The Florida Senate

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Committee on Governmental Operations

SETTING THE 2009-2010 EMPLOYER CONTRIBUTION RATES FOR THE FLORIDA RETIREMENT SYSTEM

Statement of the Issue

The multi-employer Florida Retirement System provides annuitized defined benefit and equity defined contribution benefits to nearly one million active and retired members among its nearly one thousand participating units of government in Florida. It is the fourth largest plan in the Nation and one of the best funded. It has been consistently ranked at the top in terms of efficiency of administration. Investment management is overseen by the State Board of Administration; benefits payments are the responsibility of the Department of Management Services. The plan dampens the effect of wide swings in financial markets through the creation of multiple levels of checks and balances. The cumulative effect has been to stabilize rates and provide a modest level of benefits relatively immunized from the wide fluctuations associated with capital markets.

Discussion

All fifty states provide some form of post-employment retirement benefits for their officers and employees supplemental to Social Security. In the multi-employer Florida Retirement System (FRS), participating state and local government employers have pooled their resources for the provision of post-employment income. FRS membership is compulsory for state-level and constitutional entities but optional for statutory units. Public organizations typically tend to compensate employees more in terms of benefits than salary. This is due to the relatively unchanging dynamics of public expenditures - education, public safety, and social and health services - and the labor intensity associated with the inherent nature of the services themselves.

Since its creation in 1970 as the successor to the Teachers' Retirement System and three others, the FRS has come to embrace five separately constituted plans. Efficiency improves with scale, and local governments are joining the plan at the rate of three per month in partial recognition of its longer term savings to their own budgets. The plan dampens the effects of financial market volatility through several distinct but complementary mechanisms: the State Constitution requires pre-funding of benefit increases on a sound actuarial basis to avoid intergeneration risk transfer; assets and liabilities are averaged, or "smoothed" over five years to lessen the "feast or famine effect;" assets are invested in recognized financial markets in thirty-year cycles consistent with the expected normal career length of the workforce; and the assumptions used as the building blocks of the FRS – expected salary increases, assumed rate of return, and inflation – all reflect the modest expectations of maturing capital markets and an increasingly flat to declining hiring expectation among public employers generally. The Legislature's *Long Range Financial Outlook* issued September 10, 2008 further illustrated the gap between critical needs and funding realities and pointed to significant, growing employer obligations in health insurance and pension increases over the three-year horizon.

Recent financial events have underscored the durability of the financial model used to construct the FRS. The unprecedented volatility that has infused the equity and debt markets has made the patient capital of pension plans all the more valuable as a backstop. Pension plans as a financial component of a market economy are among the most efficient and prudent investors: they do not "day-trade," unreasonably speculate, or trade on their own accounts. They invest in infrastructure, market expansion, and the emerging technology of new economies.

The Senate professional staff recommends the setting of FRS retirement contribution rates that are consistent with the near-term financial outlook and do not obligate the plan for any further benefit expansion beyond that forecast period.