

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

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

BILL: CS/SB 820

SPONSOR: Fiscal Policy Committee, Senator Thomas and others

SUBJECT: State Employees

DATE: April 25, 2000 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Wilson</u>	<u>Wilson</u>	<u>GO</u>	<u>Favorable</u>
2.	<u>Hendon</u>	<u>Hadi</u>	<u>FP</u>	<u>Favorable/CS</u>
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____

I. Summary:

The bill authorizes the Department of Management Services (DMS) and the Board of Regents to contract with a private vendor for the development of a federally tax-sheltered plan for the deposit of accumulated annual and sick leave payments from terminating employees.

This bill creates an undesignated section of the Florida Statutes.

II. Present Situation:

State of Florida employees earn annual and sick leave on the basis of the personnel system in which they are employed. For most employees the earning occurs on a step-wise, progressive scale which affords higher leave credits with longer periods of continuous service. Management employees in the Senior Management Service Class are precredited with leave upon admission to that class which is prorated over the ensuing twelve months. Elected officers do not earn leave as their compensation accompanies the office held and not upon the performance of service during an established time period.

Under current law employees are immediately vested with all of the annual leave they accumulate and may cash out at employment termination up to a statutory maximum. For employees in the Career Service System and university support personnel this maximum is 240 hours; in the State University System it is 352 hours; in court management it is 360 hours; and in the Selected Exempt Service and other exempt classes it is 480 hours. Sick leave accumulates on an unlimited basis but terminating payment is permitted only upon the completion of ten or more years of employment with a State of Florida agency, with a maximum cash payment for 480 hours, pursuant to s. 110.122, F.S.

Individuals electing a final cash payment are paid at their last hourly rate times the number of eligible hours, less Social Security and withholding taxes. Employees may also roll-over their balances to one of several deferred compensation accounts under provisions of ss. 403(b) or 457

of the United States Internal Revenue Code. These transfers shield the terminating payments from withholding taxes but not Social Security deductions.

Senate Interim Report 2000-53, *Employee Incentives for Performance*, discussed other provisions of the Internal Revenue Code which provide government employers with the opportunity to shield additional employee income from federal taxation. Under one such program the State of Florida would contract with a private vendor for the deposit of accumulated leave balances in lieu of the receipt of taxable, cash payments.

III. Effect of Proposed Changes:

The DMS and the Board of Regents are authorized to contract for the procurement of a tax-sheltered plan for the payment of accumulated employee annual and sick leave upon employment termination which minimizes employee tax liability. The procurement must proceed through a Request for Proposals and responding parties may be required to provide product ratings on their market risk. All proposals must be examined by the State Board of Administration which shall advise the DMS and the Board of Regents. These plans shall be administered by the Department of Insurance.

Employees will be permitted to withdraw their funds within 30 days without penalty and shall be indemnified from adverse tax consequence by the plan administrator.

The DMS shall also contract for a similar plan for sick leave payments due participants in the Deferred Retirement Option Program (DROP). Methods of calculation and payment shall be determined by rule of the agency.

The effective date is July 1, 2000.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None. The bill affects State of Florida employees only.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

Because the issue relates to wages, hours, and terms and conditions of employment, the Department of Management Services, and the Board of Regents, on behalf of the State

University System, would be obliged under ch. 447, F.S., to inform the affected employee collective bargaining representatives about these provisions.

There are income limits established under federal law for the maximum shielding of income. Individuals may participate under multiple tax-shelter programs simultaneously, provided they do not exceed maximum allowable compensation limits of s. 415 of the Internal Revenue Code.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

The procurement will determine the extent and scale of imposed fees by the successful vendor company. These fees take various form, such as fixed and variable fund charges, administrative fees, annual plan charges or front/back loaded fees. For annuity accounts a vendor may impose a mortality expense subject to the contract document.

B. Private Sector Impact:

The bill would provide additional income to the successful vendor company, most probably in the form of fees imposed for services. An employee participant will be subject to the provisions of the provider contract document. Participants will be offered a selection of investment options for the allocation of their payments. Amounts withdrawn will be subject to taxation and the imposition of surrender charges, if any, by the provider company.

The employee defers federal income taxes payable in the individual's bracket amount and saves the 7.65 percent imposed by the Federal Insurance Contributions Act on all contributions to the qualified plan.

C. Government Sector Impact:

The bill would reduce the amount of employer taxes paid to the federal treasury, but would not impact state revenues as the amounts shielded are not subject to state taxation.

The Legislature does not appropriate specific funds to pay sick and annual leave for departing employees. Under the bill, the Department of Management Services would implement a plan that could exempt the state from paying Social Security taxes of 7.65 percent for annual and sick leave payments to departing employees (see table below). Most of the employees paid such leave balances are in the Career Service Class. The amount of such payments are most often under \$500 or over \$2,000.

If employees elect not to put their leave payout in the plan, the bill requires the state to hold them harmless for any penalties imposed by the IRS. Such penalties are typically imposed on those under the age of 55 and the cost of such penalties would be 10 percent of the amount withdrawn. Such costs could likely be absorbed by the savings accrued under the plan.

To implement the bill, the Department of Banking and Finance would have to re-program existing computer systems that pay the state's payroll. The cost of these changes has been estimated at over \$600,000.

Amount of Leave Payouts by Pay Plans for 1999				
Pay Plan	Annual Leave	Sick Leave	Total Leave	7.65 Percent
Career Service	\$19,366,752	\$6,028,962	\$25,395,714	\$1,942,772
Board of Regents	\$6,649,018	\$1,327,703	\$7,976,721	\$610,219
Exempt Employees	\$4,421,881	\$856,465	\$5,278,346	\$403,793
State Courts	\$1,992,933	\$328,135	\$2,321,068	\$177,562
Senior Management	\$1,819,630	\$709,300	\$2,528,930	4,193,463
Other Pay Plans	\$1,091,477	\$350,380	\$1,441,857	4,110,302
Total	\$35,341,691	\$11,743,407	\$47,085,098	\$3,602,010

VI. Technical Deficiencies:

None.

VII. Related Issues:

Retiring employee-members of the FRS would not be adversely affected by this roll-over as the value of their accumulated annual leave balances is determined prior to transfer. Up to 500 hours may be added to the employees highest five years' of income to enhance, or "spike," the final benefit amount. University faculty and management personnel who participate in the optional annuity program in lieu of FRS membership are not affected by this spike as they have individual contracts with their provider companies.

Employee insurance premiums are already federally tax shielded and they may individually participate in pre-tax reimbursement accounts for out-of-pocket medical and child care expenses.

VIII. Amendments:

None.