison of FRS to MI SERS. As usual, I will open with investment performance (updated to tonight's close).

1. **Investment performance update**
    a. **As of the market close 5.24.21, FYTD up 26.2% gross, 82 basis points ahead of target.**
    b. **The FRS Trust Fund balance is at a record $196 billion, up $35.3 billion from July 1, 2020, net of benefit payments of approximately $600 million monthly.**
2. **For the first time in over five years, there was a serious legislative effort to close the FRS Pension (DB) Plan. The effort originated in the FL Senate, passing two committees and the full Senate on largely partisan votes. It did not have a House companion bill and was never taken up by the House after arriving in Senate messages roughly two and a half weeks before the session ended. Some are saying that the Senate President wants to bring this up again in the legislative session commencing January, 2022. How have advocates framed this issue and what are relevant facts? Let's break it down into assertions and facts:**
    a. ***The structure of the Pension Plan is flawed, unsustainable and subject to sudden failure, posing a serious threat to Florida's solvency.***
        i. **The structure of the pension plan has been in place since the genesis of the FRS is the early 1970s. At inception the FRS had a woefully inadequate funding ratio of around 40%. The combination of reasonable benefits, responsible funding and prudent investing brought the plan to full funding in the late 1990s and to overfunding, to a ratio of 118% at peak. The legislature decided this was too well funded, provided a decade of contribution relief for FRS member employers, saving them $6 billion and lowering the FRS funded ratio from 118% to 108% by 2007. The Great Financial Crisis then reduced asset values, driving the funding ratio down to 87%, creating the first unfunded liability in a number of years. A combination of partial underfunding (approx. $3 billion in the GFC's aftermath and unrealistic actuarial assumptions and practices subsequently has hindered the recovery of the funding ratio, despite the 2011 benefit reforms and solid investment performance. Conclusion: The FRS structure is not flawed; history clearly shows that underfunding is what causes underfunding.**

b. ***Paying off the pension plan's unfunded liability is diverting dollars from other public priorities; we need to close the pension plan to eliminate the UAL and free up those dollars for education, public safety, environmental, health and other priorities.***
    i. **Changing the plan structure has no effect on existing unfunded liability; UAL is an obligation that must be paid.**

c. ***The cost of the pension plan is just too high; Florida should follow the corporate example and offer only a defined contribution plan.***
    i. **Moody's Investor Service, a major credit rating agency tracks pension data and compares each state's Net Pension Liability (NPL) with state debt, state GDP, state GDP per capita and state household wealth. On all of these metrics, Florida's NPL is among the bottom 2 or 3 states. In addition, Florida is said to have the lowest number of state employees per capita in the US and by extension, the lowest per capita cost of state employees.**
    ii. **Florida's employer and employee contributions to the pension plan are 30% below the national average. contributions are 50%**
    iii. **Currently, over 60% of the cost of the pension plan is paid by investment earnings, not employers/taxpayers or employees. Closing the plan to new entrants will eventually limit our ability to invest in illiquid and/or volatile strategies, hampering out ability to generate returns.**
    iv. **The legislation that passed the Senate would have allowed Special Risk class employees ongoing pension fund access but excluded all other classes of employees. The actuarial study projected annual savings of $7 million in the first year and $230 million 30 years in the future (with no discounting for inflation). These numbers mean a cost reduction of 2 basis points in year one and 33 basis points in year 30.**

d. **Indications are that the Senate may bring this issue back next year. It would be helpful for the factual history of the FRS to part of the dialog. It would also be helpful to understand the national perspective on the DB vs. DC debate, the ramifications for beneficiaries and whether any other states have had experiences that would be instructive.**