

**The Florida Senate**  
**BILL ANALYSIS AND FISCAL IMPACT STATEMENT**

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Budget Committee

BILL: SPB 7056

INTRODUCER: For consideration by the Budget Committee

SUBJECT: Retirement

DATE: February 12, 2012      REVISED: \_\_\_\_\_

|    | ANALYST | STAFF DIRECTOR | REFERENCE | ACTION             |
|----|---------|----------------|-----------|--------------------|
| 1. | McSwain | Rhodes         |           | <b>Pre-meeting</b> |
| 2. |         |                |           |                    |
| 3. |         |                |           |                    |
| 4. |         |                |           |                    |
| 5. |         |                |           |                    |
| 6. |         |                |           |                    |

**I. Summary:**

Effective July 1, 2012, the bill amends:

- Sections 121.051 and 1012.875, Florida Statutes, to reduce the employer contribution rates into the Community College System Optional Retirement Program.
- Section 121.055, Florida Statutes, to reduce the employer contribution rates into the Senior Management Service Optional Annuity Program.
- Section 121.35, Florida Statutes, to reduce the employer contribution rates into the State University System Optional Retirement Program.
- Section 121.71, Florida Statutes, to adjust the employer-paid contribution rates for moral cost and unfunded actuarial liability for the Florida Retirement System (FRS), based on the 2011 Actuarial Valuation, as adjusted by the changes to the Investment Plan allocations.
- Section 121.72, Florida Statutes, to reduce the allocation rates for all retirement classes being deposited into Investment Plan member accounts.

The bill conforms provisions in chapter 121, Florida Statutes, to the proposed Senate General Appropriations Act for Fiscal Year 2012-2013.

**II. 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. Prior to 1975, members of the FRS were required to make employee contributions. Regular Class members contributed four percent of their salary while Special Risk Class Members contributed six percent. The 2011 Legislature reinstated employee contributions whereby all Class members contribute three percent of their salary.

The Florida Government System Act<sup>1</sup> governs the FRS, which is a multi-employer, contributory plan that provides retirement income benefits to 643,746 active members, 318,881 retirees and 45,092 members of the Deferred Optional Retirement System (DROP)<sup>2</sup>. It is the primary retirement plan for employees of the state and county government agencies, district school boards, community colleges and state universities. The FRS also serves as the retirement plan for 185 municipalities and 243 independent special districts that have irrevocably elected to participate.<sup>3</sup>

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

- Regular Class<sup>4</sup>: 561,618 members (87.25 percent)
- Special Risk Class<sup>5</sup>: 72,675 members (11.29 percent)
- Special Risk Administrative Support<sup>6</sup>: 71 members (0.01 percent)
- Elected Officer Class<sup>7</sup>: 2,284 members (0.31 percent)
- Senior Management Services Class<sup>8</sup>: 7,310 members (1.14 percent)

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

### **Investment Plan**

In 2000, the Legislature created the Public Employee Optional Retirement Program (Investment Plan), a defined contribution plan offered to eligible employees as an alternative to the FRS defined benefit plan. The Investment Plan was available for participation as of July 1, 2001.<sup>9</sup> Allocation rates into the accounts were based on the normal costs of the Pension Plan at the time.

Benefits under the Investment Plan accrue in individual member accounts funded by employer and employee contributions. Investments are employee-directed into State Board of Administration (SBA) approved investment providers. Members of the Investment Plan contribute three percent of their salaries to their accounts as required by SB 2100 (Chapter No. 2011-68, L.O.F.). The remainder of the allocation comes from employer-paid contributions.

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<sup>1</sup> Chapter 121, F.S.

<sup>2</sup> As of June 30, 2011 the defined benefit plan had 540,701 active members and the Investment Plan had 103,045 members. Data received from Division of Retirement staff.

<sup>3</sup> Participating Employer 2011 Report produced by the Division of Retirement.

<sup>4</sup> Members who do not qualify for membership in another class (includes renewed members.)

<sup>5</sup> Members include law enforcement officers, firefighters, correctional officers, correctional probation officers, paramedics, emergency medical technicians, certain professional health care workers, and certain forensic workers.

<sup>6</sup> Members are former members of the special risk class who are transferred or reassigned to an administrative support position in certain circumstances.

<sup>7</sup> Members include holders of specified elected offices in either state or local government.

<sup>8</sup> Members are high level executive or legal staff as provided by law.

<sup>9</sup> Part II, chapter 121, F.S.

A member vests in the Investment Plan after one-year with an FRS employer. Vested benefits are payable upon termination of employment or death as a lump-sum distribution, roll-over distribution, or periodic distribution. The Investment Plan also provides disability benefits, which is essentially an option to collect disability benefits as provided in the defined benefit plan.

The SBA is primarily responsible for administering the Investment Plan.<sup>10</sup> The SBA is comprised of the Governor as chair, the Chief Financial Officer and the Attorney General.

### **Pension Plan (Defined Benefit Plan)**

The Pension Plan is administered by the secretary of the Department of Management Services through the Division of Retirement. Investment management of retirement funds is handled by the State Board of Administration.

The 2011 Legislature made significant changes to the Pension Plan of the FRS in SB 2100 (Chapter No. 2011-68, L.O.F.), which resulted in a significant decrease in the required employer-paid contribution rates, but made no changes to the allocations into members' investment accounts, which created a funding and potential benefit inequity. Changes specifically to the Pension Plan included:

- Increasing the retirement age and years of service for all retirement classes for new enrollees;
- Decreasing the interest rate earned on DROP accounts from 6.5 percent to 1.3 percent for participants entering DROP on or after July 1, 2011;
- Providing that additional service on or after July 1, 2011, does not accrue Cost of Living Adjustments (COLA);
- Increasing the vesting period from 6 to 8 years for new enrollees employed on or after July 1, 2011;
- Increasing the period used in determining the Average Final Compensation from 5 to 8 years for new employees employed on or after July 1, 2011.

Participants of the Pension Plan were also required to contribute three percent of their salary the same as Investment Plan participants.

### **Optional Retirement Programs**

Eligible employees may choose to participate in one of the optional retirement programs instead of participating in the FRS:

- Members of the Senior Management Service Class may elect to enroll in the Senior Management Service Optional Annuity Program.<sup>11</sup>
- Members in specified positions in the State University System may elect to enroll in the State University System Optional Retirement Program.<sup>12</sup>

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<sup>10</sup> Section 121.4501, F.S.

<sup>11</sup> Section 121.055, F.S.

<sup>12</sup> Section 121.35, F.S.

- Members employed by a Florida college may elect to enroll in the State Community College System Optional Retirement Program.<sup>13</sup>

The distributions into these accounts are funded by both employer and employee contributions. Participants in these programs are also required to contribute three percent of their salaries to the plan per Chapter No. 2011-68, L.O.F, while the employer contributions vary by Retirement Class. As noted above, significant changes were made to the defined benefit plan, but as with the allocations for the Investment Plan, the employer contribution rates for the optional retirement programs remained unchanged.

### **Contribution Rates**

FRS employers are responsible for contributing a percentage of a member's monthly salary to the FRS Contributions Clearing Account Trust Fund in the Division of Retirement to fund the program. The employer contribution is a "blended contribution rate" set by statute<sup>14</sup>, as amended by the Legislature based on an annual actuarial valuation. The rate consists of a blending of the actuarially determined contribution rates necessary to fund the Pension Plan's normal cost and the allocations being made into Investment Plan accounts. The purpose of the blending is to establish the same employer contribution rates regardless of whether an employee participates in the Pension Plan or the Investment Plan.

## **II. Effect of Proposed Changes:**

The bill reduces the employer-paid shares of the allocation into the Investment Plan and employer contributions into the optional retirement plans to a level closer to the actuarial determined "blended" normal costs for the Pension Plan, as determined in the July 1, 2011 Valuation.

In addition, the bill revises the employer-paid normal cost rates for the FRS, as determined by the July 1, 2011 Annual Valuation as necessary to adequately fund the costs of retirement benefits during Fiscal Year 2012-2013 and to reflect the adjustments to the allocations for Investment Plan member accounts contained in the bill and retains, during Fiscal Year 2012-2013, the employer-paid unfunded actuarial liability (UAL) rates which are in effect during Fiscal Year 2011-2012.

**Section 1** amends s. 121.051(2)(c), F.S. to revise the employer-paid portion of the contribution for participants in the Community College Optional Retirement Program. Effective July 1, 2012, the employer-paid contribution will be 5.15 percent of employee compensation. Currently, the employer-paid contribution is 7.43 percent.

**Section 2** amends s. 121.055, F.S., to revise the employer-paid portion of the contribution for participants in the Senior Management Service Optional Annuity Program. Effective July 1, 2012, the employer-paid contribution will be 6.27% of employee compensation. Currently, the employer-paid contribution is 9.49 percent.

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<sup>13</sup> Sections 121.051 and 1012.875, F.S.

<sup>14</sup> Sections 121.031 and 121.71, F.S.

**Section 3** amends s. 121.35, F.S., to revise the employer-paid contribution for participants in the State University Optional Retirement Program. Effective July 1, 2012, the employer-paid contribution will be 5.15% of employee compensation. Currently, the employer-paid contribution is 7.42 percent.

**Section 4** amends s. 121.71(4), F.S., to establish the employer-paid contributions for normal cost effective July 1, 2012 and July 1, 2013, and amends s. 121.71(5), F.S., to establish the employer-paid contributions for unfunded actuarial liability effective July 1, 2012 and July 1, 2013, for all for FRS participants. The normal costs were “blended” with the proposed Investment Plan allocations to establish employer contribution rates. The bill maintains the same employer-paid contribution rates for Unfunded Actuarial Liability that were in effect for Fiscal Year 2011-2012. The rates for Fiscal Year 2013-14 are included in the bill to ensure the actuarial soundness of the Retirement System Trust Fund if the Legislature fails to pass legislation to set rates during the 2013 Regular Session, or if the Governor vetoes such legislation. The chart below sets for the proposed employer-paid contribution rates contained in the bill:

**Proposed FRS Employer Contributions**

| Membership Class                  | Blended Normal Costs |                | Unfunded Actuarial Liability |                |
|-----------------------------------|----------------------|----------------|------------------------------|----------------|
|                                   | As of 7/1/2012       | As of 7/1/2013 | As of 7/1/2012               | As of 7.1.2013 |
| Regular Class                     | 3.55%                | 3.55%          | 0.49%                        | 2.02%          |
| Special Risk Class                | 11.01%               | 11.01%         | 2.75%                        | 7.03%          |
| Special Risk Administrative Class | 3.94%                | 3.94%          | 0.83%                        | 27.04%         |
| Elected Officer Class             |                      |                |                              |                |
| Leg/Gov/SA/PDs                    | 6.51%                | 6.51%          | 0.88%                        | 27.18%         |
| Judges                            | 10.02%               | 10.02%         | 0.77%                        | 16.38%         |
| County Officers                   | 8.36%                | 8.36%          | 0.73%                        | 23.01%         |
| Senior Management                 | 4.84%                | 4.84%          | 0.32%                        | 11.25%         |
| DROP                              | 4.33%                | 4.33%          | 0.00%                        | 6.21%          |

**Section 5** amends s. 121.72(4), F.S., to revise the contributions from the Florida Retirement System Contributions Clearing Trust Fund to individual Investment Plan members’ individual member accounts. The contribution rates are reduced by 30 percent to effectuate a leveling of the normal costs of the Investment Plan with the normal costs of the Pension Plan.

**Section 6** amends s. 1012.875, F.S., to revise the employer-paid portion of the contribution for participants in the Community College Optional Retirement Program. Effective July 1, 2012, the employer-paid contribution will be 5.15 percent of employee compensation. Currently, the employer-paid contribution is 7.43 percent.

**Section 7** provides that a proper and legitimate state purpose is served when state and local government employees are extended basic protections afforded by governmental retirement systems and that the act “fulfills an important state interest.”

**Section 8** provides for an effective date of July 1, 2012.

**III. Constitutional Issues:**

A. Municipality/County Mandates Restrictions:

The bill will impact those municipalities who have elected to participate in FRS as well as all counties. However, Art. VII, section 19(a), Fla. Const., contains exceptions that provide that the mandates provision does not apply when the Legislature determines that the law fulfills an important state interest and when the law applies to all persons similarly situated. Also, Art VII, section 19 (d), Fla. Const., provides that laws adopted to require funding of pension benefits existing on the effective date of Art. VII, section 18, laws are exempt from the mandates provision.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

**IV. Fiscal Impact Statement:**

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

None.

C. Government Sector Impact:

An actuarial study was done by actuaries employed by the Division of Retirement to determine the impact from changes to the allocations to individual members Investment Plan accounts to the “blended” normal cost for the FRS, as determined in the July 1, 2011 Valuation Study. The net impacts of the adjustments to the “blended” normal cost of the FRS made by the bill upon state funded entities are as follows:

| <b>Entities Funded by the State</b> | <b>General Revenue Fund</b> | <b>Trust Funds</b> | <b>Total</b>    |
|-------------------------------------|-----------------------------|--------------------|-----------------|
| State                               | \$11.17M                    | 11.17M             | 22.34M          |
| School Boards                       | 46.73M                      |                    | 46.73M          |
| State University System             | 4.48M                       |                    | 4.48M           |
| Community Colleges                  | 3.47M                       |                    | 3.47M           |
| <b>Total</b>                        | <b>\$62.38M</b>             | <b>11.17M</b>      | <b>\$77.02M</b> |

The reduction in employer-paid contributions to the State University Optional Retirement Program, the Community College Optional Retirement Program and the Senior Management Service Optional Annuity Program produce the following savings to the entities indicated:

| <b>Entities Funded by the State</b> | <b>General Revenue Fund</b> | <b>Trust Funds</b> | <b>Total</b>      |
|-------------------------------------|-----------------------------|--------------------|-------------------|
| State                               | (\$0.07M)                   | (\$0.07M)          | (\$0.15M)         |
| State University System             | (45.70M)                    |                    | (45.70M)          |
| Community Colleges                  | (3.12M)                     |                    | (3.12M)           |
| <b>Total</b>                        | <b>(\$48.89M)</b>           | <b>(\$0.07M)</b>   | <b>(\$48.97M)</b> |

**V. Technical Deficiencies:**

None.

**VI. Related Issues:**

Article I, section 10, Fla. Const., prohibits any bill of attainder, ex post facto law, or law impairing the obligation of contracts from being passed by the Florida Legislature.

Section 121.011(3)(d), F.S., provides that the rights of members of the FRS are of a contractual nature, entered into between the member and the state, and such rights are legally enforceable as valid contractual rights and may not be abridged in any way. This “preservation of rights” provision was established by the Florida Legislature with an effective date of July 1, 1974.<sup>15</sup>

The Florida Supreme Court has held that the rights provision was not intended to bind future legislatures from prospectively altering benefits which accrue for future state service.<sup>16</sup> The prospective application could only alter future benefits. Those benefits previously earned or accrued by the member, under the previous benefit structure, must remain untouched and the member continues to enjoy that level of benefit for the period of time up until the effective date of the proposed changes. Further, once the participating member reaches retirement status, the benefits under the terms of the FRS in effect at the time of the member's retirement vest and cannot be adversely altered.<sup>17</sup>

The Florida Supreme Court further held that the “preservation of rights” provision was not intended to bind future legislatures from prospectively altering benefits which accrue for future state service.<sup>18</sup>

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<sup>15</sup> The “preservation of rights” provision vests all rights and benefits already earned under the present retirement plan so the legislature may now only alter benefits prospectively. *Florida Sheriffs Association v. Department of Administration, Division of Retirement*, 408 So.2d 1033, 1037 (Fla.1981).

<sup>16</sup> *Id.*

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

<sup>18</sup> *Id.*

This bill does not change any benefits that any FRS member or participant in an optional retirement program earned prior to July 1, 2012. The bill only makes changes on a prospective basis. As such, it does not appear to impair any contractual obligation between the employer and any FRS member or participant in an optional retirement program.

**VII. Additional Information:**

- A. **Committee Substitute – Statement of Substantial Changes:**  
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

- B. **Amendments:**

None.

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This Senate Bill Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.

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