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**HOUSE OF REPRESENTATIVES
COMMITTEE ON
STATE ADMINISTRATION
ANALYSIS**

BILL #: HB 149
RELATING TO: Florida Retirement System
SPONSOR(S): Representative(s) Fiorentino and others
TIED BILL(S): None

ORIGINATING COMMITTEE(S)/COUNCIL(S)/COMMITTEE(S) OF REFERENCE:

- (1) STATE ADMINISTRATION
 - (2) FISCAL POLICY & RESOURCES
 - (3) FISCAL RESPONSIBILITY COUNCIL
 - (4)
 - (5)
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I. SUMMARY:

Members of the Florida Retirement System (FRS) who must retire because of total and permanent disability are provided certain disability benefits. When the disability is not job-related, the FRS member must have 8 years of credible service to qualify for regular disability retirement. For "in-line-of-duty" (ILOD) disability, where the disability is due to an injury arising out of job performance, the member is covered from the first day of employment.

Before July 1, 2000, the minimum benefit for total and permanent disability due to an injury ILOD was 42 percent of the disabled retiree's average final compensation (AFC). As of July 1, 2000, this benefit was raised to 65 percent of the retiree's AFC. As of June 30, 2000, there are about 380 disabled members that receive ILOD benefits based on service within the Special Risk Class.

This bill removes the retirement date of July 1, 2000, or thereafter, as a requirement for receiving 65 percent of the retiree's AFC. Accordingly, this bill establishes a 65 percent threshold for the calculation of ILOD disability benefits for the FRS Special Risk Class members, regardless of their date of retirement. This would prospectively increase the threshold benefits provided to special risk members who retired due to total and permanent disability before July 1, 2000. Beginning July 1, 2001, this would increase the future benefit for any affected special risk retiree who retired before July 1, 2000, and whose disability benefit today is less than it would have been had the initial benefit been at least 65 percent of the member's AFC.

This bill would set a precedent by requiring the recalculation and potential benefit improvement for a limited group of employees-- Special Risk retirees who retired prior to July 1, 2000, due to disability. See "Other Comments" section for further detail.

In its current form, this bill fails to fund the benefit improvement provided by the bill. Consequently, this bill *appears to violate Article X, Section 14, of the State Constitution, which requires funding of benefit costs.*

This bill has state and local fiscal impacts. See "Fiscal Analysis and Economic Impact Statement" and "Applicability of the Mandates Provision" sections of this bill analysis for further detail.

II. SUBSTANTIVE ANALYSIS:

A. DOES THE BILL SUPPORT THE FOLLOWING PRINCIPLES:

- | | | | |
|-----------------------------------|------------------------------|-----------------------------|---|
| 1. <u>Less Government</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 2. <u>Lower Taxes</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 3. <u>Individual Freedom</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 4. <u>Personal Responsibility</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 5. <u>Family Empowerment</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |

For any principle that received a "no" above, please explain:

B. PRESENT SITUATION:

Disability Retirement

Under s. 121.091(4), F.S., members of the Florida Retirement System (FRS) who must retire because of total and permanent disability are provided certain disability benefits. A member is considered totally and permanently disabled "if, in the opinion of the administrator, he or she is prevented, by reason of a medically determinable physical or mental impairment, from rendering useful and efficient service as an officer or employee" under s. 121.091(4)(b), F.S.

For regular disability, where the disability is not job-related, the FRS member must have 8 years of credible service to qualify for regular disability retirement. The law may provide for earlier eligibility for a member who becomes disabled after completing five or more years of service before July 1, 1980, but less than 8 years total. s. 121.091(4)(a)1., F.S. Last year, in HB 2393¹, the Legislature provided that, effective July 1, 2001, "a member of [FRS] who becomes totally and permanently disabled after completing 8 years of creditable service" is eligible for disability retirement benefits. The minimum amount payable for regular disability retirement is 25 percent of the member's average final compensation (AFC).² If the disabled member qualifies for a service retirement benefit greater than the 25 percent minimum disability benefit, the higher benefit value is used.

For "in-line-of-duty" (ILOD) disability, where the disability is due to an injury arising out of job performance, the member is covered from the first day of employment.³ Before July 1, 2000, the minimum benefit for total and permanent disability due to an injury ILOD was 42 percent of the disabled retiree's AFC.⁴ As of July 1, 2000, this benefit was raised to 65 percent of the retiree's AFC.

As of June 30, 2000, there are about 380 disabled members that receive ILOD benefits based on service within the Special Risk Class.⁵ The Department of Management Services states that this is about 7/10ths of one percent of the Special Risk Class.⁶

¹ Chapter 2000-169, L.O.F.

² s. 121.091(4)(f)2., F.S.

³ s. 121.091(4)(a), F.S.

⁴ s. 121.091(4)(f)1., F.S.

⁵ 2001 Substantive Bill Analysis on HB 149, Department of Management Services, February 27, 2001.

Precedent for Recalculating Retiree Benefits

With the exception of annual cost-of-living increases, once a FRS member has retired, the base retirement benefit has rarely been recalculated. The Department of Management Services states that as a result of the court decisions in *Mazak v. Division of Retirement*, 1983 WL 1995 (N.D. Fla.), and *Arrington v. State, Division of Retirement*, 1984 WL 3181 (N.D.Fla.),⁷ members released from liminary service on or after December 3, 1974, were granted up to five years of employer paid retirement credit, or more if required by federal law, for active service that interrupted their FRS employment. Also, active and retired members who served in the Armed Forces reserves were allowed to buy back their active wartime military service.⁸ These decisions resulted in changes to the law, see s. 121.111, F.S., and to the rules governing the FRS, see Rules 60S-2.005 and 60S-3.006(2)(b), F.A.C., relating to military service credit. These benefits were recalculated for affected retired members to reflect the additional service credit as a result of these court decisions.

C. EFFECT OF PROPOSED CHANGES:

This bill amends s. 121.091(4)(f), F.S., by removing the date certain for retirement, which is July 1, 2000. Accordingly, the computation of the monthly retirement benefit is 65 percent of the average monthly compensation as of the disability retirement date for a member of the special risk class, irrespective of when the member retired.

Thus, this bill establishes a 65 percent threshold for the calculation of in-line-of-duty (ILOD) disability benefits for the Florida Retirement System (FRS) Special Risk Class members, regardless of their date of retirement. This would prospectively increase the threshold benefits provided to special risk members who retired due to total and permanent disability before July 1, 2000.

Beginning July 1, 2001, this would increase the future benefit for any affected special risk retiree who retired before July 1, 2000, and whose disability benefit today is less than it would have been had the initial benefit been at least 65 percent of the member's average final compensation (AFC). The Department of Management Services states that about 354 disability annuitants would receive higher in-line-of-duty disability benefits based on their service in the Special Risk Class.⁹

This bill would set a precedent by requiring the recalculation and potential improvement of the benefits for a limited group of employees, i.e., Special Risk retirees who retired prior to July 1, 2000, due to disability. Accordingly, this bill opens the door to post-retirement recalculation of benefits, after which, retirement applications would never be final.¹⁰

This bill provides that Special Risk Class employer contribution rates "shall be increased by 0 percentage points." This does not provide any funding for the benefit improvement contained in the bill. Accordingly, this bill raises constitutional concerns under Article X, Section 14 of the Florida Constitution. The constitution requires that any bill that provides an increase in the retirement benefits to the members or beneficiaries must include funding of the increase in benefits on a sound

⁶ *Id.*

⁷ Both of these cases involved conflicts between Florida law and federal law. More specifically, the conflicts involved retirees who took a leave of absence from their FRS employment to serve in the military, or who attempted to claim retirement credit under the FRS for their wartime military service in the Armed Forces' reserves that was also covered by a military pension. These retirees were allowed to obtain military service credit and have their benefits recalculated accordingly.

⁸ Bill Analysis on HB 149, Department of Management Services, at 3.

⁹ *Id.*

¹⁰ *Id.* at 9.

actuarial basis. This language does not require any increase in the employer contribution rates, and therefore does not provide any funding for the increase in benefits.

The sponsor will file an amendment that removes the language regarding the employer contribution rate increase and replaces it with a lump-sum payment from the FRS surplus to fund the increase of benefits for three years, at which time the benefit will be unfunded unless the Legislature chooses to fund the increase in benefits.

According to a report issued by the Florida State Board of Administration regarding the FRS Surplus, the surplus as of December 31, 2000 is at \$807.5 million.¹¹ In the Governor's budget recommendation, \$387.7 million is to be used to fund 2000-01 Public Employee Optional Retirement Program commitments, \$255.5 million is to be used to reduce employer contributions and \$162.3 million is to be redirected to the Fund for Florida's Future.¹² However, this "FRS Surplus" has seen a dramatic decline due to recent stock market activity.¹³ See also "Fiscal Comments."

This bill also contains a statement of "proper and legitimate state purpose," which provides that the fair and adequate protections afforded by the state retirement system fulfill an important state interest.

D. SECTION-BY-SECTION ANALYSIS:

See "Effect of Proposed Changes."

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

Although this bill does not provide for the increase of employer contributions or any other method of funding the increased benefits, those benefits will cost the state government. The Department of Management Service estimates that the increases in benefits will cost \$886,395 for FY 2001-02; \$912,987 for FY 2002-03; and, \$940,377 for FY 2003-04, for state government.¹⁴

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

¹¹ Effective Management of the Available FRS Surplus: Recommendation for a Structured Framework, A Report to the Board Issued by the Staff of the Florida State Board of Administration, January 26, 2001.

¹² *Id.* at 11; see also Governor's e-Budget—Budget Reserves, <http://www.ebudget.state.fl.us/priorities/budgetreserves.asp>, March 16, 2001.

¹³ Week of Pain on Wall Street, http://cnfn.cnn.com/2001/03/16/markets/markets_newyork, March 19, 2001.

¹⁴ Bill Analysis on HB 149, Department of Management Services, at 9.

2. Expenditures:

Although this bill does not provide for the increase of employer contributions or any other method of funding the increased benefits, those benefits will cost the local governments. The Department of Management Service estimates that the increases in benefits will cost \$1,575.814 for FY 2001-02; \$1,623,088 for FY 2002-03; and, \$1,671,781 for FY 2003-04, for local governments.¹⁵

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None.

D. FISCAL COMMENTS:

Actuarial Issues

To comply with Article X, Section 14 of the Florida Constitution, the cost of the bill must be funded. This bill improves the retirement benefits for about 350 special risk retirees¹⁶, who retired before July 1, 2000, due to total and permanent disability. The initial disability benefit for these retirees would be recalculated based on a 65 percent minimum threshold and the new initial benefit would be brought forward to the present, adding intervening cost-of-living adjustments. Approximately \$2.5 million in extra benefits would be paid in FY 2001-02.¹⁷ This amount would increase by 3 percent annually in following years (assuming the affected payees survive and benefits continue).¹⁸ The Department of Management Services states that because the affected members are a "closed group", the cost for increasing their benefits can be estimated; however, "*an actuarial special study must be conducted to project total cost and determine the appropriate rate increases.*"

FRS Surplus

Section 121.031(3)(f), F.S., establishes a rate stabilization mechanism for the Florida Retirement System (FRS). It reserves a specific portion of any actuarial surplus to offset future unfunded liabilities and allows any excess actuarial surplus to be used to offset employer contributions or increase employee retirement benefits. For FY 2000-01, the excess surplus available to the Legislature was \$660.7 million, which was used primarily for a retroactive benefit increase to certain special risk employees and for a reduction in the employer contribution rates.¹⁹

During the 2000 session, the available surplus anticipated for the 2001 session, after considering the effects of the FY 2000-01 changes, was \$520 million. The actual surplus available to the Legislature for the 2001 session is less than \$420 million. The \$100 million decrease is the result of the declining value of FRS assets in our present economy.²⁰

The House Appropriations bill anticipates the use of the entire \$420 million in rate reductions to FRS employers.²¹ About \$100 million of the surplus is used to offset a 2001 rate increase dictated by the actuarial experience study. The remainder reduces employer contributions below the current rates.

¹⁵ *Id.*

¹⁶ *Id.* at 6.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ Appropriations Staff e-mail regarding the status of the FRS Surplus, March 19, 2001.

²⁰ *Id.*

²¹ *Id.*

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

This bill contemplates an amendment that would specify an increase in employer contributions. However, this bill in its current form, does not on its face require counties or municipalities to spend funds or to take action requiring the expenditure of funds; nonetheless, the increase in benefits will cost money. Therefore, the mandates provision of the Florida Constitution applies to this bill.

However, the provisions of this bill fall under an exception to the mandates provision for legislation that affects all state and local governments with special risk employees that are "similarly situated."

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This bill does not reduce the authority that counties or municipalities have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

A. CONSTITUTIONAL ISSUES:

In its current form, this bill fails to fund the benefit improvement it provides. Consequently, this bill appears to violate Article X, Section 14, of the State Constitution, which requires funding of benefit costs.

B. RULE-MAKING AUTHORITY:

None.

C. OTHER COMMENTS:

The Department of Management Services provides a discussion of the possible legal implications of this bill as follows:

While the Legislature has on occasion provided ad hoc cost-of-living increases to improve retiree benefits, post-retirement recalculation of retiree benefits has been required only once; to resolve a conflict in federal and state law. This bill would open the door to post-retirement recalculation of benefits, after which, retirement applications might never be final.

The U.S. Supreme Court expressly disfavored retroactive liability in *Florida v. Long*, 487 U.S. 223, 224, (1988), as it would require an adjustment of "...a fixed calculation based on assumptions that both the State and the retiree held when the retirement occurred. Benefits are altered despite the circumstance that past contributions were keyed to lower benefit payments, which undermines the basic financial calculus of a pension plan . . ." ²²

²² *Florida v. Long*, at 238.

Retirees receiving in-line-of-duty disability benefits prior to July 1, 2000, are not likely to be among the litigants, as this bill would automatically afford most of them improved benefits from the effective date forward.

Current and former FRS members seeking the benefit of the 2000 amendments, such as the plaintiffs demanding special risk class inclusion in a recently filed federal lawsuit, will also be interested in this bill; if they prevail, they will be extended this retroactive coverage.²³ Judgment for the plaintiffs in this lawsuit, and any similar case, could substantially increase the cost of providing the retroactive benefit improvements proposed in this bill.

Id. at 9.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

N/A

VII. SIGNATURES:

COMMITTEE ON STATE ADMINISTRATION:

Prepared by:

Staff Director:

Jennifer D. Krell, J.D.

J. Marleen Ahearn, Ph.D., J.D.

²³ See *Menendez, Hirschbein, et. al., v. Metropolitan Miami-Dade County, Florida and the State of Florida, Department of Management Services, Division of Retirement*, Case Number 01-0379 (filed United States District Court, Southern District of Florida, Jan. 30, 2001).