

# SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based only on the provisions contained in the legislation as of the latest date listed below.)

**BILL:** CS/SB 1858

**SPONSOR:** Governmental Oversight and Productivity Committee and Senator Silver

**SUBJECT:** The Florida Retirement System

**DATE:** March 23, 1999                      **REVISED:** \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Lombardi</u>	<u>Wilson</u>	<u>GO</u>	<u>Favorable/CS</u>
2.	_____	_____	<u>FP</u>	_____
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____

**I. Summary:**

The bill creates an excess benefit plan referred to as the “Preservation of Benefit Plan.” This plan allows the Division of Retirement to pay any future retirement benefits that exceed Federal limits through a second qualified benefit plan pursuant to s. 415.(m), Internal Revenue Code.

This law takes effect July 1, 1999.

This bill amends section 121.091, Florida Statutes, (1998 Supp.) and creates s. 121.1001, F.S.

**II. Present Situation:**

The Florida Retirement System (FRS) was established December 1, 1970 by consolidating the Teachers’ Retirement System, the State and County Officers and Employees’ Retirement System, and the Highway Patrol Pension Fund. In 1972 the Judicial Retirement System was added to the new system. The FRS provides a retirement and survivor benefit program, entirely nonparticipatory, for 791 participating public employers, including state government, all county governments, universities, community colleges, school boards, and many cities and special districts. Although the FRS is a relatively young and maturing system, it is the fourth largest public pension plan in the nation.

The Division of Retirement (division) is responsible for administering the FRS, the State University System Optional Retirement Program, the Senior Management Service Optional Annuity Program, the Retiree Health Insurance Subsidy, the Institute of Food and Agricultural Sciences Supplemental Retirement Act, and five General Revenue-funded pension plans. The division is also responsible for monitoring local government retirement systems and oversees the Municipal Police and Firefighters’ Pension Plans.

### **Limitations on Benefits and Contribution Under Qualified Plans**

Congress imposed a cap on benefits payable from qualified defined benefit plans in 1975. Initially, the law was passed to prevent excessive sheltering of income by private sector entities taking tax deductions for retirement plan contributions. Congress set the annual benefit cap at \$75,000 for qualifying age 55, subject to cost of living increases. In 1982, after cost of living adjustments raised the annual benefit cap to \$136,425, Congress rolled back the cap to \$90,000 and raised the qualifying age to 62. Currently, the 1999 benefit cap stands at \$130,000 and is actuarially reduced for persons retiring before age 62. In absolute dollars, the present cap is lower than the 1982 and 1975 caps having eliminated 17 years of cumulative cost of living increases.

Section 415.(b), Internal Revenue Code, also raises concerns regarding consistency and fairness. The law reduces the cap limitation downwards for each year an employee is younger than age 62. Only firefighters and police are exempt from the maximum benefit limitation until age 62. In contrast, there are other employees within the state and local government who must already work longer to receive the same retirement benefit, and should also be entitled to receive it without maximum benefit limitations.

Other consequences of the internal revenue limitation code include: interference with the ability of the state and local units of government to manage their own retirement systems; interference with the ability of the state and local units of government to create incentives for professionals encouraging them to remain in public service careers; and most important, not allowing public employees to collect full retirement benefits when benefits were promised in lieu of higher wages.

### **III. Effect of Proposed Changes:**

The bill creates an excess benefit plan referred to as the "Preservation of Benefits Plan." This plan allows the Division of Retirement to pay any future retirement benefits that exceed Federal limits through a second qualified benefit plan pursuant to s. 415.(m), Internal Revenue Code.

In accord with s. 415., Internal Revenue Code, the Preservation of Benefits Plan is established as a qualified governmental excess benefit arrangement separate and apart from the Florida Retirement System. Participation in the plan is limited to those members and members' beneficiaries whose paid benefits were reduced by the maximum benefit limitations imposed by the Federal government.

Benefits paid under the plan shall not be subject to execution, garnishment, attachment, or other court process except qualified domestic relations orders by a court of competent jurisdiction, income deduction orders and federal income tax levies.

Contributions paid to the division by a retiree's past employer will be reduced by the employer as directed by the division by an amount necessary to meet the requirements for payment of restored benefits under the plan.

The division is directed to administer the plan and to adopt rules necessary to implement the provisions of the bill.

The Legislature has determined that the provisions of this bill serves an important state interest.

This law takes effect July 1, 1999 and expires upon the effective date of a modification or repeal of s. 415.(b), IRC in a manner that exempts governmental retirement plans from the maximum benefit limitations.

#### **IV. Constitutional Issues:**

##### **A. Municipality/County Mandates Restrictions:**

None.

##### **B. Public Records/Open Meetings Issues:**

None.

##### **C. Trust Funds Restrictions:**

Section 415.(m), Internal Revenue Code, prescribes that in establishing a “qualified governmental excess benefit arrangement” a trust be maintained solely for providing benefits under the arrangement and to ensure a tax exempt status under section 115., Internal Revenue Code.

Article III, s. 19, State Constitution, requires that no trust fund be created by law without a three-fifths vote of the membership of each house of the Legislature in a separate bill for that purpose only. Senate Bill 1856 is this bill and will be the instrument for establishing the Preservation of Benefit Plan Trust Fund.

#### **V. Economic Impact and Fiscal Note:**

##### **A. Tax/Fee Issues:**

Benefits paid to retirees are taxable at the individuals’ applicable tax rate.

##### **B. Private Sector Impact:**

The increase in discretionary income for retirees may translate to either increased spending, adding further stimulus to an already robust economy, or provide incentive for further individual savings.

##### **C. Government Sector Impact:**

There should not be any significant impact to the Florida Retirement System since all retirement benefits have already been prefunded. However, the division may experience some difficulties in accounting for and administering the program in the interim.

Clearly, benefits (dollars) which remain in tax sheltered accounts are never taxed until the distribution is taken. To the extent that an FRS member is allowed to take distributions equivalent to his full retirement benefit, those benefits are taxable in the month/year they receive them. The resulting increased benefit this bill will provide to members will also result in greater revenue flow to the Federal Treasury.

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

Federal maximum benefit limitations as applied by the FRS are specified in s. 131.30(5), F.S., and s. 60S-4.002(3), F.A.C. Members' benefits are also limited by s. 121.091(1), F.S., and s. 60s-4.002(3), F.A.C., stating that initial retirement benefits cannot exceed 100 percent of their AFC (average highest 5 years of compensation).

The table below shows the 1999 annual retirement benefit limits for members who retire between ages 42-80 under retirement options 1, 3, or 4:

Age	Ceiling	Age	Ceiling	Age	Ceiling	Age	Ceiling
42	\$33,585	52	\$62,791	62	\$130,000	72	\$256,039
43	\$35,643	53	\$67,151	63	\$130,000	73	\$285,952
44	\$37,850	54	\$71,888	64	\$130,000	74	\$320,710
45	\$40,219	55	\$77,044	65	\$130,000	75	\$361,325
46	\$42,764	56	\$82,668	66	\$141,980	76	\$409,070
47	\$45,501	57	\$88,815	67	\$155,462	77	\$465,547
48	\$48,449	58	\$95,548	68	\$170,691	78	\$532,782
49	\$51,628	59	\$102,941	69	\$187,965	79	\$613,366
50	\$55,060	60	\$111,078	70	\$207,640	80	\$710,627
51	\$58,772	61	\$120,060	71	\$230,154		

**VIII. Amendments:**

None.