

**HOUSE OF REPRESENTATIVES STAFF ANALYSIS**

**BILL #:** HB 245 CS Florida Retirement System  
**SPONSOR(S):** Williams  
**TIED BILLS:** **IDEN./SIM. BILLS:** SB 1094

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<b>REFERENCE</b>	<b>ACTION</b>	<b>ANALYST</b>	<b>STAFF DIRECTOR</b>
1) Governmental Operations Committee	6 Y, 0 N, w/CS	Mitchell	Williamson
2) Local Government Council			
3) Fiscal Council			
4) State Administration Council			
5)			

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**SUMMARY ANALYSIS**

HB 245 amends the definition of “compensation” within the Florida Retirement System Act to include two types of salary supplements made to firefighters, paramedics, or emergency medical technicians: (1) salary supplements for the “successful completion of employer-approved educational training” and (2) salary supplements for “additional job-related duties and responsibilities.” As a result, compensation levels and, ultimately, retirement benefits may be higher for some firefighters, paramedics, or emergency medical technicians.

The bill also provides that employer-reported contributions for supplemental payments are compensation for all periods prior to July 1, 2006.

The bill complies with the requirements of section 14 of article X of the Florida Constitution, which prohibits an increase in the benefits of members without providing funding for the increase on a sound actuarial basis.

There are some definitional, operational, and policy questions raised by the bill.

This bill does not appear to create, modify, or eliminate rulemaking authority.

This bill may have a fiscal impact on state and local government expenditures through the employer contribution to the retirement system for these supplemental payments.

# FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

### A. HOUSE PRINCIPLES ANALYSIS:

This bill does not appear to affect any of the House principles.

### B. EFFECT OF PROPOSED CHANGES:

#### Background on the Florida Retirement System

Chapter 121, Florida Statutes, is the Florida Retirement System Act and it governs the Florida Retirement System (FRS). The FRS is administered by the secretary of the Department of Management Services through the Division of Retirement.<sup>1</sup>

The FRS is the primary retirement plan for employees of state and county government agencies, district school boards, and community colleges and universities.<sup>2</sup> The FRS also has participating employees of 151 cities and 186 independent special districts who have elected to join the system.<sup>3</sup>

The FRS offers a defined benefit plan that provides retirement, disability, and death benefits for nearly 600,000 active members and over 270,000 retirees, surviving beneficiaries, and Deferred Retirement Option Program participants.<sup>4</sup> Members of the FRS belong to one of five membership classes:

Regular Class <sup>5</sup>	570,888 members	88.00%
Special Risk Class <sup>6</sup>	68,466 members	10.59%
Special Risk Administrative Support Class <sup>7</sup>	80 members	0.01%
Senior Management Service Class <sup>8</sup>	6,823 members	1.10%
Elected Officers Class <sup>9</sup>	2,122 members	0.30%

Each class is separately funded through an employer contribution of a percentage of the gross compensation of the member based on the costs attributable to members of that class and as provided in chapter 121, Florida Statutes.<sup>10</sup>

To receive benefits under the FRS, a member must reach his or her "normal retirement date."<sup>11</sup> The normal retirement date depends on the membership class of the member and is based on a minimum number of years of credible service and age (e.g., six or more years and age 62 for a Regular Class member) or specified amount of credible service regardless of age (e.g., 30 years for a Regular Class member).<sup>12</sup>

The amount of benefits a member ultimately receives is based on three key factors: (1) years of service, (2) accrual rate, and (3) average final compensation. "Average final compensation" is the "average of the five highest fiscal years of compensation for credible service."<sup>13</sup>

<sup>1</sup> Fla. Stat. § 121.025 (2005).

<sup>2</sup> Fla. Dep't of Mgmt. Serv., *Fla. Div. of Ret. Main Page* (visited Jan. 11, 2006) < <http://www.frs.state.fl.us/>>.

<sup>3</sup> *Id.*

<sup>4</sup> *Id.*

<sup>5</sup> Fla. Stat. § 121.021(12) (2005).

<sup>6</sup> Fla. Stat. § 121.0515 (2005).

<sup>7</sup> Fla. Stat. § 121.0515(7) (2005).

<sup>8</sup> Fla. Stat. § 121.055 (2005).

<sup>9</sup> Fla. Stat. § 121.052 (2005).

<sup>10</sup> See, e.g., Fla. Stat. 121.055(3)(a)1. (2005).

<sup>11</sup> Fla. Stat. § 121.021(29) (2005).

<sup>12</sup> *Id.*

<sup>13</sup> Fla. Stat. § 121.021(24) (2005).

Relevant to the definition of average final compensation is the definition of “compensation”: the monthly salary a member is paid by his or her employer for work performed arising from that employment.<sup>14</sup> Compensation also includes overtime payments; accumulated annual leave payments; amounts withheld for tax sheltered annuities, deferred compensation programs, or any other type of salary reduction plan authorized under the Internal Revenue Code; and payments made in lieu of a permanent increase in the base rate of pay.<sup>15</sup>

### Changing the Definition of Compensation

This bill expands the definition of compensation for firefighters, paramedics, and emergency medical technicians by allowing

any salary supplement received by a firefighter, paramedic, or emergency medical technician shall be compensation for retirement purposes if each of the following criteria apply:

- a. The salary supplement is a recurring payment received at least quarterly and in addition to the employee’s regular or overtime salary.
- b. The salary supplement is received for assignment, certifications, qualifications, or successful completion of employer-approved education as provided in a formal written policy or contract that applies to all firefighters, paramedics, or emergency medical technicians.

Any salary supplements meeting the criteria of this subparagraph which were received by the Division of Retirement for employment prior to March 1, 2006, and which have not been returned to the contributing employer or credited to the employee by July 1, 2006, shall also be compensation and credited to the employee.

Effective July 1, 2006, the bill amends the definition of compensation to include two types of salary supplements made to firefighters, paramedics, or emergency medical technicians: (1) salary supplements for the “successful completion of employer-approved educational training” and (2) salary supplements for “additional job-related duties and responsibilities.”

The bill also provides that employer-reported contributions on these salary supplements shall be compensation for all periods prior to July 1, 2006.

#### C. SECTION DIRECTORY:

Section 1 amends subsection (22) of section 121.021, Florida Statutes, to revise the definition of compensation.

Section 2 sets forth the legislative declarations and a determination that this act fulfills an important state interest.

Section 3 provides an effective date of July 1, 2006.

## **II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT**

#### A. FISCAL IMPACT ON STATE GOVERNMENT:

##### 1. Revenues:

This bill does not appear to create, modify, amend, or eliminate a state revenue source.

##### 2. Expenditures:

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<sup>14</sup> Fla. Stat. § 121.021(22) (2005).

<sup>15</sup> *Id.*

This bill may create, modify, amend, or eliminate state revenue expenditures.<sup>16</sup>

**B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

1. Revenues:

This bill does not appear to create, modify, amend, or eliminate a revenue source for local governments.

2. Expenditures:

This bill may create, modify, amend, or eliminate revenue expenditures for local governments.<sup>17</sup>

**C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

This bill does not appear to have a direct economic impact on the private sector.

**D. FISCAL COMMENTS:**

The Department of Management Services provided a fiscal note from the enrolled actuary regarding this bill:

Allowing nonrecurring payments to be treated as compensation that may be recognized in the calculation of retirement benefits could lead to artificially inflated benefits. If benefit inflation occurs, it would be a source of actuarial losses which could lead to an increase in normal costs and unfunded actuarial liabilities, possibly resulting in higher contribution rates in the future for the FRS Special Risk Class. There would be a fiscal impact resulting from HB 245, but the nature and amount of these payments are not expected to be sufficient to require a specific increase in the Special Risk Class employer contribution rate to fund this proposal. Future actuarial experience studies and valuations of the FRS would reveal the impact, if any, of covering these payments as compensation for retirement purposes and be reflected in the contribution rate recommended by future valuations.<sup>18</sup>

The Department of Management Services also evaluated the fiscal impact of the bill:

Under current law, the supplemental payments covered by this bill are not reported to the Division of Retirement, so the employer contribution portion of the cost impact cannot be directly determined from our records. Also, the language does not require employers to create new programs for these payments, only to report these payments as compensation for the FRS if they exist on or after July 1, 2006. Each impacted employer would pay an additional 18.53% of such payments to cover the contributions for the FRS benefit and the HIS. We identified approximately 126 employers with at minimum of 10,506 employees who could have additional compensation reported to the FRS under HB 245.<sup>19</sup>

**III. COMMENTS**

**A. CONSTITUTIONAL ISSUES:**

1. Applicability of Municipality/County Mandates Provision:

This bill does not appear to reduce the percentage of a state tax shared with counties or municipalities. This bill does not appear to reduce the authority that counties or municipalities have to raise revenue.

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<sup>16</sup> See Fiscal Comments *infra*.

<sup>17</sup> *Id.*

<sup>18</sup> Fla. Dep't of Mgmt. Serv., HB 245 (2006) Staff Analysis (Nov. 9, 2005) (on file with dep't).

<sup>19</sup> *Id.* Emphasis added.

This bill may, however, require counties or municipalities to spend funds or to take an action requiring the expenditure of funds. Yet, the bill appears to satisfy the requirements of section 18 of article VII of the Florida Constitution<sup>20</sup> because it provides that the act fulfills an important state interest and the expenditures are required by a law which appears to apply to all persons similarly situated, including the state and local governments.

2. Other:

Benefit changes to the state retirement system are governed by section 14 of article X of the Florida Constitution:

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.

According to the Department of Management Services, this bill complies with the requirements of section 14 of article X of the Florida Constitution.<sup>21</sup>

B. RULE-MAKING AUTHORITY:

This bill does not appear to create, modify, or eliminate rulemaking authority.

C. DRAFTING ISSUES OR OTHER COMMENTS:

Other Comment – Policy Change: Bonuses

Currently the definition of compensation specifically excludes bonuses.<sup>22</sup> A bonus is “a payment made in addition to an employee's regular or overtime salary, is usually nonrecurring, does not increase the employee's base rate of pay, and includes no commitment for payment in a subsequent year.”<sup>23</sup>

Bonus payments were excluded from the definition of average final compensation in 1984 and from the definition of compensation in 1989. The Department of Management Services described the reason for these changes:

This change was enacted based upon recommendations from the consulting actuary and the Auditor General who sought to insure that promised benefits would be funded on a sound actuarial basis as required by the Florida Constitution. By excluding bonuses from consideration as compensation, retirement benefits would not be artificially inflated by payments at or near retirement that are not representative of the regular salary or regular payments received over a member's career. This way, unanticipated contribution rate increases are prevented and retirement benefits remain properly funded. Then, in 1989, the Legislature excluded bonus payments from the definition of “compensation,” thereby making reported

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<sup>20</sup> Section 18 of article VII of the Florida Constitution provides that counties and municipalities may not be bound by a general law requiring a county or municipality to spend funds or take an action requiring the expenditure of funds unless it fulfills an important state interest and one of five criteria is met: (1) funds have been appropriated that have been estimated at the time of enactment to be sufficient to fund such expenditure; (2) the legislature authorizes or has authorized a county or municipality to enact a funding source not available for such county or municipality on February 1, 1989, that can be used to generate the amount of funds estimated to be sufficient to fund such expenditure by a simple majority vote of the governing body of such county or municipality; (3) the law requiring such expenditure is approved by two-thirds of the membership in each house of the legislature; (4) the expenditure is required to comply with a law that applies to all persons similarly situated, including the state and local governments; or (5) the law is either required to comply with a federal requirement or required for eligibility for a federal entitlement, which federal requirement specifically contemplates actions by counties or municipalities for compliance.

<sup>21</sup> *Id.*

<sup>22</sup> Fla. Stat. 121.021(22) (2005).

<sup>23</sup> Fla. Stat. 121.021(47) (2005).

compensation consistent with compensation eligible for inclusion in a member's average final compensation.<sup>24</sup>

To the extent that any of these salary supplements can operate without the constraints of “payments in addition to an employee’s base pay,”<sup>25</sup> they may operate like bonuses. Thus, the bill may create a potentially significant policy change as it relates to bonuses as well as a conflict between the definition of compensation and the definition of bonuses.

#### Other Comment – Policy Change: Differential Treatment of Class Members

This bill permits certain salary supplements to be “compensation” for retirement purposes only for firefighters, paramedics, or emergency medical technicians. Yet, the special risk class also includes law enforcement officers,<sup>26</sup> correctional officers,<sup>27</sup> community-based correctional probation officers,<sup>28</sup> youth custody officers,<sup>29</sup> certain employees whose duties involve contact with patients or inmates in a correctional or forensic facility or institution,<sup>30</sup> and employees of a law enforcement agency or medical examiner’s office who are engaged in a forensic discipline.<sup>31</sup> It is not clear how the salary supplements for firefighters, paramedics, or emergency medical technicians differ from those of the other class members such that the salary supplements for one group are counted for retirement purposes, but the salary supplements for the rest of the class are not.

#### Other Comment – Reporting for “All Periods Prior to July 1, 2006”

The bill also provides that employer-reported contributions on supplemental payments shall be compensation for all periods prior to July 1, 2006. It is not clear if that provision only applies to contributions that were previously reported to the FRS - even though these contributions may not have been allowed by law<sup>32</sup> - or if the bill allows reporting of previously unreported salary supplements.

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

On April 5, 2006, the Governmental Operations Committee adopted an amendment and reported the bill favorably with a committee substitute. The amendment revised the types of salary supplements that can be considered compensation for retirement purposes for firefighters, paramedics, or emergency medical technicians. The amendment also limited the retroactivity of the bill.

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<sup>24</sup> Fla. Dep’t of Mgmt. Serv., *supra* note 18.

<sup>25</sup> Fla. Stat. 121.021(22)3. (2005).

<sup>26</sup> Fla. Stat. § 121.0515(2)(a) (2005).

<sup>27</sup> Fla. Stat. § 121.0515(2)(c) (2005).

<sup>28</sup> Fla. Stat. § 121.0515(2)(e) (2005).

<sup>29</sup> Fla. Stat. § 121.0515(2)(g) (2005).

<sup>30</sup> Fla. Stat. § 121.0515(2)(f) (2005).

<sup>31</sup> Fla. Stat. § 121.0515(2)(h) (2005).

<sup>32</sup> *Id.*