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HOUSE OF REPRESENTATIVES
FISCAL RESPONSIBILITY COUNCIL
ANALYSIS

BILL #: CS/HB 807
RELATING TO: Florida Retirement System
SPONSOR(S): Fiscal Responsibility Council Representative(s) Fasano
TIED BILL(S):

ORIGINATING COMMITTEE(S)/COUNCIL(S)/COMMITTEE(S) OF REFERENCE:

- (1) STATE ADMINISTRATION YEAS 5 NAYS 0
- (2) FISCAL POLICY & RESOURCES YEAS 10 NAYS 0
- (3) FISCAL RESPONSIBILITY COUNCIL YEAS 25 NAYS 0
- (4)
- (5)

I. SUMMARY:

The Public Employee Optional Retirement Program (PEORP), is an optional defined contribution retirement program, within the Florida Retirement System (FRS). The plan is non-contributory, meaning the employer pays the full cost of the retirement benefit. Public employees have the opportunity to choose to participate in either the defined benefit retirement program or the defined contribution program.

This bill:

- establishes a disability benefits program under the PEORP;
- synchronizes the due dates for employer contributions and accompanying payroll data under the FRS Pension Plan and the FRS Investment Plan;
- conforms second choice election options for local government employees to the options available to other employees;
- changes the dates for the present value calculations;
- updates contribution rates for the FRS Investment Plan disability program;
- amends provisions related to death benefits payable under the FRS Investment Plan to require spousal notification whenever the designated primary beneficiary is someone other than the spouse;
- updates certain distribution provisions to conform to recent law changes; and
- modifies the SUSORP to allow a broader range of benefit distributions.

The bill is effective July 1, 2002.

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II. SUBSTANTIVE ANALYSIS:

A. DOES THE BILL SUPPORT THE FOLLOWING PRINCIPLES:

- | | | | |
|-----------------------------------|---|--|---|
| 1. <u>Less Government</u> | Yes <input type="checkbox"/> | No <input checked="" type="checkbox"/> | N/A <input type="checkbox"/> |
| 2. <u>Lower Taxes</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 3. <u>Individual Freedom</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 4. <u>Personal Responsibility</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 5. <u>Family Empowerment</u> | Yes <input checked="" type="checkbox"/> | No <input type="checkbox"/> | N/A <input type="checkbox"/> |

This bill creates a disability benefit within the PEORP. However, this benefit is necessary to create a benefit package in the PEORP that is equivalent to the benefit package in the defined benefit program.

B. PRESENT SITUATION:

The Public Employee Optional Retirement Program (PEORP)

Chapter 2000-169, L.O.F., created s. 121.4501, F.S., which regulates an optional defined contribution retirement program, the Public Employee Optional Retirement Program (PEORP), within the Florida Retirement System. The plan is non-contributory, meaning the employer pays the full cost of the retirement benefit. Public employees have the opportunity to choose to participate in either the defined benefit retirement program or the defined contribution program.

The PEORP is administered by the Trustees of the State Board of Administration (SBA).

Unlike the defined benefit retirement program, the PEORP offers retirement payments that are not fixed for a lifetime. Rather, a participant may elect to receive the benefits in a lump-sum, in a lump-sum distribution that is rolled over to another qualified investment, or in periodic distributions. However, both plans are specifically regulated under the Internal Revenue Code.

Chapter 2000-169, L.O.F., provides a phase-in schedule for current employees to elect participation in the optional program. Employees of state entities are given the option to join the optional program between June 1, 2002, and August 31, 2002; employees of education-related employers between September 1, 2002, and November 30, 2002; and, other local government employees between December 1, 2002, and February 28, 2003.

Disability

Disability Benefits under the Public Employee Optional Retirement Program

Subsection 121.4501(16), F.S., provides:

For any participant in the optional retirement program who becomes totally and permanently disabled, as defined in s. 121.091(4)(b), the participant shall be entitled to receive those moneys that have accrued in his or her participant account. It is the intent of the Legislature to design a disability benefit for participants of the optional program similar to those disability benefits afforded

defined benefit program members. The department is directed to study the potential options of such coverage, including self-insurance and commercial coverage, the alternative methods of administering such benefits, and the fiscal impacts on the employees and employers, and to make recommendations to the Legislature by January 15, 2001.

Section 121.571, F.S., requires employers of participants of the Public Employee Optional Retirement Program to contribute funds to the Public Employee Disability Trust Fund. These funds will be used to provide disability coverage for participants in the optional retirement program. The statutory contributions are based on the participant's gross monthly compensation and are noted below:

Regular Class	0.39%
Special Risk Class	1.25%
Special Risk Administrative Support Class	0.73%
Elected Officers' Class	
Legislators	0.61%
Governor, Lt. Governor, Cabinet	0.61%
State Attorneys, Public Defenders	0.61%
Justices, Judges	1.45%
County Elected Officers	0.86%
Senior Management Service Class	0.50%

Disability Benefits under the Defined Benefit Program

Generally

The Florida Retirement System defined benefit program protects the accrued benefits of participants who become totally and permanently disabled during active employments. Participants may be eligible for either regular disability or in-line-of-duty disability.

Regular disability is granted for an illness or injury from natural causes or an accident not related to employment. Currently, to be eligible for regular disability, a member must complete 5 to 8 years of creditable service to be entitled to a monthly disability benefit. The minimum annual regular disability benefit is 25 percent of the member's average final compensation.

Disability in line of duty is defined under s. 121.021(13), F.S., as "an injury or illness arising out of and in the actual performance of duty required by a member's employment during his or her regularly scheduled working hours or irregular working hours as required by the employer." Unlike regular disability, a member is eligible for in-line-of-duty disability benefits from the first day of employment. Special Risk Class members receive a minimum annual in-line-of-duty disability benefit of 65 percent of average final compensation. For members of other classes of FRS, the minimum in line of duty disability benefit is 42 percent of average final compensation.

Benefit Payout Options

If a member is approved for disability retirement benefits, the member is permitted to choose one of four benefit options. These options include:

Option 1 – a monthly benefit payable for the member's lifetime and continued disability. Upon the member's death, the monthly benefit will cease and the beneficiary is entitled to receive a refund of any contributions the member paid which exceed the amount received in benefits. This option maximizes the lifetime benefit.

Option 2 – a reduced monthly benefit payable for the member's lifetime and continued disability. If the member dies after 10 years of retirement, no benefits are payable to the beneficiary. If the member dies within 10 years of retirement, the beneficiary continues to receive the monthly benefit until completion of the 120-month period.

Option 3 -- a reduced monthly benefit payable for the member's lifetime and continued disability. Upon a member's death, the member's joint annuitant, if living, receives a lifetime monthly benefit in the same amount as the member had received. Special rules apply if the joint annuitant is not the member's spouse.

Option 4 – a reduced monthly benefit payable while the member is disabled and both the member and joint annuitant are living. Upon the death of either the member or the joint annuitant, the monthly benefit is reduced to 2/3 of the monthly benefit received while both were living. Special rules apply if the joint annuitant is not the member's spouse.

Mercer Study of Disability Benefits

The Department hired William M. Mercer, Inc. (Mercer) to conduct the disability study and to make recommendations. The Mercer recommendations were published in "Study of Disability Benefits Per HB 2393" and are summarized below:

1. In order to assure that equitable disability benefits are provided to all participants, the account balance transferred for the Florida Retirement System defined benefit plan should be used first to pay benefits to disabled PEORP participants.
2. The state should administer PEORP and the FRS defined benefit plan on an internal basis to realize substantial savings over the cost of external administration. Mercer estimated the cost of internal administration at \$150,000 annually and the cost of external administration at \$7-14 million annually.
3. The state should continue to self-insure the disability retirement program, thus avoiding insurance company risk, profit loads and state premium taxes.
4. The state should fund PEORP through a new Disability Benefit Trust, which offers the benefits of self-insurance and plan asset protection.

Time of Payment of Retirement Contributions

Under the defined benefit plan, employers must remit retirement contributions to the department no later than the 20th day of the month immediately following the month during which the payroll period ended. If the contributions are remitted late, a delinquent fee is assessed equal to 1% of the late contributions for each month or portion thereof that the contributions are late. (see s. 121.071, F.S.)

Under the defined contribution plan, the employers must remit retirement contributions by the 5th day of the month immediately following the month during which the payroll period ended. (see s. 121.571(7)). No penalties are specified for late payment of these contributions.

PEORP Accumulated Benefit Obligations

Section 121.4501(3), F.S., sets out the eligibility of participants for the PEORP. Each participant is permitted to elect to transfer the present value of the participant's accumulated benefit obligation (ABO) under the defined benefit plan to the defined contribution plan. The ABO is estimated based

on hypothetical service credit and average final compensation for a member on the eve of that member's PEORP election window opening. For state employees, the estimate date is May 31, 2002; for school district employees, the estimate date is August 31, 2002; and for local government employees, the estimate date is November 30, 2002.

Death Beneficiary

Under the defined benefit plan and the defined contribution plan, a participant is not required to notify a spouse if the participant designates someone other than the spouse as the death beneficiary.

State University Optional Retirement Program

In 1983, the Legislature enacted the State University Optional Retirement Program. This program is a defined contribution plan in which certain executive personnel and faculty members of the State University System may choose to participate in lieu of participation in the Florida Retirement System. This program allows for immediate vesting in both employer and employee contributions. Currently, four vendors provide the investment products for this program. These vendors are Security First Group; TIAA-CREF; VALIC; and Great American Reserve. Retirement benefits accrued under this program must be paid out in the form of an annuity.

C. EFFECT OF PROPOSED CHANGES:

Disability

This bill creates a disability retirement program for those in the PEORP. The bill also creates a death benefit regime for the survivors of an employee in the PEORP. These two benefit programs are analogous to the existing disability and death benefit programs for employees in the FRS.

Time of Payment of Retirement Contributions

This bill synchronizes the employer contribution deposit dates for the FRS. Regardless of an employee's participation in the defined benefit plan or the defined contribution plan, the employer must remit the retirement contributions and accompanying payroll data no later than the 5th working day of the month immediately following the month during which the payroll period ended.

PEORP Accumulated Benefit Obligations

The ABO estimates are modified to coincide with the participant's service, average final compensation and age as of June 30, 2002, for state employees, September 30, 2002, for school board employees, and December 31, 2002, for local government employees. These dates appear to be inconsistent with the service, compensation and age of a participant when that participant first would be eligible for enrollment in the PEORP. Subsection (4) of s. 121.4501, F.S., states :

(t)he employee's enrollment in the Public Employee Optional Retirement Program shall be effective the first day of the month *for which* a full month's employer contribution is made into the optional program. (emphasis added)

If a school board employee, first eligible to enroll in PEORP on September 1, 2002, makes the election on that date, the employer will submit September's payroll in October. October's contribution is for September's service, thus it appears the employee is enrolled in PEORP beginning September 1 (the first day of the month for which a full month's contribution is made).

Death Beneficiary

A participant in the PEORP will be required to notify the spouse if the participant designates some other person as the death beneficiary.

State University System Optional Retirement Program

This bill lifts the restriction that benefits under this program be paid out as an annuity. Instead, the benefit distributions can be made by with lump-sum distribution, lump-sum direct rollover, periodic distributions, a partial lump-sum and a partial periodic distribution; or any other method provided by contract with the vendor. Additionally, the bill permits the program to accept contributions to participants' accounts in the form of rollovers and other transfers, if eligible under the federal tax code.

D. SECTION-BY-SECTION ANALYSIS:

Section 1 amends s. 121.052, F.S., relating to the Elected Officers Class of the FRS to provide that contributions from employers of members of this class are due and payable no later than the 5th working day of the month immediately following the month during which the payroll period ended.

Section 2 amends s. 121.055, F.S., relating to the Senior Management class of the FRS to provide that contributions from employers of members of this class are due and payable no later than the 5th working day of the month immediately following the month during which the payroll period ended.

Section 3 amends s. 121.071, F.S., relating to the Regular Class, the Special Risk Class and the Special Risk Administrative Support Class, to provide that contributions from employers of members of these classes are due and payable no later than the 5th working day of the month immediately following the month during which the payroll period ended.

Section 4 amends s. 121.4501, F.S., relating to the PEORP. This section defines "average monthly compensation" and "covered employment" for purposes of the defined contribution program.

The section also provides fixed estimate dates to determine estimated creditable service and estimated average final compensation under the defined benefit program for purposes of determining the present value of employees accumulated benefit obligation for purposes of enrolling the PEORP. For state employees, the initial estimate will be made as of midnight, June 30, 2002; for district school board employees, midnight, September 30, 2002; and for local government employees, midnight December 31, 2002.

Additionally, for employees that have creditable service and are hired by an employer after the window for that employee group has opened, the estimated value of the accumulated benefit obligation is set as of midnight on the last day of the month before the employee's enrollment date in the PEORP.

This section provides that retirement benefits under the PEORP and disability benefits under the PEORP are to be paid in accordance with s. 121.591, F.S. (created in section 6 of this bill).

Section 5 amends s. 121.571(3), F.S., to adjust contribution rates for contributions to disability accounts of employees in the PEORP. These contributions must be deposited in the disability account of the Florida Retirement System Trust Fund are to be separately accounted for and are to be used to provide disability coverage for participants in the PEORP. The rates for disability contributions, effective July 1, 2002, for the retirement member classes are as follows:

- Regular Class: 0.25%
- Special Risk Class: 1.33%
- Special Risk Administrative Support Class: 0.45%
- Elected Officers Class:
 - Legislators 0.41%
 - Governor, Lt. Governor & Cabinet Officers 0.41%
 - St. Attorneys & Public Defenders 0.41%
 - Justices & Judges 0.73%
 - County Elected Officers 0.41%

Contributions made pursuant to this section are paid no later than the 5th working day of the month immediately following the month during which the payroll period ended.

Section 6 creates s. 121.591, F.S., to provide for the payment of benefits under the PEORP, including the payment of normal (retirement) benefits, disability retirement benefits, and death benefits. Benefits may be paid out in one of three ways: in a lump-sum distribution to the participant; in a lump-sum amount payable to an eligible retirement account of the participant; and in periodic distributions (as it would under the defined benefit plan).

This section sets forth the eligibility requirements for claiming a disability retirement benefit; establishes how benefits are to be computed; and addresses the event of a participant recovering from a disability. In addition, this section provides for the payment of death benefits under the PEORP. Limitations on legal process to attach the benefits payable to a participant in the PEORP are codified.

Section 7 amends s. 110.123, F.S., to provide that retirees under the PEORP may participate in the State Employee Health Insurance Program if: (a) the retiree begins receiving retirement benefits immediately upon retirement from state office or employment; and (b) has either (1) met the age and service requirements to qualify for normal retirement under the defined benefit program; or (2) has attained age 59 ½ and has 6 years of creditable service.

Section 8 provides for the legislative determination of an important state interest.

Section 9 allows the Department of Management Services to contract with a private sector firm to administer the disability benefit program. The Department may provide to the Legislature a recommendation for an alternative method of administering and funding disability benefits afforded under the Florida Retirement System.

Section 10 provides legislative intent regarding the maintenance of the qualified status of the Florida Retirement System.

Section 11 amends s. 110.205, F.S., to grant senior management service benefits to county public health department directors and administrators.

Section 12 amends s. 121.35, F.S., to allow retirement benefits accrued under the State University System Optional Retirement Program to be distributed as either a lump-sum, periodic distributions or a combination thereof.

Section 13 provides an effective date of July 1, 2002.

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

This bill reduces the potential revenues generated to fund the disability benefits afforded participants of the Public Employee Optional Retirement Program. See "D. FISCAL COMMENTS" below.

2. Expenditures:

The bill reduces the potential expenditures of state government necessary to fund the disability benefits afforded participants of the Public Employee Optional Retirement Program. See "D. FISCAL COMMENTS" below.

This bill grants senior management service benefits to county public health department directors and administrators. The anticipated costs of these benefit increases is approximately \$150,000 from trust funds.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

The bill reduces the potential expenditures of local government necessary to fund the disability benefits afforded participants of the Public Employee Optional Retirement Program. See "D. FISCAL COMMENTS" below.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None.

D. FISCAL COMMENTS:

According to the Department of Management Services, this bill carries out the mandate of the Legislature in creating a disability benefit program for the PEORP similar to the disability benefit program afforded to members of the defined benefit plan. Program costs would be funded from four sources:

By employer contributions made under s. 121.571(3), F.S.

By transferred proceeds from the disability retiree's investment account(s);

By transferred funds representing any remaining present value the disability retiree may have under the FRS Pension Plan; and,

By interest and earnings on such moneys.

One caution: The Mercer study on which the contribution rates found in this bill are based does not explicitly recognize that the vesting period for regular disability benefits is reduced from 10 years to 8 years, although the study does specifically refer to the legislation which affected this vesting change. If Mercer's estimates were based on the longer vesting period, the funding could ultimately need to be increased slightly.

The contribution rates for disability coverage under the Public Employee Optional Retirement Program will be modified as follows:

	<u>Current Law</u>	<u>New Rate</u>
Regular Class	0.39%	0.25%
Special Risk Class	1.25%	1.33%
Special Risk Administrative Support Class	0.73%	0.45%
Senior Management Service Class	0.50%	0.26%
Elected Officers' Class		
Legislators	0.61%	0.41%
Governor, Lt. Governor, Cabinet	0.61%	0.41%
State Attorneys, Public Defenders	0.61%	0.41%
Judges, Justices	1.45%	0.73%
Elected County Officers	0.86%	0.41%

The funding for the disability benefit is provided by contributions made by state and local government employers on behalf of their FRS employees who are PEORP participants. The costs below reflect the projected employer costs system wide based on the adjusted rates as recommended by the Mercer Study and provided under section 2 of this bill, if we assume that *half* of the members of the defined benefit program elect to transfer to the PEORP. In the defined benefit plan, these costs are embedded in the retirement contribution rate. The rate adjustments implemented in this bill would result in an *overall reduction* in the amount of required employer contributions.

Employer Costs Based On New Disability Contribution Rates

	<u>FY 02-03</u>	<u>FY 03-04</u>	<u>FY 04-05</u>
State	\$11,242,000	\$11,804,000	\$12,395,000
Local Govt.	<u>\$29,585,000</u>	<u>\$31,064,000</u>	<u>\$32,617,000</u>
Total	\$40,827,000	\$42,868,000	\$45,012,000

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

The bill does not require cities and counties to spend money or take an action to expend funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

The bill does not reduce the authority that counties or municipalities have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

The bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

A. CONSTITUTIONAL ISSUES:

None. (But see "VI AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES" below)

B. RULE-MAKING AUTHORITY:

The Department of Management services is authorized to adopt rules to implement the bill provisions creating the disability retirement benefit and death benefit programs for participants in the PEORP.

C. OTHER COMMENTS:

None.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

The Committee on State Administration at its January 30, 2002, meeting adopted two amendments, now traveling with the bill, which require that employer contributions for PEORP participants be deposited in the Clearing Trust Fund (to be created in a separate bill) and to provide criteria for employees to qualify for state group insurance participation upon termination of employment.

The amendment concerning deposit of contributions into the Clearing Trust Fund contains directory language that should be placed in the directory paragraph of the bill section. It should be removed from the text of the bill and placed in the appropriate location in the directory paragraph.

On February 8, 2002, the Committee on Fiscal Policy and Resources adopted one amendment. The amendment allows the Department of Management Services to contract with private sector companies to administer the disability program. The amendment grants authority to the Department to implement an alternative method of administering the disability benefit program, including the use of commercial insurance. This amendment raises a concern regarding unlawful delegation of legislative authority because the amendment appears to grant authority to the Department to implement an alternative funding method for the disability program.

On February 27, 2002, the Fiscal Responsibility Council adopted a series of 14 amendments and approved a council substitute for the bill. The amendments adopted by the Council are described below:

Amendments 1 through 3 require payroll data, along with the retirement contributions, to be submitted by the 5th working day.

Amendments 4 and 5 require interest to be credited to a disabled member's account when that member has transferred the PEORP account balance to the defined benefit program as a condition of receiving disability retirement payments.

Amendment 6 clarifies the payment of disability retirement benefits for certain judicial officers.

Amendment 7 allows a disabled member's beneficiary to collect the remaining account balance if the disabled member dies prior to receiving disability benefits equal to the PEORP balance transferred to the defined benefit disability program.

Amendment 8 clarifies the time period in which a PEORP retiree is eligible to join the State Employee Health Insurance Program as a retiree.

Amendment 9 clarifies that DMS may contract for the administration of the disability program.

Amendment 10 provides intent language regarding the qualified status of the FRS.

Amendment 11 grants county public health department directors and administrators senior management service benefits.

Amendment 12 modifies the benefits payable under the State University System Optional Retirement Program.

Amendments 13 and 14 clarify that a newly hired employee will receive only an amount equal to the defined benefit contributions made on his behalf during his election period until he makes an election to participate in PEORP.

VII. SIGNATURES:

COMMITTEE ON STATE ADMINISTRATION:

Prepared by:

David M. Greenbaum

Staff Director:

J. Marleen Ahearn, Ph.D., J.D.

AS REVISED BY THE COMMITTEE ON FISCAL POLICY & RESOURCES:

Prepared by:

Adam Shamy

Staff Director:

Lynne Overton

AS FURTHER REVISED BY THE FISCAL RESPONSIBILITY COUNCIL:

Prepared by:

Joe McVaney

Staff Director:

David Coburn