

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.)

Date: March 13, 1998

Revised: 03/17/98

Subject: Fiduciary Duties of Retirement Trustees

	<u>Analyst</u>	<u>Staff Director</u>	<u>Reference</u>	<u>Action</u>
1.	<u>Wilson</u>	<u>Wilson</u>	<u>GO</u>	<u>Fav/1 amendment</u>
2.	<u></u>	<u></u>	<u>WM</u>	<u></u>
3.	<u></u>	<u></u>	<u>RC</u>	<u></u>
4.	<u></u>	<u></u>	<u></u>	<u></u>
5.	<u></u>	<u></u>	<u></u>	<u></u>

I. Summary:

The Joint Resolution proposes to amend section 18, Article X, State Constitution, to prescribe the specific fiduciary duties of public retirement systems and their trustees.

II. Present Situation:

Part VII of Chapter 112, Florida Statutes, *The Florida Protection of Public Employee Retirement Benefits Act*, prescribes minimum compliance standards for publicly funded pension systems in the State. The autonomous Division of Retirement in the Department of Management Services is given oversight responsibility for the assurance of minimum thresholds of operating performance of these plans. Among the principal standards to which such plans must adhere are:

- ▶ A description of plan features and benefits that is written in non-technical language;
- ▶ Specification of grievance procedures to be followed for a plan member to challenge a benefit determination;
- ▶ Non-discrimination in the administration of benefits on the basis of demographic factors unrelated to age or disability.

There are several hundred different public sector pension plans and plan types in Florida which fall into the following broad categories:

- ▶ **The Florida Retirement System [FRS]** - This multi-employer pension plan is the Nation's third largest and comprises 800 state, county, municipal, and special district governments. It is administered by the Division of Retirement directly for the purposes

of benefit payments while its investments are managed by the State Board of Administration. Participation is compulsory for constitutional entities and optional for statutorily created governmental units.

- ▶ **Municipal Firefighters' Pension Trusts** - These plans are governed by individual boards of trustees and receive supplemental funding through insurance premium tax distributions provided in Chapter 175.
- ▶ **Municipal Police Officers' Retirement Trusts** - Like the ch. 175, F.S., plans for firefighters, the ch. 185, F.S., police plans have independent boards of trustees and also receive funding through insurance premium taxes which are remitted to the plans through the Division of Retirement.
- ▶ **General Local Government Plans** - Individual local governments, which otherwise are not members of the FRS, may create their own pension systems for their own non-sworn employees.
- ▶ **Supplemental Plans** - there are additional varieties of other supplemental plans qualified under the Internal Revenue Code. For sworn employees the most common type is a share plan but all employers have some provision for a 457, or deferred compensation plan, in which unmatched employee contributions can received tax-sheltered status until retirement.
- ▶ **Optional Annuity Plans** - Some public employers give designated management personnel a choice of participation in either their prototype defined benefit plans or enrollment in a portable, defined contribution plan. Such plans provide equivalent payroll contribution rates, offer immediate vesting, and provide personal ownership but do not promise the member any fixed cash or annuitized benefit at retirement. In this alternative arrangement the participant acts as a personal investment authority.

Art. X, s. 14, State Constitution, requires all public sector retirement plans to be pre-funded on an actuarial sound basis so that the financial consequence of paying for present benefits is not improperly transferred to future generations. The significance of this provision stems from the creation of the FRS in the early 1970s as a means of preventing the since closed Teachers' Retirement System (TRS) from a default on its obligations. Insufficient employer contributions were made to the TRS from prior generations of employers and employees and as the post-World War II retiree pool expanded in the late 1960s the specter of default loomed large. The FRS was created to incorporate the potentially insolvent TRS along with two other solvent but smaller pension systems. About 80 percent of the unfunded liability of the FRS can be attributed to the prior TRS. Only in the last several years has the escalating unfunded obligation peaked and begun to fall. From a high of some \$17 billion four years ago the actuarial deficit has been reduced to some \$5.4 billion this biennium. It is expected that this liability will be fully eliminated within four years at assumed or better rates of investment return and nominal salary growth.

Federal legislation, the Employee Retirement Income Security Act (ERISA), governs the composition and standards of private sector pension plans. Its provisions are not applicable to public sector plans although Florida adopts its more comprehensive standards for the conduct of the FRS by statute.

III. Effect of Proposed Changes:

The Joint Resolution creates a new s. 18, Art. X, State Constitution, to provide that all public sector pension plans shall be governed by three objectives:

- They shall hold all of their investments in trust for the exclusive benefit of members and beneficiaries;
- They shall ensure that no part of the trust's principal or income is used for any purpose other than the payment of benefits and plan expenses;
- All plans shall be governed by sound actuarial objectives to include the receipt of reports prepared by enrolled and competent actuaries.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

Section 18, Art. VII, State Constitution, excuses counties and municipalities from adhering to certain state laws which provide unfunded financial mandates upon them in certain defined circumstances. This Joint Resolution would amend the Florida Constitution, and would not, therefore, appear to fall under the provisions of Article VII.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

It is unknown at present whether the effective adoption of ERISA standards for all public pension systems would precipitate technical or substantive compliance issues upon some plans. It would have no effect upon the FRS since it adheres to these optional higher standards already.

V. Economic Impact and Fiscal Note:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

None.

C. Government Sector Impact:

As discussed above, any technical or substantive compliance issues would have to be determined individually by each plan board of trustees. The scale of this is unknown at present and will require individual actuarial review in conjunction with the periodic valuations required of such plans pursuant to part VII of ch. 112, F.S.

Since there will be a general election held in November 1998, there will be no additional costs attendant to adding the provisions of this resolution to the existing ballot provisions already proposed by the Constitutional Revision Commission.

VI. Technical Deficiencies:

Use of the term “competent” as a modifier of the qualifications of an actuary poses an awkward circumstance. Enrollment as a member in good standing in a recognized professional actuarial society would presume credentialing and competence. The absence of competence itself may be judged on a performance basis only *after* the fact of an engagement in which there has been a material departure from accepted standards of performance.

VII. Related Issues:

The substance of this bill was introduced before the Constitutional Revision Commission but, as yet, has not received final approval.

VIII. Amendments:

#1 by Governmental Reform and Oversight:

Deletes specific reference to the term “competent” as a modifier of an enrolled actuary.