

**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 Governmental Oversight and Accountability

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BILL: SPB 7038

INTRODUCER: For consideration by the Governmental Oversight and Accountability Committee

SUBJECT: Employer Paid Contributions for Retiree Benefits

DATE: March 3, 2015

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

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ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1. <u>McVaney</u>	<u>McVaney</u>	_____	<b><u>Pre-meeting</u></b>

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**I. Summary:**

SPB 7038 establishes the contribution rates paid by employers participating in the Florida Retirement System (FRS) beginning July 1, 2015. These rates are intended to fund the full normal cost and the amortization of the unfunded actuarial liability of the FRS. With these modifications to employer contribution rates, the FRS will receive roughly \$34.5 million less in revenue on an annual basis beginning July 1, 2015.

The bill also increases the contributions paid by employers participating in the retiree health insurance subsidy program. With the increased contribution rates, the Retiree Health Insurance Trust Fund will receive roughly \$96.8 million of additional revenues on an annual basis beginning July 1, 2015.

**II. Present Situation:**

**The 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 FRS, 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.<sup>1</sup> The FRS is a contributory system, with most members contributing three percent of their salaries.<sup>2</sup>

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<sup>1</sup> The Florida Retirement System Pension Plan and Other State Administered Systems Comprehensive Annual Financial Report Fiscal Year Ended June 30, 2014, at p. 29. Available online at: [https://www.rol.frs.state.fl.us/forms/2013-14\\_CAFR.pdf](https://www.rol.frs.state.fl.us/forms/2013-14_CAFR.pdf).

<sup>2</sup> Prior to 1975, members of the FRS were required to make employee contributions of either 4 percent for Regular Class employees or 6 percent for Special Risk Class members. Employees were again required to contribute to the system after July 1, 2011. Members in the Deferred Retirement Option Program do not contribute to the system.

The FRS is a multi-employer, contributory plan, governed by the Florida Retirement System Act in Chapter 121, F.S. As of June 30, 2014, the FRS had 622,089 active members, 363,034 annuitants, 16,137 disabled retirees, and 38,058 active participants of the Deferred Retirement Option Program (DROP).<sup>3</sup> As of June 30, 2014, the FRS consisted of 1,014 total employers; it is the primary retirement plan for employees of state and county government agencies, district school boards, Florida College institutions, and state universities, and also includes the 186 cities and 262 special districts that have elected to join the system.<sup>4</sup>

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

- The Regular Class<sup>5</sup> consists of 537,993 active members, plus 5,402 in renewed membership;
- The Special Risk Class<sup>6</sup> includes 68,593 active members;
- The Special Risk Administrative Support Class<sup>7</sup> has 84 active members;
- The Elected Officers' Class<sup>8</sup> has 2,040 active members, plus 147 in renewed membership; and
- The Senior Management Service Class<sup>9</sup> has 7,607 members, plus 184 in renewed membership.<sup>10</sup>

### ***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 Pension Plan.

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

A member vests immediately in all employee contributions paid to the investment plan.<sup>11</sup> With respect to the employer contributions, a member vests after completing one work year of employment with an FRS employer.<sup>12</sup> Vested benefits are payable upon termination or death as a

<sup>3</sup> Florida Retirement System Annual Financial Report Fiscal Year Ended June 30, 2014, at 112.

<sup>4</sup> *Id.*, at 146.

<sup>5</sup> The Regular Class is for all members who are not assigned to another class. Section 121.021(12), F.S.

<sup>6</sup> The Special Risk Class is for members employed as law enforcement officers, firefighters, correctional officers, probation officers, paramedics and emergency technicians, among others. Section 121.0515, F.S.

<sup>7</sup> The Special Risk Administrative Support Class is for a special risk member who moved or was reassigned to a nonspecial risk law enforcement, firefighting, correctional, or emergency medical care administrative support position with the same agency, or who is subsequently employed in such a position under the Florida Retirement System. Section 121.0515(8), F.S.

<sup>8</sup> The Elected Officers' Class is for elected state and county officers, and for those elected municipal or special district officers whose governing body has chosen Elected Officers' Class participation for its elected officers. Section 121.052, F.S.

<sup>9</sup> The Senior Management Service Class is for members who fill senior management level positions assigned by law to the Senior Management Service Class or authorized by law as eligible for Senior Management Service designation. Section 121.055, F.S.

<sup>10</sup> All figures from Florida Retirement System Annual Financial Report Fiscal Year Ended June 30, 2014, at 115.

<sup>11</sup> Section 121.4501(6)(a), F.S.

<sup>12</sup> If a member terminates employment before vesting in the investment plan, the nonvested money is transferred from the member's account to the SBA for deposit and investment by the SBA in its suspense account for up to five years. If the member is not reemployed as an eligible employee within five years, then any nonvested accumulations transferred from a member's account to the SBA's suspense account are forfeited. Section 121.4501(6)(b) – (d), F.S.

lump-sum distribution, direct rollover distribution, or periodic distribution.<sup>13</sup> The investment plan also provides disability coverage for both inline-of-duty and regular disability retirement benefits.<sup>14</sup> An FRS member who qualifies for disability while enrolled in the investment plan must apply for benefits as if the employee were a member of the pension plan. If approved for retirement disability benefits, the member is transferred to the pension plan.<sup>15</sup>

The State Board of Administration (SBA) is primarily responsible for administering the investment plan.<sup>16</sup> The SBA is comprised of the Governor as chair, the Chief Financial Officer, and the Attorney General.<sup>17</sup>

### ***Pension Plan***

The pension plan is administered by the secretary of the Department of Management Services through the Division of Retirement.<sup>18</sup> Investment management is handled by the State Board of Administration.

Any member initially enrolled in the pension plan before July 1, 2011, vests in the pension plan after completing six years of service with an FRS employer.<sup>19</sup> For members enrolled on or after July 1, 2011, the member vests in the pension plan after eight years of creditable service.<sup>20</sup> Benefits payable under the pension plan are calculated based on the member's years of creditable service multiplied by the service accrual rate multiplied by the member's average final compensation.<sup>21</sup> For most members of the pension plan, normal retirement occurs at the earliest attainment of 30 years of service or age 62.<sup>22</sup> For public safety employees in the Special Risk and Special Risk Administrative Support Classes, normal retirement is the earliest of 25 years of service or age 55.<sup>23</sup> Members initially enrolled in the pension plan on or after July 1, 2011, have longer vesting requirements. For members initially enrolled after that date, the member must complete 33 years of service or attain age 65, and members in the Special Risk classes must complete 30 years of service or attain age 60.<sup>24</sup>

### ***Optional Retirement Programs***

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

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<sup>13</sup> Section 121.591, F.S.

<sup>14</sup> See s. 121.4501(16), F.S.

<sup>15</sup> Pension plan disability retirement benefits, which apply for investment plan members who qualify for disability, compensate an in-line-of-duty disabled member up to 65 percent of the average monthly compensation as of the disability retirement date for special risk class members. Other members may receive up to 42 percent of the member's average monthly compensation for disability retirement benefits. If the disability occurs other than in the line of duty, the monthly benefit may not be less than 25 percent of the average monthly compensation as of the disability retirement date. Section 121.091(4)(f), F.S.

<sup>16</sup> Section 121.4501(8), F.S.

<sup>17</sup> Section 4, Art. IV, Fla. Const.

<sup>18</sup> Section 121.025, F.S.

<sup>19</sup> Section 121.021(45)(a), F.S.

<sup>20</sup> Section 121.021(45)(b), F.S.

<sup>21</sup> Section 121.091, F.S.

<sup>22</sup> Section 121.021(29)(a)1., F.S.

<sup>23</sup> Section 121.021(29)(b)1., F.S.

<sup>24</sup> Sections 121.021(29)(a)2. and (b)2., F.S.

- Members of the Senior Management Service Class may elect to enroll in the Senior Management Service Optional Annuity Program;<sup>25</sup>
- Members in specified positions in the State University System may elect to enroll in the State University System Optional Retirement Program;<sup>26</sup> and
- Members in specified positions at a Florida College institution may elect to enroll in the State Community College System Optional Retirement Program.<sup>27</sup>

**Contribution Rates**

FRS employers are responsible for contributing a specified percentage of the member’s monthly compensation to the Division of Retirement to be distributed into the FRS Contributions Clearing Trust Fund. The employer contribution rate is a blended contribution rate set by statute, which is the same percentage regardless of whether the member participates in the pension plan or the investment plan.<sup>28</sup> The rate is determined annually based on an actuarial study by the Department of Management Services that calculates the necessary level of funding to support all of the benefit obligations under both FRS retirement plans.

In the annual actuarial valuation of the Florida Retirement System based on July 1, 2014, plan assets and liabilities, Milliman, Inc., the state actuary, determined the following key data relating to the FRS pension plan.

	<b>Valuation Results (in \$ billions)</b>			
	<b>July 1, 2011</b>	<b>July 1, 2012</b>	<b>July 1, 2013</b>	<b>July 1, 2014</b>
Actuarial Liability	\$144.1	\$147.2	\$153.3	\$160.1
Actuarial Value of Assets	\$126.1	\$127.9	\$131.7	\$138.6
Unfunded Actuarial Liability	\$ 18.0	\$ 19.3	\$ 21.6	\$21.5
Funded Percentage	87.5%	86.9%	85.9%	86.6%

The following are the current employer contribution rates for each class and the blended rates recommended by the state actuary beginning in July 2015:<sup>29</sup>

<sup>25</sup> The Senior Management Service Optional Annuity Program (SMSOAP) was established in 1986 for members of the Senior Management Service Class. Employees in eligible positions may irrevocably elect to participate in the SMSOAP rather than the FRS. Section 121.055(6), F.S.

<sup>26</sup> Eligible participants of the State University System Optional Retirement Program (SUSORP) are automatically enrolled in the SUSORP. However, the member must execute a contract with a SUSORP provider within the first 90 days of employment or the employee will default into the pension plan. If the employee decides to remain in the SUSORP, the decision is irrevocable and the member must remain in the SUSORP as long as the member remains in a SUSORP-eligible position. Section 121.35, F.S.

<sup>27</sup> If the member is eligible for participation in a State Community College System Optional Retirement Program, the member must elect to participate in the program within 90 days of employment. Unlike the other optional programs, an employee who elects to participate in this optional retirement program has one opportunity to transfer to the FRS. Section 1012.875, F.S.

<sup>28</sup> Section 121.70(1), F.S.

<sup>29</sup> Section 121.71(4) and (5), F.S.

Membership Class	Current Rates Effective July 1, 2014		Recommended Rates to be effective July 1, 2015	
	Normal Cost	UAL Rate	Normal Cost	UAL Rate
Regular Class	3.53%	2.54%	2.91%	2.65%
Special Risk Class	11.01%	7.51%	11.35%	8.99%
Special Risk Administrative Support Class	4.18%	36.59%	3.71%	27.54%
Elected Officer’s Class				
• Legislators, Governor, Lt. Governor, Cabinet Officers, State Attorneys, Public Defenders	6.30%	38.66%	6.48%	37.62%
• Justices and Judges	10.10%	21.77%	11.39%	22.62%
• County Officers	8.36%	33.58%	8.48%	32.09%
Senior Management Service Class	4.80%	15.04%	4.32%	15.41%
Deferred Retirement Option Program	4.30%	6.72%	4.23%	7.12%

For all membership classes, except the DROP and certain members with renewed membership, employees contribute three percent of their compensation towards retirement.<sup>30</sup>

After employer and employee contributions are placed into the FRS Contributions Clearing Trust Fund, the allocations under the investment plan are transferred to third-party administrators to be placed in the employee’s individual investment accounts, whereas contributions under the pension plan are transferred into the FRS Trust Fund.<sup>31</sup>

**Retiree Health Insurance Subsidy**

Section 112.363, Florida Statutes, provides for a retiree health insurance subsidy. This subsidy is paid from the Retiree Health Insurance Subsidy Trust Fund to eligible retirees of the FRS. The amount of the monthly subsidy is \$5 for each year of service in the FRS, but not less than \$30 nor more than \$150.

The subsidy is funded through a contribution by employers participating in the FRS. The current contribution is 1.26 percent of the employer’s monthly payroll. The contribution is paid to the Department of Management Services for deposit in the Retiree Health Insurance Subsidy Trust Fund. This program is funded on a “pay-as-you-go” basis rather than on an actuarial basis. This means that the revenues and expenditures of the trust fund are designed to match each other on an annual basis, with minimal reserves accumulated.

Participants of the university, community college, and senior management service defined contribution retirement programs receive contributions directly into their retirement accounts during the years of employment; these participants will not receive the health insurance subsidy

<sup>30</sup> Section 121.71(3), F.S.

<sup>31</sup> See sections 121.4503 and 121.72(1), F.S.

during retirement. Participants of the FRS investment plan will not receive the health insurance subsidy contributions directly but will be eligible to receive the health insurance subsidy upon retirement.

Sections 121.052, 121.055, and 121.071, F.S., also set forth the employer-paid contributions for the retiree health insurance trust fund for the various FRS membership classes.

A recent cash flow analysis of the Retiree Health Insurance Subsidy Trust Fund indicates the following key cash flow data for Fiscal Year 2010-2011 through Fiscal Year 2014-2015. Under current law and current administration and assuming only two percent payroll growth for Fiscal Year 2013-2014 and Fiscal Year 2014-2015, the trust fund is expected to deplete its reserves by September 2015. After that date, the trust fund may not have sufficient revenues to pay the full monthly benefits to retirees.

<b>Retiree Health Insurance Subsidy Trust Fund</b>				
<b>Changes in Fund Balance (in \$ millions)</b>				
	<b>FY 2013-14</b>	<b>FY 2014-15</b>	<b>FY 2015-16</b>	<b>FY 2016-17</b>
Fund Balance – beginning of Year	\$121.53	\$60.49	\$7.25	(\$59.20)
Revenues (employer contributions and	\$366.24	\$372.53	\$379.66	\$387.25
Expenditures	\$407.28	\$425.77	\$446.11	\$468.94
Excess of Revenues over Expenditures	(\$61.04)	(\$53.24)	(\$66.45)	(\$81.69)
Fund Balance – end of year	\$60.49	\$7.25	(\$59.20)	(\$140.89)
Reserves (balance / monthly expenses)	1.8 months	0.2 months	(1.6 months)	(3.6 months)

**III. Effect of Proposed Changes:**

The bill increases the employer-paid contributions for the retiree health insurance subsidy program. Also, the bill revises the employer-paid normal cost rates and unfunded actuarial liability (UAL) rates for the FRS, as determined by the July 1, 2013 Annual Valuation as necessary to adequately fund the costs of retirement benefits during Fiscal Year 2014-2015.

**Section 1** amends s. 112.363, F.S., to increase the employer paid contribution to the Retiree Health Insurance Trust Fund from 1.26 percent of gross compensation to 1.58 percent of gross compensation for each member of the Florida Retirement System.

**Section 2** amends s. 121.052, F.S., to increase the employer paid contribution to the Retiree Health Insurance Trust Fund from 1.26 percent of gross compensation to 1.58 percent of gross compensation for each member of the Elected Officers’ Class of Florida Retirement System.

**Section 3** amends s. 121.055, F.S., to increase the employer paid contribution to the Retiree Health Insurance Trust Fund from 1.26 percent of gross compensation to 1.58 percent of gross compensation for each member of the Senior Management Service Class of Florida Retirement System.

**Section 4** amends s. 121.071, F.S., to increase the employer paid contribution to the Retiree Health Insurance Trust Fund from 1.26 percent of gross compensation to 1.58 percent of gross compensation for each member of the Regular, Special Risk, and Special Risk Administrative Support classes of Florida Retirement System.

**Section 5** amends s. 121.71, F.S., to set the employer-paid contributions to the Florida Retirement System Trust Fund for each membership class of the FRS.

**Sections 6 and 7** provide findings that the bill fulfills important state interests.

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

#### **IV. Constitutional Issues:**

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

Subsection (a) of s. 18, Art. VII of the Florida Constitution provides that “no county or municipality shall be bound by any general law requiring such county or municipality to spend funds . . . unless the legislature has determined that such law fulfills an important state interest and unless: . . . the expenditure is required to comply with a law that applies to all persons similarly situated . . .”.

This bill includes legislative findings that the bill fulfills important state interests, and the bill applies to all persons similarly situated (those employers participating in the Florida Retirement System), including state agencies, school boards, community colleges, counties, and municipalities.

##### **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:**

**Florida Retirement System**

The aggregate employer contributions anticipated to be paid into the Florida Retirement System Trust Fund in Fiscal Year 2015-2016 will decrease by approximately \$34.4 million when compared to the employer contributions paid in Fiscal Year 2014-2015. However, the impacts on particular employer vary significantly based on whether the employers have members in the Special Risk Class or the Judicial Subclass. The impacts by employer group for Fiscal Year 2015-2016 are noted below.

<b>Employer Group</b>	<b>Impact on Contributions</b>
<b>State Agencies</b>	\$3.9 m
<b>Universities</b>	(\$2.7 m)
<b>Colleges</b>	(\$4.5 m)
<b>School Boards</b>	(\$60.5 m)
<b>Counties</b>	\$31.5 m
<b>Other</b>	(\$2.1 m)
<b>Total</b>	(\$34.5 m)

**Retiree Health Insurance Trust Fund**

With the enactment of this legislation, the revenues expected to flow into the Retiree Health Insurance Trust Fund will increase by approximately \$96.8 million annually. The increases by employer group for Fiscal Year 2015-2016 are noted below. With these increased contributions, the trust fund is not expected to deplete its reserves during the forecasted period.

<b>Employer Group</b>	<b>New Contributions</b>
<b>State Agencies</b>	\$14.8 m
<b>Universities</b>	\$4.3 m
<b>Colleges</b>	\$3.4 m
<b>School Boards</b>	\$43.3 m
<b>Counties</b>	\$25.8 m
<b>Other</b>	\$5.2 m
<b>Total</b>	\$96.8 m

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

None.

**VIII. Statutes Affected:**

This bill substantially amends the following sections of the Florida Statutes: 112.363, 121.052, 121.055, 121.071, and 121.71.

**IX. Additional Information:**

**A. Committee Substitute – Statement of 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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