# HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 1815 PCB GO 05-11 State Financial Matters
**SPONSOR(S):** Governmental Operations Committee, Kottkamp
**TIED BILLS:** None **IDEN./SIM. BILLS:** SB 1446

| REFERENCE | ACTION | ANALYST | STAFF DIRECTOR |
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| Orig. Comm.: Governmental Operations Committee | 6 Y, 0 N | Williamson | Everhart |
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## SUMMARY ANALYSIS


The bill makes numerous changes to the Public Employee Optional Retirement Plan (PEORP or Investment Plan), which is managed by the State Board of Administration (SBA). The bill:

- Deletes obsolete language.
- Deletes obsolete cross-references.
- Amends definitions.
- Provides limitations on reemployment after retirement for Investment Plan members, in addition to penalties for violating the reemployment limitations.
- Creates consistent requirements between the Investment Plan and Pension Plan (the defined benefit plan) for new hire and second election filings, and beneficiary designation.
- Authorizes Pension Plan members in the Deferred Retirement Option Program to rollover, tax-free, their lump sum to the Investment Plan at termination.
- Provides for benefits checks not cashed within five years of issuance to be forfeited and reverted to the Investment Plan.
- Creates Investment Plan distribution requirements.
- Authorizes distribution of benefits in a form equivalent to a written application.
- Authorizes the SBA to invest in asset-backed securities.

The bill could have a fiscal impact, though indeterminate, on state government. It does not appear to have a fiscal impact on local governments.

## FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

**Provide limited government** – The bill authorizes the State Board of Administration (SBA) to create rules regarding distribution of an Investment Plan participant's benefits.

**Safeguard individual liberty** – The bill allows Deferred Retirement Option Program (DROP) participants to rollover their DROP lump sum to the Investment Plan at termination, which provides an increase in investment options for such participants.

B. EFFECT OF PROPOSED CHANGES:

**Background**

Florida Retirement System

The Florida Retirement System (FRS) provides retirement income benefits to more than 633,000 active and more than 226,000 retired members and beneficiaries of its more than 800 state and local government employers.[1] The Department of Management Services (DMS) through its Division of Retirement administers benefit payments, while the State Board of Administration (SBA) provides investment management. Benefits are exempt from federal taxation until received by the employee. There are two retirement income plans.

Defined Benefit Plan (Pension Plan)

Under the FRS "Pension Plan," retirement income is a guaranteed percent of final pay, based on an established formula. Participants accrue retirement credits based upon their eligibility in one of several membership classes. For most membership classes, normal retirement occurs at 30 years of service or age 62. For public safety employees in the Special Risk Retirement Class, normal retirement occurs at 25 years of service or age 55. Members seeking early retirement receive a five percent reduction in their retirement income for each year below the normal age or normal years of service threshold. The defined benefit plan includes a fixed, annual cost of living increase of three percent.

All membership classes permit enrollment in the Deferred Retirement Option Program (DROP) that allows retirees to work an additional five years after retirement. Classroom teachers may participate in DROP for eight years. At the end of DROP, retirees receive their retirement income as a lump sum, plus 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.[2] The IRS had to approve this program.

Defined Contribution Plan (Investment Plan)

A 2000 law created the Public Employees Optional Retirement Program as an alternative defined contribution or "Investment Plan" for its members.[3] While a defined benefit plan provides an annuitized monthly benefit expressed as a percent of final pay, a defined contribution plan allows members to invest their retirement contribution. However, the investment plan does not assure a guaranteed result.

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[1] Department of Management Services 2005 Substantive Bill Analysis, HB 123, February 1, 2005, at 3.
[2] Section 121.091(13), F.S.
[3] Part II of chapter 121, F.S.

All active employees in 2000 could switch to the Investment Plan, with one additional opportunity to switch before reaching retirement. DROP enrollment is not available for the Investment Plan participants.

The SBA has identified problems with the way the Investment Plan currently functions. Some of those problems include administrative problems due to differences between the state's two retirement plans; a conflict between the Internal Revenue Service reemployment after retirement guidelines and the Florida's law; and issues, some administrative, surrounding inter-plan transfers.

**Effect of Bill**

Reemployment

The bill limits reemployment after retirement for Investment Plan members consistent with limits in the Pension Plan. An FRS employer cannot reemploy a retiree for three months following that retiree's retirement, unless that retiree has reached the normal retirement thresholds. The penalty to the retiree and the employing agency for violation of this provision is to repay the retirement trust fund the amount of retirement benefits paid to the retiree. In order to avoid liability, the employing agency must have a written statement from the retiree that states he or she is not retired from a state-administered retirement system.

Transferring from One Retirement Plan to the Other

Current law has the effect, in some cases, of preventing inter-plan transfers when the date of the transfer falls in a later month from the month in which the transfer is made, thus requiring manual correction. In order to correct this problem, the bill changes the filing and effective dates when employees switch from one retirement plan to the other, and creates consistent requirements between the Investment Plan and Pension Plan for new hire and second election filings. An FRS member may file his or her second election while actively employed; however, the employee is not required to work in the following month. According to the SBA, approximately 750 employees have their elections reversed each year, generating complaints, reversals of accumulated benefit obligation[4] transfers and contributions between the two FRS trust funds, and unproductive administrative work.[5] The bill further clarifies that the second election is available in the month following enrollment in the first election.

Technical Change

The bill deletes references to the non-existent Public Employee Optional Retirement Program (PEORP or Investment Plan) Advisory Committee; the Investment Council remains as the advisory body to the SBA.

Beneficiaries

The bill creates a new section relating to designation of beneficiaries for the Investment Plan. It tracks the Pension Plan by allowing for beneficiary designation by law, making it easier on Investment Plan participants to designate beneficiaries. It also tracks the Pension Plan with regards to trusts created for a beneficiary who is incapacitated or a minor dependent at the time of the member's death.

DROP

The bill authorizes DROP participants to rollover, tax-free, their accumulated and deferred benefit to the Investment Plan when they terminate employment.

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[4] Accumulated benefit obligation is the present value calculation of benefits earned to date.

[5] State Board of Administration Proposed 2005 Legislative Changes, January 26, 2005.

Retirement Checks Not Cashed

The bill requires forfeiture of retirement checks, over five years old, that have not been chased, and the funds revert to the FRS Investment Plan trust fund. At present, the SBA holds 10 retirement checks, not cashed and totaling $37,096.60.[6]

Three-month Hold on Investment Payout

Though employees terminated less three months may not receive their total Investment Plan pay-out, the SBA may adopt by rule providing for a payout, of up to 10 percent of the participant's Investment Plan account, one-month after termination. This exception only applies if the program participant has reached the normal retirement thresholds. In addition, a program participant may elect to receive his or her benefits in a "form equivalent to a written application," in addition to a written application. According to the SBA, this change allows a program participant to direct his or her payout over the telephone in lieu of providing the current requirement of a written application, which is current practice. Those telephone calls are recorded and kept indefinitely for verification purposes.[7]

Asset-backed Securities

The bill provides the SBA with the authority to invest in asset-backed securities. Asset-backed securities are bonds or notes backed by loan paper or accounts receivables originated by banks, credit card companies, or other providers of credit. Such securities are often enhanced by a bank letter of credit or by insurance coverage provided by an institution other than the issuer.[8]

C. SECTION DIRECTORY:

Section 1 amends s. 121.021, F.S., amending a definition.

Section 2 amends s. 121.091, F.S., providing limitations on reemployment after retirement for Investment Plan members.

Section 3 amends s. 121.4501, F.S., relating to the PEORP.

Section 4 amends s. 121.591, F.S., relating to benefits payable under the PEORP.

Section 5 amends s. 215.47, F.S., authorizing investments in asset-backed securities.

Section 6 provides a July 1, 2005, effective date.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   Authorizing benefit checks not cashed within five years of issuance to be forfeited and reverted to the Investment Plan trust fund could decrease plan expenses by reducing administrative costs for program participants.[9]

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[6] Telephone conversation with the SBA, March 11, 2005.
[7] Public testimony, SBA staff, House Governmental Operations Committee Meeting, March 16, 2005.
[8] State Board of Administration Proposed 2005 Legislative Changes, January 26, 2005.
[9] *Id.* Telephone conversation with the SBA, March 11, 2005.

2. Expenditures:

Authorizing DROP participants to rollover their DROP lump sum to the Investment Plan at termination could save such participants management fees and provide a better selection of quality investment options at little or no cost to the FRS. All members of the Investment Plan would benefit from increased economies of scale.[10]

The Division of Retirement and the SBA have not reached an agreement on whether a financial impact is associated with the provisions of the bill regarding inter-plan transfers. The SBA takes the position that there is no fiscal impact; however, the division has yet to concur.[11]

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None. This PCB does not create, modify, amend, or eliminate a local revenue source.

2. Expenditures:

None. This PCB does not create, modify, amend, or eliminate a local expenditure.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Private investors could lose business to the SBA if DROP participants decide to rollover their lump sum to the Investment Plan.

D. FISCAL COMMENTS:

None.

## III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

The bill does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds. The bill does not reduce the percentage of a state tax shared with counties or municipalities. The bill does not reduce the authority that municipalities have to raise revenue.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

The bill directs the SBA to authorize, by rule, for the distribution of up to 10 percent of an Investment Plan participant's account after being terminated for one calendar month if such participant has reached the normal retirement requirements of the Pension Plan.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

## IV. AMENDMENTS/COMMITTEE SUBSTITUTE & COMBINED BILL CHANGES

None.

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[10] *Id.*

[11] Senate Staff Analysis and Economic Impact Statement, SB 1446, March 11, 2005, at 4.