

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

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

BILL: CS/SB 1650

SPONSOR: Appropriations Committee and Senator Wise

SUBJECT: Retirement

DATE: March 11, 2004 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Wilson</u>	<u>Wilson</u>	<u>GO</u>	<u>Favorable</u>
2.	<u>McVaney</u>	<u>Hayes</u>	<u>AGG</u>	<u>Fav/CS</u>
3.	_____	_____	<u>AP</u>	<u>Withdrawn: Fav/CS</u>
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

The bill revises both the defined benefit and defined contributions plans administered, respectively, by the Department of Management Services and the Board of Administration. Specifically, the bill provides the determination of the beneficiary of a deceased member of the defined contribution plan, defines “retiree” for purposes of the defined contribution plan, allows de minimus accounts to be cashed out, changes the dates of election to participate in the defined contribution plan, and revises the investment guidelines for the funds in the defined benefit plan.

This bill substantially amends the following sections of the Florida Statutes: ss. 112.363, 121.4501, 121.591, 121.78, 215.47, 215.475, and 215.5601.

II. Present Situation:

The Florida Retirement System (FRS) is a multi-employer, non-contributory pension plan providing retirement income benefits to the more than 600,000 active and 200,000 retired members and beneficiaries of its more than 800 employers. Originally established in 1970 as the successor to the Teachers’ Retirement System (TRS) and the State and County Officers’ and Employees’ Retirement System (SCOERS), the FRS is today an amalgamation of four previously separate pension plans. Benefit payments are administered by the Department of Management Services through its Division of Retirement while investment management is undertaken by the Board of Administration. Established as a 401(a) government plan under the Internal Revenue Code, its benefits are exempt from federal taxation until received by the employee.

As a defined benefit plan, the FRS “Pension Plan” provides retirement income expressed as a percent of final pay. Participants accrue retirement credits based upon their eligibility in one of

several membership classes. The retirement benefit at normal retirement age is calculated by multiplying the member's final average compensation (the average salary over the five highest fiscal years of earnings, adjusted by up to 500 hours of annual leave) by a factor equal to the number of years of creditable service multiplied by the accrual rate for the membership class. The accrual rates range from 1.60 percent for the Regular Class to 3.33 percent for the Justices and Judges subclass of the Elected Officers Class. For most membership classes, normal retirement occurs at the earlier of thirty years of service or age 62. For public safety employees in the Special Risk Retirement Class, normal retirement occurs at the earlier of twenty-five years of service or age 55. Members seeking early retirement receive a five percent reduction in the benefit for each year below their normal age threshold. All membership classes permit enrollment in a Deferred Retirement Option Program (DROP) under which a participant may extend employment for an additional five years - eight years for instructional personnel in district school boards - and receive a lump sum benefit at a fixed rate of interest for that supplemental service. Enrollment in DROP nominally requires the participant to serve the employer with a deferred resignation from employment at the end of the period. The defined benefit plan includes a fixed, annual cost-of-living adjustment of three percent.

The 2000 Legislature enacted sweeping changes to the FRS by creating the Public Employees Optional Retirement Program (Part II of ch. 121, F.S.), an alternative defined contribution or "Investment Plan" for its members. While a defined benefit plan provides an annuitized monthly benefit expressed as a percent of final pay, a defined contribution plan gives a member an equity interest in the employer's payroll contributions made on the member's behalf and the associated earnings, although it does not assure a guaranteed result. Generally, a defined benefit plan rewards career employment as its annuitized benefits become more generous with longer service. A defined contribution plan works best for those who value public service for only short employment experiences or who prefer to manage their own investments. DROP enrollment is unavailable for the Investment Plan due to the incompatibility of plan designs. During the initial enrollment period for the defined contribution plan, each active member of the FRS was given the option to enroll in the new defined contribution plan or maintain participation in the defined benefit plan. After the initial enrollment period, each employee is granted an additional opportunity to change participation between the plans.

All state employees are provided with the opportunity within the first thirty days of retirement to elect to receive post-retirement health insurance coverage and, along with it, a financial stipend to cushion the premium burden. The monthly retiree health insurance subsidy is equal five dollars for each year of creditable service, not to exceed \$150 per month. Current law requires retired members of the state health insurance program not eligible for the Medicare Program to pay a premium equal to the total premium paid on behalf of an active employee (both the employee's and the employer's shares of the premium).

III. Effect of Proposed Changes:

Section 1. Section 112.363, F.S., is amended to presumptively establish the spouse at the time of the retiree's death as the designated beneficiary for the purposes of the health insurance subsidy, unless otherwise designated subsequent to the participant's most recent marriage.

Section 2. Subsections (2), (4), (10), and (15) of s. 121.4501, F.S., are amended, as follows:

Subsection (2) defines “retiree” for the purposes of the Investment Plan as a former participant of the Investment Plan who has terminated employment and taken a distribution, other than a minimal account distribution of less than \$5000.

Subsection (4) is amended to change the times frames for enrollment in the Investment Plan for those on leave of absence. The current time frame of 90 days following conclusion of the leave of absence is changed to the last business day of the fifth month following the month the leave of absence concludes. Amendments also change the effective date provisions for the second election of plan changes from the currently undefined period to the newly defined month following the effective date of the plan selection.

Subsection (10) places an obligation on all member employers of the FRS to communicate the existence of the two enrollment choices as part of their personnel management function using educational materials supplied by the Board of Administration and the Department of Management Services.

Subsection (15) changes a cross reference made to the Code of Federal Regulations promulgated by the United States Department of Labor under the statutory provisions of the Employee Retirement Income Security Act (ERISA) of 1974. The ERISA legislation exempts government plans but Florida has elected to have both the Pension Plan and the Investment Plan adhere to its provisions. The amendment to this subsection allows the Board of Administration to disclose to Investment Plan participants the actual institutional fees charged by its investment providers, which are less than those disclosed in similar prospectus filings issued to retail customers of the same funds.

Section 3. Subsection 121.591(1), F.S., is amended to permit both the Board of Administration and the Department of Management Services to cash out or transfer to a successor custodian an account with a minimum balance of \$ 5000 or less for persons who have terminated employment for at least six months. Subsection (2) is also amended to provide that the survivor of a disabled Investment Plan member shall receive only the remaining account balance in the plan in which membership was established. It eliminates the circumstance in which a survivor can claim a benefit under both systems with membership in only one.

Section 4. Section 121.78, F.S., is amended to require the public employer to make financial adjustments to the Board for payroll contribution rates it has entered in error and to make the employee whole for market losses resulting from late contributions. Terminated participants are also required to return contributions erroneously made by the employer although the Board of Administration and the Department of Management Services shall not experience any gain or loss as a result of these corrections.

Section 5. Section 215.47, F.S., is amended to permit the Board of Administration to invest in fixed-income obligations issued by foreign governments or their agencies if they are rated investment grade by at least one nationally recognized rating agency. In addition, the costs of acquisition of private equity interests will be included in the overall costs of the investment.

Section 6. Section 215.475, F.S., is amended to provide corrected nomenclature reference to the “Defined Benefit Plan” as the one to which its Investment Policy Statement on permitted and excluded investments applies.

Section 7. Section 215.5601, F.S., is amended to provide a similar terminology reference to the Lawton Chiles Endowment Fund, as described in s. 6, above.

Section 8. The act takes effect July 1, 2004.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

There are some 55,000 terminated FRS employees with vested pension rights. Under current law, these FRS members may change pension plans only upon resumption of employment for one year. Such former employees who do not expect to resume covered FRS employment would be able to switch to the Investment Plan and realize an immediate equity recognition in their individual accounts.

C. Government Sector Impact:

The Board of Administration has reported that some public employers have failed to advise their employees of the two pension choices available in the workplace. Some other employers have either not been distributing the official descriptive material relating to this choice or directing, or “spinning,” information from other providers not a part of the FRS product offerings.

Chapter 215, F.S., lists the type of investments that are permitted for the FRS. Current law provides two different statements on the appropriateness of investments in products that are not dollar-denominated, thus limiting the Board of Administration’s discretion from debt or equity exposure held in other currencies. While dollar- and non-dollar

language is contained in the authorization granted by s. 215.47, F.S., the most recent change added dollar-denominated as the modifier.

The most recent large-scale defaults on publicly issued debt have been the Soviet-era debt of Russia (1988, \$40 billion) and Argentina (2001, \$90 billion), and other lesser amounts by Liberia and Zimbabwe. Iraq's debt, including unserviced war reparations, exceed these combined amounts. In the case of Argentina, the country revalued its currency in pesos rather than denominated dollars in an attempt to service its sovereign public and private debt. That defaulted debt is now in excess of \$99 billion.

There are three major debt ratings services: Standard & Poor; Fitch; and Moody. Each uses a combination of letters and numbers to assign a credit worthiness to the debt issuance. Investment grade, the only suitable rating for investment plan fiduciaries, has its minimum level at BBB or its equivalent.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
