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.)

Prepared By: Governmental Oversight and Productivity Committee

BILL: SB 442

INTRODUCER: Senators Lawson and Argenziano

SUBJECT: Retiree Health Insurance Subsidy

DATE: January 4, 2006 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Wilson	Wilson	GO	**Favorable**
2.			WM	
3.				
4.				
5.				
6.				

I. Summary:

The bill increases the monthly health insurance premium subsidy (HIS) payable to retirees and beneficiaries of the Florida Retirement System by $2 per month per year of creditable service beginning January 1, 2007.

This bill substantially amends s. 112.363 of the Florida Statutes.

II. Present Situation:

The Florida Retirement System (FRS) is a multi-employer, non-contributory pension plan providing annuitized defined benefit and equity-based defined contribution retirement benefits to the more than 620,000 active and 210,000 retired members of its more than 800 state and local government employer members. A principal benefit feature of the FRS is its incorporation of a health insurance subsidy payment as an additive to the plan's retirement income features.

Section 112.363, F.S., allows each FRS retiree to apply for and receive a subsidy payment equal to $5 per month per year of creditable service. For defined benefit, or Pension Plan participants, this payment is incorporated as an itemized addition to the monthly retirement income check. For participants in the alternative defined contribution, or Investment Plan, an equivalent amount is added to their account.

An FRS participant must have vested rights, that is, six years of service in the Pension Plan or one year of service in the Investment Plan, to be eligible for the HIS payment. The subsidy requires the applicant to demonstrate that there is an out-of-pocket post-retirement health insurance premium for the subsidy to apply. The participant must also separately apply for this additional benefit feature. An estimated 206,000 retirees or beneficiaries were receiving this benefit in March 2005. The benefit is paid by the imposition of an additional employer contribution rate of 1.11 percent, or 111 basis points,[1] on the employer active payroll. The contribution rate is imposed uniformly on all FRS retirement classes.[2] To effect payment of the subsidy the participant must be retired and have terminated employment. Participants in DROP are still actively employed, though retired, and do not receive this payment until cessation of all covered FRS employment and the receipt of a monthly benefit.

III. Effect of Proposed Changes:

Section 1. The bill amends s. 112.363, F.S., to add new ss. (3)(f) and (g) to increase the FRS retiree health insurance subsidy from $5.00 to $7.00 per month per year of creditable service, in two stages. The first stage increases the benefit from $5.00 to $6.00 effective January 1, 2007. The second stage, from $6.00 to $7.00 funded on July 1, 2006 is effective January 1, 2008. This change is made applicable to all participants and eligible beneficiaries in the Pension Plan and the Investment Plan.

Subsection (8) of s. 112.363, F.S., is amended to fund the benefit increase with a 64 basis point increase in the active employer payroll contribution rate. The revised rate for the HIS will be 1.75 percent effective July 1, 2007 and thereafter.

Section 2. This section provides a statement of important state interest to effect compliance with s. 18, Art. VII (local government legislative mandates) and s. 14, Art. X of the State Constitution (prefunding of public sector pension benefits) and Part VII of ch. 112, F.S (actuarial soundness of retirement systems).

Section 3. The bill takes effect upon becoming a law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

The bill contains an important state interest clause to effect compliance with s. 18, Art. VII, State Constitution.

The full pension funding provisions of s. 14, Art. X, State Constitution are not implicated as the HIS subsidy is not a pension plan. It is, however, incumbent on affected local government employers to remit the increased contributions to pay for the benefit increase.

B. Public Records/Open Meetings Issues:

None.

[1] One basis point is .01%, or .0001.

[2] Regular, Special Risk, Special Risk Administrative Support, Senior Management, and Elected Officers, the latter inclusive of three subclasses of state officers, local government officers, and justices and judges.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

The additional payroll contributions will be remitted by all participating FRS employers on and after the effective date of the bill.

B. Private Sector Impact:

Each retiree and beneficiary will receive an additional $1.00 per month per years of service effective January 1, 2007 and $2.00 per month per year of service effective January 1, 2008. The minimum monthly subsidy payment will increase to $42 from $30 and the maximum will increase to $210 from $150.

C. Government Sector Impact:

Each $1 of HIS equals 22.5 basis points. The effect of this bill will be to increase the current assessment from 111 to 175 basis points. The impact is passed through to FRS employers in the form of an increased payroll contribution rate.

The Division of Retirement (the division) determines the actuarial amount required to fund the HIS. Past practice has been to maintain a minimum reserve of six months' of payments.

On March 14, 2005, the division estimated the following fiscal impact of the original bill:

Table 1
Fiscal Impact of HIS Changes, SB 2266 (2005)

	FY 2006	FY 2007	FY 2008
State Agencies	$11,844,500	$ 24,637,000	$ 25,622,000
Local Governments	$42,220,000	$ 87,818,000	$ 91,330,000
TOTAL	$54,064,500	$112,455,000	$116,952,000

On March 25, 2005, the division responded to a request to provide three alternate financial models for benefit increases in the HIS using various combinations of time lag and payment levels. **Option 1** provided a lower monthly increase to $6.00 and deferred the funding increase to July 2006. The $7.00 HIS payment was made effective January 2007. This option lowered the five-month HIS reserve for three months, April through June 2006, but restored it for the remainder of the period through the year 2010. A six-month minimum funding level is restored by July 2007 and continues to increase after that time. **Option 2** modeled a smaller payroll contribution rate increase effective July 2005 but provided a greater total rate increase in 2006 to accommodate the two-step HIS increase from $6.00 to $7.00 by the year 2007. **Option 3** increased the HIS employer contribution rate by the same amount of benefits increase, about 20 percent, but had a lower rate increase after 2007 than Option 2.

All three of the above options eliminated the fixed cost-of-living allowance in subsequent years.

On November 3, 2005, the Division of Retirement reanalyzed the fiscal impact based upon a rescheduling of the proposed payroll contribution rate increases. A tabular summary of that analysis appears below:

Table 2
Dollar Impact of Proposed Changes, SB 442 (2006)

	FY 2007	**FY 2008**	**FY 2009**
State Agencies	$17,519,000	$ 36,440,000	$ 37,898,000
Local Governments	$62,448,000	$129,892,000	$135,088,000
TOTAL	$79,967,000	$166,332,000	$172,986,000

The analysis underpinning Table 2 assumes a 64 basis point increase effective July 1, 2007.

Table 2a
Alternative Dollar Impact of Proposed Changes, SB 442 (2006)

	FY 2007	**FY 2008**	**FY 2009**
State Agencies	$11,771,000	$ 24,483,000	$ 25,463,000
Local Governments	$41,957,500	$ 87,271,000	$ 90,762,000
TOTAL	$53,728,500	$111,754,000	$116,225,000

The analysis underpinning Table 2a assumes a 43 basis point increase effective January 1, 2007.

Table 2b
Alternative Dollar Impact of Proposed Changes, SB 442 (2006)

	FY 2007	**FY 2008**	**FY 2009**
State Agencies	$ 23,542,000	$ 24,483,000	$ 25,463,000
Local Governments	$ 83,915,000	$ 87,271,000	$ 90,762,000
TOTAL	$107,457,000	$111,754,000	$116,225,000

The analysis underpinning Table 2b assumes a July 1, 2006 effective date and a 43 basis point increase.

Each impact estimate is satisfactory to assure a financial reserve of approximately six months of contributions. The essential differences involve the use of current amounts in excess of this threshold and the timing of the payment increase. While the HIS operates like an annuity, it funded on a pay-as-you-go basis.

VI. Technical Deficiencies:

None.

VII. Related Issues:

Eligibility for payment of the HIS does not require a participating FRS public employer to provide post-retirement health insurance coverage. State of Florida employees may continue their state insurance coverage after retirement provided the choice is exercised within 30 days of retirement and termination of employment. Retirees must pay the full premium, unreduced by any employer premium cost-sharing arrangement after this change is made. Participants in the Deferred Retirement Option Program are considered retirees for pension purposes but are active employees for all other benefits until termination of employment.

The Governmental Accounting Standards Board (GASB) establishes financial accounting standards for state and local governments. Three of its most recent publications are GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*, GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, and Exposure Draft, *Accounting for Termination Benefits.* Governments at all levels will soon have to provide additional disclosure of the funding status of promised workplace benefits. The effect will be to provide, in the specific instance of HIS, a disclosure of the actual positive or negative cash flows associated with the benefit in agency financial statements.

VIII. Summary of Amendments:

None.