



# The Florida Senate

Interim Project Report 2000-50

February 2000

Committee on Governmental Oversight and Productivity

Senator Jack Latvala, Chairman

## INFORMED EMPLOYEE CHOICES IN RETIREMENT INCOME SECURITY

### SUMMARY

Public and private employers worldwide constantly seek innovative ways of retaining and recruiting capable employees. This is no less true for public agencies in the State of Florida that must cope with a workforce which is entering retirement. Hiring for life may be a wave of the past and the altruism which accompanies public employment is no longer an exclusive motivator. Legislative debate has in the recent past concentrated on developing performance expectations in the public workplace. Along with that has come serious discussion of market-based incentive programs which can permit employees to competitively set their own careers on an equal basis with their employers. With more than 30 percent of the state operating budget in contracted programs, a direction has already been set for the deployment of state services outside of conventional methods of organization. The report describes the recent history of alternative pension plan discussions, establishes a framework for providing choice in a complex environment, and identifies issues which must be addressed in total workforce development and deployment.

### BACKGROUND

For the past several years the Florida Legislature has been presented with proposals for alternative pension plans for public employees. The current plan, the Florida Retirement System (FRS), is itself a relatively recent addition to the retirement sector. Founded in 1970 as an amalgamation of solvent and insolvent plans, this more than \$100 billion multi-employer plan provides guaranteed income security for the participant and survivors at retirement. In the parlance of the street it is a *defined benefit* plan, in which the employer as the owner assures the participant of an inflation-adjusted fixed benefit at retirement expressed as a percentage of final pay. This is by no means the only design type. Since 1984 faculty in the state university system, as well as managerial employees, have been

permitted to select alternative pension arrangements which are employee-owned. These *defined contribution* plans mimic corporate-type counterparts and allow the employee immediate benefit qualification, or vesting, but with personal, rather than employer responsibility, for retirement income assurance. The appropriateness of extending this choice to more of the 600,000 members of the FRS has become the focal point of contemporary discussions. The 1999 Florida Senate passed a bill, CS/CS/SB 356, which would have extended defined contribution plan choices to all members of its general pension class. While the bill received no further action, the House of Representatives did establish a framework through which interim discussions could proceed on the development of a consensus product. Central to that activity was the commissioning of a study designed to assess what values public employees brought to the issue. Most recently the Governor's recommended budget for the Fiscal Year 2001 endorsed continued legislative efforts in this area.

### METHODOLOGY

This report attempts to partially address the provisions contained in House Bill 1883 passed by the 1999 Florida Legislature calling for a review of the issues in pension choice. In doing so, the report uses information developed by the retirement staff of the Florida Department of Management Services, the investment management staff of the State Board of Administration, and related public and private sector sources to describe the benefit types.

### FINDINGS

The durability of a global economic recovery finishing its tenth year has impressed even optimists. With equity valuations at their historic peaks, long-term interest rates in their lowest ranges, and inflation well under historic trends, increased attention has turned to sustaining individual recovery. As increasingly larger parts of state-delivered service move from the public to

the private sector, so too has the notion that public services more closely emulate their private sector counterparts. Competitive procurement at the lowest price has evolved into larger discussions of competitive government, performance-based management and funding, delivering previously monopolistic services in a pluralistic economy, and transforming state agencies into service brokers rather than direct providers. As discussions turn to benefits and their administration individuals may find that committing a minimum of ten years' service to a single public employer to be less relevant than ever. With a fully funded pension plan, debate may now proceed on whether a retirement plan should serve only the employer's needs. Only recently has the development of a hybrid plan been suggested as a variation of even traditional private sector pension arrangements. In this design, a defined benefit plan incorporates both fixed and variable components. The employee receives the assurances of a fixed allocation, usually in excess of 60 percent, and may invest the remaining percentage in a group of funds that provide variable rates of return and risk. Such plans pose design considerations for equitable age treatment and under investment but do permit a customization of benefits as a function of career choice.

In any rethinking of the design or deployment of benefits, the relationship of one element to the other is critical. Following legislative initiatives, the Department of Management Services has delivered a plan for the integration of salary, training, and benefits changes for the workforce of the next generation. That plan interconnects the previously diverse discussions of compensation, choice, and benefits in an accountable, performance-based environment.

## RECOMMENDATIONS

There is already emerging consensus on the principles accompanying alternative choice. With the House of Representatives' desire to proceed with sensitivity to employees' needs and concerns, the following elements appear as central to the development of pension choice:

1. The choice should be **informed** with the employee given the assurance that all information affecting the decision is adequate, timely, and understandable .
2. The decision should be **unconstrained** such that an employee's desire for self-determination is not compromised by an employer's desire to off-load all benefit responsibility.
3. Alternative pension choices should be **fiscally neutral** to avoid selection bias which could undermine the employee's choice or produce unfunded liabilities for subsequent generations of taxpayers.
4. The choice package should be **equitable**, not only in terms of realizing an equivalent benefit to the legacy system at retirement, but also in treating women and low-wage earners, a majority of the membership, with the special sensitivity that accompanies the financial realities of their employment, compensation, and economic interests.
5. The plan should contain internal **checks and balances** for routine employee and employer oversight and from which a competitive procurement can be obtained to secure the best of class vendors and products at the lowest expense.
6. The plan should be **adaptable** so that employees find it easier to qualify for benefits earlier in their careers irrespective of interrupted or continuous public or private sector employment.
7. The plan should be **interdependent** such that it represents one of several co-equal elements in the development of a multifaceted public workforce infrastructure.

### COMMITTEE(S) INVOLVED IN REPORT *(Contact first committee for more information.)*

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### MEMBER OVERSIGHT

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