HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/CS/HB 525 Florida Retirement System
SPONSOR(S): Appropriations Committee, Workman and others
TIED BILLS: **IDEN./SIM. BILLS:** SB 1280

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Government Operations Subcommittee	7 Y, 6 N, As CS	Meadows	Williamson
2) Appropriations Committee	12 Y, 8 N, As CS	Delaney	Leznoff
3) State Affairs Committee		Meadows	Hamby

SUMMARY ANALYSIS

The Florida Retirement System Act governs the Florida Retirement System (FRS), which is a multi-employer, contributory plan that provides retirement income benefits to 643,746 active members, 319,689 retired members and beneficiaries, and 45,092 members of the Deferred Retirement Option Program. Members of the FRS have two plan options available for participation; a pension plan, which is a defined benefit plan, and an investment plan, which is a defined contribution plan.

The bill increases the pension plan vesting requirements from eight to 11 years for all members of the FRS who enroll in the pension plan on or after July 1, 2012. It also increases the years of service for the disability retirement benefit to conform to the changes for vesting in the pension plan.

The bill revises the normal retirement age for Special Risk Class members for those members initially enrolled in the FRS on or after July 1, 2011. Members must be age 55 and vested, be at least age 48 and have 25 years of special risk service, or be age 52 with 25 years of service, including special risk service and up to four years of wartime military service credit.

The bill requires new members initially enrolled on or after July 1, 2012, to default into the investment plan after the 12 month plan election window closes.

The bill allows members of the Senior Management System Optional Annuity Program (SMSOAP), the State University System Optional Retirement Program (SUSORP), and the State Community College System Optional Retirement Program (SCCSORP) to receive a benefit distribution of up to 10 percent of their account balance one month after termination. It clarifies that the current prohibition on hardship loans for optional retirement programs does not apply to a requested distribution for retirement, a mandatory de minimis distribution authorized by the administrator, or a required minimum distribution provided pursuant to the Internal Revenue Code. The bill clarifies that members of the SMSOAP, the SUSORP, and the SCCSORP are prohibited from being reenrolled as a renewed member in a state administered retirement plan. In addition, members of the SUSORP may not receive benefits funded by voluntary personal contributions until after termination from employment for three calendar months.

The bill revises the required contribution rates for the pension plan and the required employer contribution rates to fund the unfunded actuarial liability of such plan.

The bill provides a declaration of important state interest.

The bill has a fiscal impact on state and local governments. *See* section II. Fiscal Analysis & Economic Impact Statement.

The bill provides for an effective date of July 1, 2012.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Present Situation

Florida Retirement System

The Florida Retirement System (FRS) was established in 1970 when the Legislature consolidated the Teachers' Retirement System, the State and County Officers and Employees' Retirement System, and the Highway Patrol Pension Fund. In 1972, the Judicial Retirement System was consolidated into the pension plan and, in 2007, the Institute of Food and Agricultural Sciences Supplemental Retirement Program was consolidated under the Regular Class of the FRS as a closed group.[1]

The Florida Retirement System Act[2] governs the FRS, which is a multi-employer, contributory plan that provides retirement income benefits to 643,746 active members,[3] 319,689 retired members and beneficiaries,[4] and 45,092 members of the Deferred Retirement Option Program.[5] It is the primary retirement plan for employees of state and county government agencies, district school boards, community colleges, and universities. The FRS also serves as the retirement plan for participating employees of the 182 cities and 231 independent special districts that have elected to join the system.[6]

The membership of the FRS is divided into five membership classes:

- Regular Class[7] has 561,192 members;
- Special Risk Class[8] has 72,675 members;
- Special Risk Administrative Support Class[9] has 63 members;
- Elected Officers' Class[10] has 2,218 members; and
- Senior Management Service Class[11] has 7,598 members.[12]

Each class is funded separately based upon the costs attributable to the members of that class.

Members of the FRS have two plan options available for participation:

- The pension plan, which is a defined benefit plan; and
- The investment plan, which is a defined contribution plan.

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[1] The Florida Retirement System Annual Report, July 1, 2009 – June 30, 2010, at 60 (on file with the Government Operations Subcommittee).
[2] *See* Chapter 121, F.S.
[3] As of June 30, 2011, the FRS pension plan, which is a defined benefit plan, had 540,701 members, and the investment plan, which is a defined contribution plan, had 103,045 members. Information provided by telephone on December 16, 2011, by Mr. Garry Green, Operations & Management Consultant Manager, Division of Retirement, Research and Education Section, Department of Management Services.
[4] Information provided by telephone on December 16, 2011, by Mr. Garry Green, Operations & Management Consultant Manager, Division of Retirement, Research and Education Section, Department of Management Services.
[5] *Id.*
[6] *Id.*
[7] Regular Class members are those members who do not qualify for membership in the other classes within the FRS. *See* s. 121.021(12), F.S.
[8] Members include law enforcement officers, firefighters, correctional officers, correctional probation officers, paramedics, emergency medical technicians, certain professional health care workers within the Department of Corrections and the Department of Children and Family Services, and certain forensic employees. *See* s. 121.0515, F.S.
[9] Members are former members of the special risk class who are transferred or reassigned to an administrative support position in certain circumstances. *See* s. 121.0515(8), F.S.
[10] Membership is comprised of those participants who hold specified elective offices in either state or local government. *See* s. 121.052, F.S.
[11] Members generally are high level executive and legal staff or as specifically provided in law. *See* s. 121.055, F.S.
[12] Information provided by telephone on December 16, 2011, by Mr. Garry Green, Operations & Management Consultant Manager, Division of Retirement, Research and Education Section, Department of Management Services.

Investment Plan
The State Board of Administration (SBA) is primarily responsible for administering the investment plan.[13] The SBA is comprised of the Governor as chair, the Chief Financial Officer, and the Attorney General.[14]

Benefits under the investment plan accrue in individual member accounts funded by employer and employee contributions and earnings.[15] Benefits are provided through employee-directed investments offered by approved investment providers.

A member is immediately vested in all employee contributions paid to the investment plan.[16] With respect to the employer contributions, the member vests upon the completion of one year of work.[17] Vested benefits are payable upon termination or death as a lump-sum distribution, direct rollover distribution, or periodic distribution.[18] In addition to normal benefits and death benefits, the investment plan also provides disability coverage.[19]

Pension Plan
The pension plan is administered by the secretary of the Department of Management Services through the Division of Retirement.[20] Investment management is handled by the SBA.

The pension plan provides retirement income expressed as a percent of final pay. The member receives a monthly benefit which begins to accrue on the first day of the month of retirement and is payable on the last day of the month for the member's lifetime.[21] Years of creditable service multiplied by average final salary multiplied by the accrual rate for the membership class, plus up to 500 hours of annual leave, yield the monthly annuity benefit at normal retirement.[22]

Current law provides that a member employed before July 1, 2011, vests in the pension plan after completing six years of service with an FRS employer.[23] A member employed on or after July 1, 2011, vests in the pension plan after completing eight years of service.[24] Benefits payable under the pension plan are calculated based on years of service X accrual rate X average final compensation. For members of the pension plan enrolled before July 1, 2011, normal retirement occurs at the earlier attainment of 30 years of service or age 62.[25] For members enrolled on or after July 1, 2011, normal retirement occurs at the earlier attainment of 33 years of service or age 65.[26] For members of the Special Risk or Special Risk Administrative Support Class enrolled before July 1, 2011, normal retirement occurs at the earlier attainment of 25 years of service or age 55.[27] For members of the Special Risk or Special Risk Administrative Support Class enrolled on or after July 1, 2011, the normal retirement is the attainment of eight or more years of creditable service and 60 years of age, or attainment of 30 years of creditable service.[28]

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[13] *See* s. 121.4501(8), F.S.
[14] Established by Article IV, s. 4(e) of the State Constitution.
[15] Section 121.4501(7), F.S.
[16] Section 121.4501(6)(a), F.S.
[17] Section 121.4501(6)(b), F.S.
[18] *See* s. 121.591, F.S.
[19] *See* s. 121.4501, F.S.
[20] Section 121.025, F.S.
[21] Section 121.091(1), F.S.
[22] *See* s. 121.091, F.S.
[23] Section 121.021(45)(a), F.S.
[24] Section 121.021(45)(b), F.S.
[25] Section 121.021(29)(a)1.a. and b., F.S.
[26] Section 121.021(29)(a), F.S.
[27] Section 121.021(29)(b)1.a. and b., F.S.
[28] Section 121.021(29)(b)2.a. and b., F.S.

Plan Selection
Florida law provides that a new FRS enrollee automatically defaults into the pension plan if, by the last business day of the fifth month following the month of hire the enrollee does not make an active election of a retirement plan, between the pension plan or the investment plan.[29] If the member does not actively select a retirement plan they are defaulted to the pension plan.[30,31]

Second Election Option
Once a member completes his or her initial plan choice period, the member has a one-time second election option to switch retirement plans (pension plan to investment plan or investment plan to pension plan).[32] This change must be made while the member is actively working for an FRS employer. A member switching to the pension plan from the investment plan must buy-in to the pension plan using the member's account balance in the investment plan and any outside monies necessary to make the pension plan whole.[33]

<u>Optional Retirement Plans</u>

State University System Optional Retirement Program
The optional retirement program for the State University System (SUSORP) is a retirement plan that is provided as an alternative to FRS membership for eligible State University System faculty, administrators, and administrative professionals, and executive service personnel.[34,35] As of June 30, 2011, there were 16,999 SUSORP participants.[36]

Through this program, participants elect coverage as an alternative to membership in the FRS.[37] An employee that is eligible to participate in the SUSORP becomes a compulsory member of the SUSORP unless that member elects within the first 90 days to join the FRS, or fails to complete the SUSORP election process during this period.[38] A member who signs a contract with an eligible SUSORP provider during that initial 90 day window has elected to participate in the SUSORP.[39] A member who do not execute a SUSORP contract is deemed to have elected participation in the FRS and has the remaining portion of the six month election window to choose between the pension plan or the investment plan.[40]

Members of the SUSORP who have executed a contract may make voluntary contributions by salary reduction or deduction in an amount not to exceed the percentage amount contributed by the employer.[41] Current law provides that members may receive a payout of benefits funded by the member's voluntary contributions at any time within the limits of the contract between the member and the provider company.[42]

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[29] Section 121.4501(4)(a)1.a., F.S.
[30] Section 121.4501(4)(a)1.b., F.S.
[31] For the 2010-11 fiscal year, there were 40,051 new hires who completed the retirement plan choice process. Of those members, 25 percent actively elected the investment plan, 22 percent actively elected the pension plan, and 53 percent defaulted to the pension plan. *See* Substantive analysis of HB 525, State Board of Administration, November 9, 2011 (on file with the Government Operations Subcommittee).
[32] Section 121.4501(4)(g), F.S.
[33] Section 121.4501(4)(g)2., F.S.
[34] Section 121.35(2)(a), F.S., provides that SUSORP is available to certain instructional and research faculty, administrative and professional personnel, and the Chancellor and university presidents. Section 121.051(1)(a)2., F.S., requires faculty members at a college with faculty practice plans to participate in the optional retirement program.
[35] *See* s. 121.35, F.S.
[36] Information provided by telephone on December 15, 2011, by Mr. Todd Gunderson, Senior Benefits Analyst, DMS.
[37] Section 121.35(1), F.S.
[38] Section 121.35(2)(c), F.S.
[39] *Id.*
[40] Section 121.35(2)(c)3., F.S.
[41] Section 121.35(4)(e), F.S.
[42] Section 121.35(5)(g), F.S.

State Community College System Optional Retirement Program
The optional retirement program for the State Community College System (SCCSORP) is a retirement plan that is provided as an alternative to FRS membership for eligible State Community College employees.[43] Employees of public community colleges and charter technical career centers sponsored by public community colleges[44] who are members of the Regular Class of the FRS may, in lieu of participating in the FRS, elect to withdraw from the system and participate in the SCCSORP.[45] As of June 30, 2011, there were 1,569 SCCSORP participants.[46]

Senior Management Service Optional Annuity Program
The Senior Management Service Optional Annuity Program (SMSOAP) is a retirement plan that is provided as an alternative to FRS membership for members of the Senior Management Service Class.[47] Under this optional annuity plan, eligible members may purchase retirement, death, and disability benefits.[48] As of June 30, 2011, there were 38 members of the SMSOAP.[49]

<u>Senate Bill 2100 (2011)</u>
During the 2011 Session, the Legislature passed Senate Bill 2100. Senate Bill 2100 made several changes to the FRS, including the following changes:

- Required a 3 percent employee contribution for members of a state-administered retirement plan.[50]
- Increased the years of service required for vesting from six to eight years of creditable service for employees initially enrolled in the pension plan on or after July 1, 2011.[51]
- Revised the definition of "average final compensation" for members who initially enroll in the pension plan on or after July 1, 2011, to mean the average of the eight highest fiscal years of compensation for creditable service prior to retirement, for purposes of calculating retirement benefits.[52]
- Reduced the interest accrual rate from 6.5 percent to 1.3 percent for members who enter the Deferred Retirement Option Program on or after July 1, 2011.[53]
- Increased the retirement age and years of service for members of the FRS who initially enroll on or after July 1, 2011.[54]

Effect of the Bill

The bill makes changes to the FRS; however, changes impacting member benefits do not apply to those persons who have already retired from FRS employment.

The bill revises the definition of “vesting” to clarify that the vesting schedule solely applies to pension plan members. It also revises the definition of “normal retirement date” to clarify that normal retirement age for pension plan members is attained on the normal retirement date of the member. It further clarifies that the normal retirement age for investment plan members is the later of the date a member attains his or her normal retirement age, or is vested under the investment plan as provided by law.

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[43] Section 1012.875, F.S.
[44] *See* s. 1000.21(3)(a)-(bb), F.S., for a list of public community colleges and charter technical careers that are sponsored by public community colleges.
[45] Section 121.051(2)(c)
[46] Information provided by telephone on January 20, 2012, by Mr. Garry Green, Operations & Management Consultant Manager, Division of Retirement, Research and Education Section, Department of Management Services.
[47] Section 121.055(6)(a), F.S.
[48] *Id.*
[49] Information provided by telephone on January 20, 2012, by Mr. Garry Green, Operations & Management Consultant Manager, Division of Retirement, Research and Education Section, Department of Management Services.
[50] Codified in ss. 121.71, 121.055(6)(d)1.c., 121.35(4)(a)3., and 1012.875(4)(a)2., F.S.
[51] Codified in s. 121.021(45)(b), F.S.
[52] Codified in s. 121.021(24), F.S.
[53] Codified in s. 121.091(13)(c)1.b., F.S.
[54] Codified in ss. 121.021(29)(a) and (b)2.a. and b., F.S.

The bill revises the definition of normal retirement date for Special Risk Class members to retroactively apply to members hired on or after July 1, 2011. Such members attain normal retirement age and vest on the first day of the month the member:

- Attains age 55 and completes the required years of service for vesting;
- Attains age 48 and completes 25 years of creditable service in the Special Risk Class; or
- Completes 25 years of creditable service and attains age 52, which may include a maximum of four years of military service.

For members initially enrolled in the FRS on or after July 1, 2012, the bill increases the length of creditable service needed to vest in the pension plan from eight to 11 years. It also increases the years of service for the disability retirement benefit for members initially enrolled on or after July 1, 2012, to conform to the changes for vesting in the pension plan.

The bill provides that an employee hired on or after July 1, 2012, by an employer who participates in the FRS, automatically defaults into the investment plan. The employee maintains the opportunity to elect to participate in the pension plan, but this election must be made by the last business day of the twelfth month after the employee's month of hire. If the employee fails to elect to participate in the pension plan during the prescribed period, then that option is deemed to be forfeited. These changes do not affect the initial election process for eligible members of the SUSORP, the SMSOAP, or the SCCSORP.[55]

The bill provides that a member of the SMSOAP, the SUSORP, or the SCCSORP may receive a distribution of up to 10 percent of his or her benefit after termination for one calendar month. This provision aligns the optional retirement programs with the investment plan.

For purposes of the SMSOAP, the SUSORP, and the SCCSORP, the bill clarifies that the current prohibition on hardship loans does not apply to:

- A requested distribution for retirement;
- A mandatory de minis distribution authorized by the administrator; or
- A required minimum distribution provided pursuant to the Internal Revenue Code.

The bill makes it clear that a retiree of the SMSOAP, the SUSORP, or the SCCSORP who is reemployed on or after July 1, 2010, is prohibited from being reenrolled as a renewed member of a state-administered retirement system.

The bill clarifies that a member of the SUSORP may receive payment of benefits from either annuity contracts or investment contracts. Additionally, it provides that the term benefit, for purposes of the SUSORP, means a distribution taken by the member, or surviving beneficiary, funded in part or in whole by employer and employee contributions. A rollover distribution to another qualified plan qualifies as a distribution. A member of the SUSORP may not receive benefits funded by voluntary personal contributions until after termination from employment for three calendar months.

The bill revises the required contribution rates for the pension plan and the required employer contribution rates to fund the unfunded actuarial liability of such plan.

The bill provides a declaration of important state interest.

Finally, the bill provides for an effective date of July 1, 2012.

B. SECTION DIRECTORY:

Section 1 amends s. 121.021, F.S., to revise the definitions of "normal retirement date" and "vested" or "vesting."

[55] Information provided by electronic mail on February 9, 2012, by Mr. Garry Green, Operations & Management Consultant Manager, Division of Retirement, Research and Education Section, Department of Management Services (on file with the Government Operations Subcommittee).

Section 2 amends s. 121.055, F.S., to clarify provisions relating to the prohibition of hardship loans or payments; to clarify that a retiree who is reemployed in a regularly established position after a certain date may not be enrolled as a renewed member; to authorize certain distributions; to provide rulemaking authority to the Department of Management Services.

Section 3 amends s. 121.091, F.S., to revise provisions relating to the early retirement benefit calculation to conform to changes made by the act; to revise provisions relating to the disability retirement benefit calculation to conform to changes made by the act.

Section 4 amends s. 121.35, F.S., to provide that a benefit for the purpose of the optional retirement system for the State University System includes certain distributions; to clarify provisions relating to the prohibition of hardship loans or payments; to authorize certain distributions; to clarify when voluntary contributions may be paid out; to provide rulemaking authority to the Department of Management Services.

Section 5 amends s. 121.4501, F.S., to require new employees to, by default, be enrolled in the investment plan; to revise the benefit commencement age to conform to changes made by the act.

Section 6 amends s. 121.591, F.S., to revise provisions relating to the disability retirement benefit calculation to conform to changes made by the act.

Section 7 amends s. 1012.875, F.S., to clarify provisions relating to the prohibition of hardship loans or payments; to authorize certain distributions; to provide rulemaking authority to the college.

Section 8 provides for contribution rate adjustments to fund benefit changes provided for in this act.

Section 9 provides a declaration of important state interest.

Section 10 provides an effective date of July 1, 2012.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   None.

2. Expenditures:

   The estimated fiscal impact for fiscal year 2012-2013 is as follows:
   - General Revenue Fund: $38,000
   - Trust Funds: $1,155,000 – the trust fund fiscal impact will be divided and absorbed among all state entities participating in the Florida Retirement System, with a net average impact of approximately $39,000 per agency, which will vary depending number and retirement class of employees and agency funding sources.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

   None.

2. Expenditures:

   The fiscal impact for fiscal year 2012-2013 is as follows:

- Counties: $18,075,000
- Municipalities/Others: $908,000

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

The mandates provision of Art. VII, s. 18 of the State Constitution appears to apply because this bill will cause counties and municipalities to incur additional expenses associated with the improved FRS benefits provided by the bill; however, an exception applies as the Legislature has determined that this bill satisfies an important state interest. In addition, similarly situated persons are all required to comply.

2. Other:

Actuarial Requirements
Article X, s. 14 of the State Constitution requires that benefit improvements under public pension plans in the State of Florida 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.

Article X, s. 14 of the State Constitution is implemented by statute under part VII of chapter 112, F.S., the "Florida Protection of Public Employee Retirement Benefits Act" (Act). The Act establishes minimum standards for the operation and funding of public employee retirement systems and plans in the State of Florida. It prohibits 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.

This bill appears to meet the requirements of Article X, s. 14 of the State Constitution.

B. RULE-MAKING AUTHORITY:

The bill provides rulemaking authority to the Department of Management Services and the board of trustees for state community colleges. It authorizes the department and the board to adopt rules to provide for the distribution of certain benefits for qualified members of optional retirement programs.

C. DRAFTING ISSUES OR OTHER COMMENTS:

According to the State Board of Administration the change to the normal retirement date for the Special Risk Class may generate a legal challenge. In addition, some employees or their unions may feel that the Special Risk Class is getting preferential treatment by receiving a much better retirement benefit than other FRS members.[56]

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

On January 31, 2012, the Government Operations Subcommittee adopted a strike-all amendment and reported the bill favorably with a committee substitute.

The strike-all amendment revises the definition of “normal retirement date” to clarify the normal retirement age for pension plan and investment plan members.

The strike-all amendment revises the definition of normal retirement date for Special Risk Class members to retroactively apply to members hired on or after July 1, 2011. Such members attain normal retirement age and vest on the first day of the month the member:

- Attains age 55 and completes the required years of service for vesting;
- Attains age 50 and completes 25 years of creditable service in the Special Risk Class; or
- Completes 25 years of creditable service and attains age 52, which may include a maximum of four years of military service.

The strike-all amendment increases the vesting period for pension plan members initially enrolled on or after July 1, 2012, from eight to 11 years. It also increases the years of service for the disability retirement benefit to conform to the changes for vesting in the pension plan.

The strike-all amendment allows members of the SMSOAP, the SUSORP, and the SCCSORP to receive a distribution of up to 10 percent of their account one month after termination. It clarifies that members of the SMSOAP, the SUSORP, and the SCCSORP may not be reenrolled as a renewed member of a state administered retirement program. The strike-all amendment also provides for a definition of benefit for purposes of the SUSORP. For purposes of the SMSOAP, the SUSORP, and the SCCSORP, it clarifies that the current prohibition on hardship loans does not apply to a requested distribution for retirement, a mandatory de minis distribution authorized by the administrator, or a required minimum distribution provided pursuant to the Internal Revenue Code. It provides that members of the SUSORP may not receive benefits funded by voluntary personal contributions until after termination from employment for three calendar months.

The strike-all amendment revises the required contribution rates for the pension plan and the required employer contribution rates to fund the unfunded actuarial liability of such plan.

Finally, the strike-all amendment provides a declaration of important state interest.

On February 15, 2012, the Appropriations Committee adopted a strike-all amendment to the bill and reported the bill favorably as a committee substitute. The amendment:

- Decreased the retirement age with 25 years of service from 50 to 48 years of age.
- Increased the election default period from 5 months to 12 months after month of hire.
- Clarifies language related to adjustments in employer contribution rates. .

This analysis is drafted to the committee substitute to the committee substitute as passed by the Appropriations Committee.

[56] Substantive analysis of HB 525, State Board of Administration, November 9, 2011, at 3 (on file with the Government Operations Subcommittee).