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 1026

SPONSOR: Governmental Oversight and Productivity Committee and Senators Silver and Latvala

SUBJECT: Florida Retirement System

DATE: March 24, 2000 REVISED: 03/27/00

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Wilson	Wilson	GO	Favorable/CS
2.	Hendon	Hadi	FP	Fav/2 amendments
3.				
4.				
5.				

I. Summary:

The bill changes from five years to three years the time period for averaging final compensation for computation of a final pension benefit under the Florida Retirement System (FRS). It provides a uniform level of five years for vesting all classes of membership in place of the existing three vesting periods of seven, eight, and ten years. It increases the accrual rate for active members only of the Special Risk Class for periods of service occurring between 1978 and 1993. Additionally, the bill provides special risk retirement class coverage for pilots of fixed wing aircraft, and Senior Management Service Class coverage for assistant state attorneys, assistant statewide prosecutors, and assistant public defenders. The bill also provides for the development of a retirement rate stabilization mechanism to prevent future cyclical variations in the payroll contribution rates charged member employers. The bill funds the benefit increases by an increase in the payroll contribution rates which are later offset by a recognition of ten percent of the accrued actuarial surplus and a one-time deduction of monies from the surplus to fund repurchase of special risk upgrade time.

This bill substantially amends sections 121.021, 121.0515, 121.052, 121.053, 121.055, 121.081 121.091, 121.1115, 121.1122, 121.031, and 121.121, Florida Statutes.

II. Present Situation:

The FRS is a multi-employer, non-contributory, defined benefit pension plan providing an annuitized benefit to the some 600,000 active and 175,000 retired members of its 800 public employer members. Its employee participants are grouped within seven classes or subclasses of membership with varying terms of vesting and normal service. For most members benefits are earned after the service of ten creditable years and a full, normalized retirement occurs at the sooner achievement of 30 years' service or age 62. Members of all classes are permitted to participate in a retirement deferral program for up to five additional years in exchange for a full or partial cash distribution for those periods of extra service.

The Special Risk Retirement Class encompasses some 55,000 state, county, and municipal law enforcement, firefighter, correctional officer and emergency medical technician members. It values each year of service at three percent, which, when multiplied times the years of service in excess of ten and the average of the best five years of compensation and accrued leave, yields a final pension benefit. A normalized benefit occurs at the sooner achievement of age 55 or twenty-five years' of service. For a number of years beginning in 1978 this percentage accrual rate was reduced to two percent and, when subsequently adjusted upward, was restored to its original three percent by 1993.

Average final compensation (AFC) is computed by law as the average of the five highest fiscal earning years, plus accrued annual leave not to exceed 500 hours, divided by 60 months. For state employees only, this maximum leave accrual is set at 480 hours.

Managerial positions are enrolled in the Senior Management Service Class which values each year of creditable service at two percent. Members of this class are permitted to enroll in the FRS or receive an identical state contribution to a personally owned defined contribution account in lieu of membership.

Rotor craft pilots with firefighting responsibilities are already enrolled in the Special Risk Class as the craft are engaged in the active suppression of fires at low altitudes. Fixed-wing aircraft operate at higher altitudes and provide surveillance services only.

III. Effect of Proposed Changes:

Sections 1, 3, 4, 6, 8, 9, and 10. The bill changes the definition of the average final compensation from the average of the five highest to the average of the three highest fiscal years of compensation. In addition, the bill changes the number of years of credible service from ten to five years for members of the FRS.

Section 2. Pilots of fixed-wing aircraft with firefighting responsibilities in the Department of Agriculture and Consumer Services are enrolled in the Special Risk Class of the FRS.

Section 5. The bill includes assistant state attorneys, assistant statewide prosecutors, and assistant public defenders in the Senior Management Service Class in the FRS.

Section 7. The bill also retroactively reinstates a three percent accrual rate for all periods of special risk service between 1978 and 1993 for those members who have not yet retired.

Section 11. The bill revises the contribution rates for the various member classes in the FRS in order to fund the costs for changes in vesting requirements and changes in the calculation of the average final compensation.

Section 12. The bill funds the retroactive reinstatement of the accrual rate special risk service between 1978 and 1993, the changes in the vesting requirements, and the computation of the average final compensation by a one-time lump sum payment from the excess in the FRS Trust Fund.

Section 13. The bill recognizes a ten percent surplus in the FRS trust fund, and applies this surplus recognition to reduce overall retirement rates for the ensuing fiscal year.

Section 14. The bill reduces the contribution rates for the member classes in the FRS.

Section 15. The bill calls for the development of a retirement rate stabilization mechanism using the professional actuarial expertise of the State Board of Administration and the Division of Retirement.

Section 16. The bill finds a proper and legitimate state purpose in the revisions to the FRS and declares that the bill serves an important state interest.

Section 17. The bill provides an effective date of July 1, 2000.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

Because the FRS is a multi-employer pension plan, the effects of this bill extend to all local government employers with members of the Special Risk Class as employees. The bill provides an *Important State Interest Clause* to address the issues raised by that impact and the effect of Art. VII, s. 18, State Constitution, on local government unfunded mandates.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

The bill provides the necessary rate adjustments to fund the benefit increases in compliance with the actuarial letters issued by the FRS external actuarial consulting firm to effect compliance with Art. X, s. 14, State Constitution, and Part VII of ch. 112, F.S.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

The bill will pass along to all employer members of the FRS an adjustment to their statutory payroll costs in order to fund the enhancement of the proposed benefit changes. The amount of this change is noted below. In all cases the changes produce lower payroll costs than is currently experienced.

B. Private Sector Impact:

Membership in the Senior Management Class of the FRS affords participants the opportunity to subscribe to one of several private annuity providers and share in personal ownership in a defined contribution pension plan in lieu of FRS membership. Participants making this choice will provide additional funds to their selected provider and will personally pay any fees or administrative expenses imposed through their contract.

C. Government Sector Impact:

On March 14, 2000, the FRS consulting actuarial firm of Milliman and Robertson issued a letter opinion on program changes to the benefits payable under the pension plan in response to a legislative request. The letter amended a previous report on the same subject by incorporating the results of a morbidity and mortality experience review of plan participants. Expressed as a percentage of payroll, the changes to AFC would cost an additional 1.15 percent. The employer’s retroactive repurchase of enhanced credit in that same class to all active members would cost some $804 million if deducted one time from the FRS surplus of some $9.22 billion. As a percentage of payroll, the service repurchase would be the equivalent to a 3.69 percent payroll increase for the Special Risk Class alone. The cumulative effect of the changes effected by the bill can be expressed as follows:

Cumulative Effects of Contribution Rate Changes in CS/SB 1026

Entering composite rate from FY 99-00	10.55
Adjustment for experience study	.36
Composite Rate, including experience	10.91
Addition for 5-year vesting	.56
Addition for 3-year AFC	.59
Less Recognition of 10% of Surplus	3.43
Adjusted Composite Rate for FY 00-01	**8.63**

In its present form the bill does not specifically address the recognition of the morbidity and mortality experience study prepared on June 30, 1998. This study suggests an additional contribution rate increase equivalent of .36 percent, or the use of some $73 million of additional FRS surplus. The Legislature is not obligated to recognize this study. A method of taking this into account is suggested below.

The transfer of the assistant state attorney, statewide prosecutor, and public defender positions to Senior Management Class in the FRS has a fiscal impact of $1.55 million for FY 00-01. These positions already enjoy the expanded personnel benefits package approved and funded by a prior Legislature. Additional expense associated with the effect of the bill on employees of the Department of Agriculture and Consumer Services is, likewise, unbudgeted.

Unless otherwise funded by a specific appropriation these amounts will have to be assumed within the payroll costs structure of the named agencies within budgeted funds. No contribution rate effect of this upgrade, other than that noted above, is presented.

By law and policy the FRS undergoes an annual valuation by outside actuaries which must be confirmed through a second, separate review. This latter requirement directs the confirmatory opinion to be issued to the legislative branch of state government. The original valuation was prepared by Milliman and Robertson and received in late 1999 for the plan year ending June 30, 1999. The second confirmatory opinion was issued February 4, 2000, by the actuarial firm of Buck Consultants to the Office of Program Policy and Governmental Accountability.

Costs associated with the development of a retirement contribution rate stabilization mechanism can be assumed within the normal actuarial expenses incurred by the Division of Retirement and the State Board of Administration.

VI. Technical Deficiencies:

None.

VII. Related Issues:

A March 14, 2000, letter from the consulting actuaries for the FRS, Milliman and Robertson, discussed a number of other actuarial consequences of benefit changes. Contained in that report were discussions of the effects to members of the Regular Class of opting out of the FRS and purchasing their own defined contribution retirement plan with a fixed contribution rate of 10 percent.

That letter opinion also suggested that at assumed rates of investment return the use of the surplus would extend the over funding status of the FRS an additional twelve years.

Gains and losses to the FRS are amortized over a thirty year cycle. Two key assumptions used in the determination of a rate structure, other than those fixing the elements of the retirement classes themselves, are an assumed investment return of 8 percent and an overall salary increase of 6.25 percent, graded by age and years of service.

Because the FRS is noncontributory by employees, unvested members who fail to qualify for benefits at retirement have their contributions forfeited to the plan. This acts as a suppressant to higher plan costs. Contribution rates are allocated uniformly over all age groups in an actuarial method known as entry age normal.

The decision of how to recognize the experience study can be addressed in either an addition to the composite contribution rate or by recognition of a one-time deduction from the net accrued actuarial surplus. Should the latter be the chosen method, additional provision in the bill, or in the appropriations act or other implementing legislation, would be sufficient.

VIII. Amendments:

#1 by Fiscal Policy:
Recognizes the results of the 1999 actuarial experience study and funds increased costs for fiscal year 2000-2001 by a one time lump sum payment from the excess assets of the Florida Retirement System Trust Fund.

#2 by Fiscal Policy:
Provides appropriations from General Revenue for funding the costs of adding assistant state attorneys, assistant public defenders, and assistant statewide prosecutors to the Senior Management Service Class of the Florida Retirement System.