

**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.)

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Prepared By: The Professional Staff of the Committee on Appropriations

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BILL: CS/SB 242

INTRODUCER: Community Affairs Committee and Senator Brandes

SUBJECT: Publicly Funded Retirement Plans

DATE: April 8, 2015

REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Peacock</u>	<u>McVaney</u>	<u>GO</u>	<b>Favorable</b>
2.	<u>White</u>	<u>Yeatman</u>	<u>CA</u>	<b>Fav/CS</b>
3.	<u>Shettle</u>	<u>Kynoch</u>	<u>AP</u>	<b>Pre-meeting</b>

**Please see Section IX. for Additional Information:**

COMMITTEE SUBSTITUTE - Substantial Changes

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**I. Summary:**

CS/SB 242 requires local government pension plans, in conducting the actuarial valuations of their pension plans, to use mortality table methodologies consistent with the methodologies used in either of the two most recently published actuarial valuation report of the Florida Retirement System (FRS). In most instances, the mortality tables used will recognize longer lifetimes for annuitants and result in higher annual contributions required to be paid into the pension funds in the near term.

Similarly, the bill revises the mortality tables to be used in the actuarial disclosures in financial statements submitted to the Department of Management Services (DMS). This modification does not impact the actuarial funding of the various pension plans but does provide some information that may be useful when comparing local pension plans and the FRS.

To the extent the use of the updated mortality tables results in increases to the normal costs or unfunded liabilities of local government pension plans, this bill will result in higher contributions being paid into the local government pension plans in the near term.

The bill provides an effective date of July 1, 2015.

## II. Present Situation:

### Florida Local Retirement Systems and Plans

The Division of Retirement of the DMS reports<sup>1</sup> that as of September 30, 2014, there are 491 defined benefit plans sponsored by 249 local governments in Florida. The vast majority of the plans, 486, are local government defined benefit systems that provide benefits to 87,097 retirees, with 97,677 active employees, and total plan assets of \$30.5 billion.<sup>2</sup> The average annual pension in these local defined benefit plans is \$25,252, and the average annual required contribution rate as a percentage of payroll is 31.96 percent. The total unfunded actuarial accrued liability for all the defined benefit plans as of September 30, 2014, was \$10.5 billion.

### Actuarial Soundness of Retirement Plans

The Florida Constitution requires public pension plans in the State of Florida to be concurrently funded on a sound actuarial basis.<sup>3</sup> The Florida Protection of Public Employee Retirement Benefits Act (Act)<sup>4</sup> establishes the minimum standards for the operation and funding of public employee retirement systems and plans in the State of Florida. The 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.”<sup>5</sup>

Under current law, total contributions to a public sector retirement plan must be sufficient to fund the normal cost of the retirement plan and to amortize the unfunded actuarial liability over a period not to exceed 40 years.<sup>6</sup> If an unfunded liability arises from a plan amendment, changes in actuarial assumptions, changes in funding methods or actuarial gains or losses, the liability must be amortized within 30 years.<sup>7</sup> The laws establishing the municipal police<sup>8</sup> and firefighter<sup>9</sup> pension plans have similar provisions.

Enrolled actuaries prepare and certify actuarial reports for each retirement plan subject to the Act, at regular intervals of at least three years.<sup>10</sup> The actuarial reports must include at least the following information:<sup>11</sup>

- Adequacy of employer and employee contributions;

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<sup>1</sup> Division of Management Services, *Florida Local Government Retirement Systems*, 2014 Annual Report, available online at: [http://www.dms.myflorida.com/workforce\\_operations/retirement/local\\_retirement\\_plans/local\\_retirement\\_section/local\\_government\\_annual\\_reports](http://www.dms.myflorida.com/workforce_operations/retirement/local_retirement_plans/local_retirement_section/local_government_annual_reports) (last visited on February 12, 2015).

<sup>2</sup> The other 6 plans are school board early retirement programs that provide benefits to 1,686 retirees, with active plan membership of 4,506, and total plan assets of \$64.8 million.

<sup>3</sup> FLA. CONST. art. X, s. 14 (1976).

<sup>4</sup> Part VII of Ch. 112, F.S., implements Article X, Section 14, of the Florida Constitution.

<sup>5</sup> Section 112.61, F.S.

<sup>6</sup> Section 112.64(2), F.S.

<sup>7</sup> Section 112.64(4), F.S.

<sup>8</sup> Section 185.07, F.S.

<sup>9</sup> Section 175.091, F.S.

<sup>10</sup> Section 112.63, F.S.

<sup>11</sup> Section 112.63(a)-(f), F.S.

- A plan to amortize any unfunded liability and a description of actions taken to reduce the unfunded liability;
- A description and explanation of actuarial assumptions;
- A schedule illustrating the amortization of unfunded liabilities, if any;
- A comparative review illustrating the actual salary increases granted and the rate of investment return realized over the 3-year period preceding the actuarial report with the assumptions used in both the preceding and current actuarial reports;
- A disclosure of the present value of the plan's accrued vested, nonvested, and total benefits, as adopted by the Financial Accounting Standards Board, using the FRS's assumed rate of return; and
- A statement by the enrolled actuary that the report is complete and accurate and that the techniques and assumptions used are reasonable and meet the requirements of state law.

The actuarial reports are submitted to the DMS, which reviews each report to determine whether the actuarial valuation is complete, accurate, and based on reasonable assumptions.<sup>12</sup>

### **Mortality Tables, Generally**

Because mortality assumptions control the expected length of time for annuity payments, they are a critical component in determining the liabilities of a defined benefit plan.<sup>13</sup> Defined benefit accounting standards do not dictate mortality assumptions, leaving sponsors to decide which assumptions they use for financial statement reporting. However, the Pension Protection Act of 2006 (PPA) gives the IRS authority to prescribe mortality rates used in the calculation of funding liabilities. In this way, the RP-2000 Mortality Tables have been implemented pursuant to section 430(h)(3) of the Internal Revenue Code (IRC).

The RP-2000 was published by the Society of Actuaries (SOA) in the year 2000.<sup>14</sup> In 2009, the SOA started the process of creating updated mortality tables for pension plans. Some sponsors have already started using the interim Scale BB improvement actors, which were released in 2012. In February 2014, the SOA released the RP-2014 tables and MP-2014 improvement scales. Although the IRS has not publicly indicated when it will review funding of mortality assumptions, as required every 10 years by PPA, analysts within the industry suggest the new RP-2014 tables may be “in use as early as 2016 for both funding requirements and lump-sum conversions.”<sup>15</sup> For accounting purposes, adoption of the new mortality tables will be at the discretion of the plan sponsor.

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<sup>12</sup> Section 112.63(4)(a), F.S.

<sup>13</sup> Russell Research, *How Will the New RP-2014 Mortality Tables Affect my DB Plan Strategy*, available at <http://www.russell.com/documents/institutional-investors/research/how-will-the-new-rp-2014-mortality-tables-affect-my-db-strategy.pdf> (last visited March 23, 2015).

<sup>14</sup> RP-2000 Mortality Tables are available at <https://www.soa.org/research/experience-study/pension/research-rp-2000-mortality-tables.aspx> (last visited on February 23, 2015).

<sup>15</sup> Russell Research, *How Will the New RP-2014 Mortality Tables Affect my DB Plan Strategy*, available at <http://www.russell.com/documents/institutional-investors/research/how-will-the-new-rp-2014-mortality-tables-affect-my-db-strategy.pdf> (last visited March 23, 2015).

**Mortality Tables used by FRS**

The FRS uses different mortality tables for its general employee and special risk classes for non-disability retirement. The 2014 FRS Valuation used the RP-2000 mortality table with Scale BB improvement actors. Non-disability retirements have a separate mortality basis for Special Risk Class members compared to all other membership classes. Disability retirements have a common mortality basis for all classes. The disability requirement for FRS members is total and permanent from all forms of employment as certified by two licensed physicians.

**Mortality Tables used by Local Government Retirement Plans**

In determining the actuarially required contributions for a local government pension plan, the pension plan’s board of trustees, with guidance from its professional advisors, chooses a mortality table to be applied in the valuation report.<sup>16</sup> The table below shows the various mortality tables used by local government retirement plans and the frequency of use among the plans.

<b>Mortality Table</b>	<b>Number of local government plans using this table</b>
1983 Group Annuity Mortality (GAM 83)	20
1994 Group Annuity Mortality (GAM 94)	10
1994 Group Annuity Mortality with Scale AA (GAR 94)	7
Uninsured Population 1994 (UP 94)	4
Retirement Plans 2000 (RP 2000)	437
Internal Revenue Service Prescribed	8
Other	3
Total	489

**Mortality Tables, as Additional Disclosures**

In addition to the valuation report, s. 112.664, F.S., requires certain actuarial disclosures used to determine required funding for all publicly-funded defined benefit retirement plans, other than FRS. Amongst other provisions, these additional actuarial disclosures mandate the use of the “RP-2000 Combined Healthy Participant Mortality Tables, by gender, with generational projection by Scale AA.”<sup>17</sup>

The additional reporting requirements must be provided to the DMS annually, within 60 days after receipt of the certified actuarial report submitted after the close of the plan year that ends after June 30, 2014, and thereafter in each year in which an actuarial valuation of the plan is done. Plans that fail to submit timely the required information within 60 days after receipt of the plan’s actuarial report will be deemed to be in noncompliance. The DMS may notify the Department of Revenue (DOR) and Department of Financial Services (DFS) of the noncompliance, and the DOR and DFS must withhold funds payable to the plan sponsor, which are not pledged towards bond debt service.

<sup>16</sup> Dep’t of Management Services, *2015 Legislative Bill Analysis: SB 242*, at 2 (Jan. 20, 2015).

<sup>17</sup> Section 112.664(1)(a), F.S.

### III. Effect of Proposed Changes:

**Section 1** amends s. 112.63, F.S., to require the actuarial valuations of local government pension plans to use mortality table methodology consistent with either of the two most recently published actuarial valuation reports of the FRS. For the 2014 Actuarial Valuation of the FRS, the RP-2000 mortality table with Scale BB was used.

While the FRS uses RP-2000 mortality table with Scale BB, additional adjustments are made based on gender, membership class, and varying mixes of white collar and blue collar work. For example, different mortality bases are used for non-disability retirements in the Special Risk Class compared to the mortality bases used for non-disability retirements in other membership classes. At first glance, one would assume that the mortality assumptions used for FRS Special Risk Class would be an acceptable assumption to use for the police and firefighter pension plans. However, the FRS Special Risk Class has a broader membership than those local pension plans.<sup>18</sup> This broader membership base may result in a different mix of white collar and blue collar jobs. The bill specifies that the mortality tables must include the projection scale for mortality improvement; appropriate risk and collar adjustments must be made based on plan demographics; and the tables must be used for assumptions for preretirement and postretirement mortality.

**Section 2** amends s. 112.664, F.S., to revise the information included in a defined benefit retirement system or plan's annual report to the DMS to include financial statements that use mortality table methodology consistent with either of the two most recently published actuarial valuation report of the FRS. In general, this change will require local plans to use Scale BB rather than Scale AA with the RP-2000 mortality table.

**Section 3** provides that the Legislature determines that the bill fulfills an important state interest as related to publicly funded retirement plans.

**Section 4** provides an effective date of July 1, 2015.

### IV. Constitutional Issues:

#### A. Municipality/County Mandates Restrictions:

To the extent this bill requires a local government to expend funds to comply with its terms, the provisions of Art. VII, s. 18(a) of the Florida Constitution may apply. If those provisions do apply, in order for the law to be binding upon the cities and counties, the Legislature must find that the law fulfills an important state interest, and one of the following relevant exceptions must apply:

- The expenditure is required to comply with a law that applies to all persons similarly situated; or

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<sup>18</sup> Section 121.0515, F.S., defines membership in the FRS Special Risk Class also to include correctional officers, certain emergency medical technicians and paramedics, certain nurses and other health professionals, certain forensic laboratory technicians, and certain employees of a medical examiner's office.

- The law must be approved by two-thirds of the membership of each house of the Legislature.

Since this bill requires all public sector pension plans to use similar mortality methodologies, it appears the bill applies to all persons similarly situated (state, municipalities and special districts sponsoring pension plans). The bill also contains a finding that the bill fulfills an important state interest (section 3). Thus, it appears the bill is binding upon cities and counties that sponsor retirement plans.

**B. Public Records/Open Meetings Issues:**

None.

**C. Trust Funds Restrictions:**

None.

**V. Fiscal Impact Statement:**

**A. Tax/Fee Issues:**

None.

**B. Private Sector Impact:**

None.

**C. Government Sector Impact:**

Under CS/SB 242, local governments' pension plan board of trustees, and professional advisors, will be required to use the FRS mortality tables in their actuarial valuations, which may result in different contribution requirements from prior plans' valuation reports.<sup>19</sup>

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

None.

**VIII. Statutes Affected:**

This bill substantially amends the following sections of the Florida Statutes: 112.63 and 112.664.

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<sup>19</sup> Dep't of Management Services, *2015 Legislative Bill Analysis: SB 242*, at 5 (Jan. 20, 2015).

**Additional Information:**

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

**CS by Community Affairs on March 10, 2015:**

Actuarial reports and annual financial statements must include mortality tables from either of the two most recent FRS reports, instead of just the most recently published one. The mortality tables must specifically include the projection scale for mortality improvement; appropriate risk and collar adjustments must be made based on plan demographics; and the tables must be used for assumptions for preretirement and postretirement mortality.

- B. **Amendments:**

None.