

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

This bill does not implicate any of the House Principles.

B. EFFECT OF PROPOSED CHANGES:

Present situation

The Florida Retirement System (FRS) provides retirement and disability benefits for Florida state and county employees and for employees of those cities and special districts which choose to participate in the FRS. As of June 30, 2004, state employees (including university employees) represent 21.83% of the FRS membership; counties, 23.46%; district school boards, 48.3%; and community colleges, 2.84%; and cities and special districts that have opted to join the FRS, 3.57%.¹

The active membership of the FRS is divided into five membership classes. Each class is separately funded based upon the costs attributable to the members of that class. The classes and their current employer contribution rates as a percent of gross compensation are:

- Regular Class, 6.20%.
- Special Risk Class, 17.34%.
- Special Risk Administrative Support Class, 8.73%.
- Elected Officers' Class, 11.30%-17.46%, depending on subclass.
- Senior Management Service Class, 8.18%.

The membership criteria for the Special Risk Class are in s. 121.0515, F.S. The class is intended for persons working in certain categories of law enforcement, firefighting, criminal detention, and emergency medical care positions. Because these individuals must perform work that is physically demanding or arduous, or work that requires extraordinary agility and mental acuity, their careers may be shorter than other employees', the Legislature provided different retirement benefits for them. Compared to a Regular Class member, a Special Risk Class member:

- Earns retirement credit at the rate of 3% of average final compensation (AFC) for each year of service, as opposed to the 1.60%-to-1.68% credit per year of service earned by a Regular Class member.
- Qualifies for normal retirement at an earlier age (age 55 vs. age 62) or with fewer years of service (25 years vs. 30 years).
- Who is totally and permanently disabled in the line of duty qualifies for a 65% minimum option 1 benefit payment compared to a Regular Class member similarly disabled, who qualifies for a 42% minimum option 1 benefit payment.

Proposed changes

Special Risk Class members who received Regular Class credit while attending training academies or similar training programs between July 1, 1978, and June 30, 1984, or their employers, would be allowed to purchase an upgrade of their Regular Class credit to Special Risk Class credit. The cost to the member or employer would be the difference in contributions paid and the Special Risk contribution that would have been paid during the period being claimed, plus interest at 6.5% compounded annually until the date the payment is made.

¹ Bill Analysis for HB 339, Department of Management Services.

The consulting actuary for the Department of Management Services' Division of Retirement performed an actuarial study to determine the effect of this change on the Florida Retirement System. Based on the records reviewed during their study, it appears that between approximately 1,900 and 2,800 individuals may be eligible for this benefit. Such individuals may be eligible to upgrade an average of approximately 0.2 years' (or about 2.3 months) worth of Regular Class credit.

While the individuals or their employers would be paying for a portion of the cost of the increased benefit, according to the actuarial study, "the actuarial costs associated with allowing an eligible member to upgrade the specified service is not fully offset by the cost to the member".

Based on certain assumptions², the consulting actuaries have identified a cost to the entire Special Risk Class—not just the employers of those individuals receiving this benefit—of 0.003% of gross compensation, or additional unfunded actuarial liability to the Florida Retirement System of \$1.7 million.

C. SECTION DIRECTORY:

Section 1 amends s. 121.0515, F.S., to grant certain Special Risk Class members the ability to upgrade Regular Class creditable service earned under certain conditions.

Section 2 provides an effective date of upon becoming a law.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

The Retirement System Trust Fund could receive revenues of up to \$1.1 million from purchases of upgraded credit.

2. Expenditures:

See "Fiscal Comments", below.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

See "Fiscal Comments", below.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None.

D. FISCAL COMMENTS:

According to the actuarial study, "the projected increase in actuarial liabilities is \$2.8 million offset by the projected cost the members pay for the eligible service under this proposal of \$1.1 million, which results in the net additional unfunded liabilities of \$1.7 million." To fully fund this benefit, Special Risk

² Based on documents provided by the Division of Retirement, the consulting actuaries assumed that 2,788 individuals would be eligible, each having an average of 0.1957 years of upgradable training service; all elections occurred on June 30, 2004 (since it is to the individual's benefit to purchase the upgrade as soon as possible, avoiding additional interest cost); and that annual salary increases over time were equal to the interest cost of 6.5%.

Class contribution rates would need to increase by 0.0032%. However, because increases are rounded to two decimal points, the actuaries determined that the actual increase in Special Risk Class employer contribution levels should be 0.00%. The actuaries caution that "while there is not an increase in the contribution rates (due to the practice of rounding to two decimal points), there is still a cost to provide this enhanced benefit which will be paid by the Special Risk Class." This cost would be recognized in future valuations of the Florida Retirement System (FRS), resulting in higher rates paid by all Special Risk Class employers, not just employers whose members would receive this benefit. Such employers include state agencies, counties, district school boards, and municipalities and special districts which have opted into the FRS. Special Risk Class employer contribution rates for FY 2004-05 are 17.34% of gross compensation and are scheduled to increase to 22.16% for FY 2005-06, absent Legislative action.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Since it appears that the expenditure related to this increased benefit may be absorbed within the existing plan resources at this time, this bill does not appear to require counties and municipalities to take actions requiring the expenditure of funds. This bill does not reduce the percentage of a state tax shared with counties or municipalities. This bill does not reduce the authority that municipalities have to raise revenue.

2. Other:

Article X, s. 14, Florida Constitution

Since 1976, the Florida Constitution has required that benefit improvements under public pension plans in the State of Florida must be concurrently funded on a sound actuarial basis, as set forth below:

SECTION 14. State retirement systems benefit changes.--A governmental unit responsible for any retirement or pension system supported in whole or in part by public funds shall not after January 1, 1977, provide any increase in the benefits to the members or beneficiaries of such system unless such unit has made or concurrently makes provision for the funding of the increase in benefits on a sound actuarial basis.

Part VII of Chapter 112, F.S.

Article X, s. 14, of the Florida Constitution is implemented by statute under part VII of chapter 112, F.S., the "Florida Protection of Public Employee Retirement Benefits Act," which establishes minimum standards for the operation and funding of public employee retirement systems and plans in the State of Florida. The key provision of this act states the legislative intent to "prohibit the use of any procedure, methodology, or assumptions the effect of which is to transfer to future taxpayers any portion of the costs which may reasonably have been expected to be paid by the current taxpayers."

A study has been performed to assess the bill's compliance with Article X, s. 14, of the Florida Constitution and Part VII of Chapter 112, F.S. While the bill provides for individuals or their employers to purchase upgrades of Regular Class service to Special Risk class service, the consulting actuaries have determined that these payments are unlikely to fund the cost of the benefit. According to the actuarial study, "the projected increase in actuarial liabilities is \$2.8 million offset by the projected cost the members pay for the eligible service under this proposal of \$1.1 million, which results in the net additional unfunded liabilities of \$1.7 million." To fully fund this benefit, Special Risk Class contribution rates would need to increase by 0.0032%. However, because increases are

rounded to two decimal points, the actuaries determined that the actual increase in Special Risk Class employer contribution levels should be 0.00%.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/COMMITTEE SUBSTITUTE & COMBINED BILL CHANGES

None.