

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

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

BILL: SB 1650
 SPONSOR: Senator Wise
 SUBJECT: Retirement
 DATE: February 9, 2004 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Wilson</u>	<u>Wilson</u>	<u>GO</u>	<u>Favorable</u>
2.	_____	_____	<u>AGG</u>	_____
3.	_____	_____	<u>AP</u>	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

The bill makes changes to the method of receiving public employee retiree benefits from the health insurance subsidy and both the defined benefit and defined contributions plans administered, respectively, by the Department of Management Services and the Board of Administration.

This bill substantially amends the following sections of the Florida Statutes: ss. 112.363; 121.4501; 121.591; 121.78, 215.47; 215.475; and 215.5601.

II. Present Situation:

The Florida Retirement System (FRS) is a multi-employer, non-participatory pension plan providing retirement income benefits to the more than 600,000 active and 200,000 retired members and beneficiaries of its more than 800 employers. Originally established in 1970 as the successor to the Teachers' Retirement System and the State, and County Officers' and Employees' Retirement System, the FRS is today an amalgamation of four previously separate pension plans. Benefit payments are administered by the Department of Management Services through its Division of Retirement while investment management is undertaken by the Board of Administration. Established as a 401(a) government plan under the Internal Revenue Code its benefits are exempt from federal taxation until received by the employee.

As a defined benefit plan the FRS "Pension Plan" provides retirement income expressed as a percent of final pay. Participants accrue retirement credits based upon their eligibility in one of several membership classes. Years of creditable service multiplied by average salary multiplied by the accrual rate for the membership class plus up to 500 hours of annual leave yields a monthly benefit at normal retirement. The accrual rates range from 1.60 percent for the Regular

Class to 3.33 percent for Justices and Judges. For most membership classes normal retirement occurs at the earlier of thirty years' service or age 62. For public safety employees in the Special Risk Retirement Class, normal retirement is the earlier of age 55 or twenty-five years' service. Members seeking early retirement receive a five percent reduction in the benefit for each year below their normal age threshold. All membership classes permit enrollment in a Deferred Retirement Option Program (DROP) under which a participant may extend employment for an additional five years - eight years for instructional personnel in district school boards - and receive a lump sum benefit at a fixed rate of interest for that supplemental service. Enrollment in DROP nominally requires the participant to serve the employer with a deferred resignation from employment at the end of the period. The defined benefit plan includes a fixed, annual cost-of-living adjustment of three percent.

The 2000 Legislature enacted sweeping changes to the FRS by creating the Public Employees Optional Retirement Program (Part II of ch. 121, F.S.), an alternative defined contribution or "Investment Plan" for its members. While a defined benefit plan provides an annuitized monthly benefit expressed as a percent of final pay, a defined contribution plan gives members an equity interest in their employer's payroll contributions and their earnings, although it does not assure a guaranteed result. All new FRS-covered employees were given the option to enroll in the new plan and employees were provided a once-in-a-lifetime opportunity to change their current enrollment. Generally, a defined benefit plan rewards career employment as its annuitized benefits become more generous with longer service. A defined contribution plan works best for those who value public service for only short employment experiences or who prefer to manage their own investments. DROP enrollment is unavailable for the Investment Plan due to the incompatibility of plan designs.

All state employees are provided with the enrollment opportunity within the first thirty days of retirement to receive post-retirement health insurance coverage and, along with it, a financial stipend to cushion the premium burden. That health insurance subsidy is a five dollar per year of service stipend paid monthly to each retiree. The upper limit is 30 years' service or \$150 a month. Florida law requires all members seeking to keep their health insurance benefits during their retirement to pay the full, active employee premium, unreduced by employer contribution.

III. Effect of Proposed Changes:

Section 1. Section 112.363, F.S., is amended to presumptively establish the spouse at the time of the retiree's death as the designated beneficiary for the purposes of the health insurance subsidy, unless otherwise designated subsequent to the participant's most recent marriage.

Section 2. Subsections (2), (4), (10), and (15) of s. 121.4501, F.S., are amended, as follows:

Subsection (2) defines "retiree" for the purposes of the Investment Plan as a former participant of the Investment Plan who has terminated employment and taken a distribution, other than a minimal account distribution of less than \$5000.

Subsection (4) is amended to change the times frames for enrollment in the Investment Plan for those on leave of absence. The current time frame of 90 days following conclusion of the leave of absence is changed to the last business day of the fifth month following the month the leave of

absence concludes. Amendments also change the effective date provisions for the second election of plan changes from the currently undefined period to the newly defined month following the effective date of the plan selection. The final change in this subsection permits terminated, vested employees to utilize their once-in-a-lifetime opportunity to change plans without having to return to employment for the one year under state law.

Subsection (10) places an obligation on all member employers of the FRS to communicate the existence of the two enrollment choices as part of their personnel management function using educational materials supplied by the Board of Administration and the Department of Management Services.

Subsection (15) changes a cross reference made to the Code of Federal Regulations promulgated by the United States Department of Labor under the statutory provisions of the Employee Retirement Income Security Act (ERISA) of 1974. The ERISA legislation exempts government plans but Florida has elected to have both the Pension Plan and the Investment Plan adhere to its provisions. The amendment to this subsection allows the Board of Administration to disclose to Investment Plan participants the actual institutional fees charged by its investment providers, which are less than those disclosed in similar prospectus filings issued to retail customers of the same funds.

Subsection (20) is created to discharge the Board of Administration from the responsibility of locating persons who have terminated employment prior to the establishment of the Investment Plan and who may be eligible to join as a consequence of the amendments to subsection (4), above.

Section 3. Subsection 121.591(1), F.S., is amended to permit both the Board of Administration and the Department of Management Services to cash out or transfer to a successor custodian an account with a minimum balance of \$ 5000 or less for persons who have terminated employment for at least six months. Subsection (2) is also amended to provide that the survivor of a disabled Investment Plan member shall receive only the remaining account balance in the plan in which membership was established. It eliminates the circumstance in which a survivor can claim a benefit under both systems with membership in only one.

Section 4. Section 121.78, F.S., is amended to require the public employer to make financial adjustments to the Board for payroll contribution rates it has entered in error and to make the employee whole for market losses resulting from late contributions. Terminated participants are also required to return contributions erroneously made by the employer although the Board of Administration and the Investment Plan shall not experience any gain or loss as a result of these corrections.

Section 5. Section 215.47, F.S., is amended to permit the Board of Administration to invest in fixed-income obligations issued by foreign governments or their agencies if they are rated investment grade by at least one nationally recognized rating agency.

Section 6. Section 215.475, F.S., is amended to provide corrected nomenclature reference to the "Defined Benefit Plan" as the one to which its Investment Policy Statement on permitted and excluded investments applies.

Section 7. Section 215.5601, F.S., is amended to provide a similar terminology reference to the Lawton Chiles Endowment Fund, as described in s. 6, above.

Section 8. The act takes effect July 1, 2004.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

There are some 55,000 terminated FRS employees with vested pension rights. Under current law they may change pension plans only upon resumption of employment for one year. Such former employees who do not expect to resume covered FRS employment would be able to switch to the Investment Plan and realize an immediate equity recognition in their individual accounts.

C. Government Sector Impact:

The actuarial valuation method employed by the FRS recognizes a loss in benefit payment obligation as a greater offset than the actual loss of equity for those participants electing to switch plans. For terminated participants with vested pension rights, the immediate liquidation of this benefit obligation tends to suppress pension plan costs in subsequent years, notwithstanding the asset transfer.

The Board of Administration has reported that some public employers have failed to advise their employees of the two pension choices available in the workplace. Some other employers have either not been distributing the official descriptive material relating to this choice or directing, or “spinning,” information from other providers not a part of the FRS product offerings.

Chapter 215, F.S., lists the type of investments that are permitted for the FRS. Current law provides two different statements on the appropriateness of investments in products that are not dollar-denominated, thus limiting the Board of Administration's discretion from debt or equity exposure held in other currencies. While dollar- and non-dollar language is contained in the authorization granted by s. 215.47, F.S., the most recent change added dollar-denominated as the modifier.

The most recent large-scale defaults on publicly issued debt have been the Soviet-era debt of Russia (1988, \$40 billion) and Argentina (2001, \$90 billion), and other lesser amounts by Liberia and Zimbabwe. Iraq's debt, including unserviced war reparations, exceed these combined amounts. In the case of Argentina, the country revalued its currency in pesos rather than denominated dollars in an attempt to service its sovereign public and private debt. That defaulted debt is now in excess of \$99 billion.

There are three major debt ratings services: Standard & Poor; Fitch; and Moody. Each uses a combination of letters and numbers to assign a credit worthiness to the debt issuance. Investment grade, the only suitable rating for investment plan fiduciaries, has its minimum level at BBB or its equivalent.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.