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IN GOVERNMENT FINANCE



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2020 Winner for Creative Solution to a Common Challenge



CITY OF PHILADELPHIA, PENNSYLVANIA PHILADELPHIA'S ROAD TO PENSION RECOVERY

In 2018, the City of Philadelphia, Pennsylvania, adopted a comprehensive plan to improve the long-term health of its pension system by paying down its unfunded liability more quickly while also reducing the rate at which future liabilities will grow. Its funding ratio has historically been below average, compared to peer cities, and the funded level dropped 10 points from 2008 to 2009, to 45%. When reform discussions began in 2016, the fund was still only 44.8% funded, with just \$4.9 billion available to cover \$11 billion in liabilities. To combat the underfunding, the city employed a bilateral approach, focusing on reforms that foster effective decision making and fiscal discipline, and wide-ranging partnerships that engage elected officials, union officials, and pension board members. The system is expected to be fully funded by 2033.

The city's plan will improve the pension system's funded level to 80% by 2029 and 100% by 2033 by dedicating additional assets to the fund, reducing the rate at which future liabilities grow, and reducing the plan's risk profile.

Additional funding comes from dedicated city sales tax revenue, additional employee contributions negotiated through collective bargaining, and payment of the full actuarially required contribution every year.

To reduce the rate at which future liabilities grow, the city administration and union negotiators agreed to create a new mandatory "stacked hybrid" plan for new, non-uniformed hires. The new plan combined elements of a traditional defined benefit plan, which is capped at \$65,000, and a 401(k) plan, in which participation is voluntary. By FY29, the flat cap is projected to reduce future plan liabilities by more than \$100 million.

To reduce the plan's risk profile, the pension board has voted to make some changes in the way the assets are managed. They gradually reduced the assumed rate of return, which affects investment decisions and the amount of the city's contribution, from an all-time high of 9% ten years ago to 7.55%. They also shifted assets into passive investments with lower management fees and transferred assets from expensive and often volatile hedge funds into more stable real estate funds.