HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 1575 w/CS Transfer/Division of Retirement to State Board of Administration
SPONSOR(S): Peterman
TIED BILLS: **IDEN./SIM. BILLS:** 1258

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) State Administration	4 Y, 0 N w/CS	Brazzell	Everhart
2) Commerce & Local Affairs (Sub)			
3) Appropriations			
4)			
5)			

SUMMARY ANALYSIS

This bill transfers the Division of Retirement (DOR) in the Department of Management Services (DMS) to the State Board of Administration (SBA) by a type one transfer. It removes the DOR from the organizational structure of the DMS and creates the Division of Retirement in the State Board of Administration. The Division is subject to the executive director of the SBA.

This bill makes numerous reference changes in the Florida Statutes to reflect the transfer of powers from the Division in its current location at the DMS to the transferred location at the SBA.

There is a conservative estimate of a recurring cost to the state of $249,908 annually (trust fund).

This bill takes effect July 1, 2003.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. DOES THE BILL:

1. Reduce government?	Yes[]	No[]	N/A[x]
2. Lower taxes?	Yes[]	No[]	N/A[x]
3. Expand individual freedom?	Yes[]	No[]	N/A[x]
4. Increase personal responsibility?	Yes[]	No[]	N/A[x]
5. Empower families?	Yes[]	No[]	N/A[x]

For any principle that received a "no" above, please explain:

B. EFFECT OF PROPOSED CHANGES:

Background:

Reorganization and Methods of Transfer

Section 20.06, F.S., establishes two "shorthand" methods of facilitating the reorganization of the executive branch. These methods of transferring departments, units of departments and programs are specifically stated not to affect the validity of any judicial or administrative proceeding pending on the day of the transfer. Furthermore, the agency which receives the powers, duties, and functions relating to the pending proceeding must be substituted as the party in interest.

- *Type One Transfer:* Section 20.06(1), F.S., defines a type one transfer as the *transferring intact* of an *existing agency or department* so that the agency or department *becomes a unit* of another agency or department. Any agency or department transferred to another agency or department by a type one transfer will exercise its powers, duties, and functions as prescribed by law, subject to review and approval by, and under the direct supervision of, the head of the agency or department to which the transfer is made.
- *Type Two Transfer:* Section 20.06(2), F.S., defines a type two transfer as the *merging* into another agency or department of an *existing agency or department or a program, activity, or function* thereof, or if certain identifiable units or subunits, programs, activities, or functions are removed from the existing agency or department, or are abolished, it is the merging into an agency or department of the existing agency or department with the certain identifiable units or subunits, programs, activities, or functions removed or abolished. Unless otherwise provided by law, in a type two transfer, the head of the agency or department to which an existing agency, department, activity, or function is transferred is authorized to establish units or subunits to which the agency or department is assigned, and to assign administrative authority for identifiable programs, activities, or functions to the extent authorized by ch. 20, F.S.

In both a type one and type two transfer, any agency or department, program, activity or function transferred has all its statutory powers, duties, and functions, and its records, personnel, property, and unexpended balances of appropriations, allocations, or other funds transferred to the agency or department to which it is transferred. The transfer of segregated funds must be made in such manner that the relation between program and revenue source as provided by law is retained.

Additionally, in both a type one and type two transfer, unless otherwise provided by law, the administrative rules of any agency or department involved in the transfer which are in effect immediately before the transfer remain in effect until specifically changed.

The Division of Retirement, Department of Management Services

Section 20.22, F.S., creates the Department of Management Services (DMS). The head of the DMS is the Secretary of Management Services. The secretary is appointed by the Governor, subject to Senate confirmation, and serves at the pleasure of the Governor.

DMS is the administrative arm of state government. DMS consolidates the state's purchasing power for buying commodities and services and establishes rules and guidelines to ensure a fair, competitive procurement process. It is the central entity for the construction, operation, maintenance, and security of state-owned facilities. It provides telecommunications services to state and local governments and oversees state human resources administration. DMS also administers the statewide government employee retirement system and monitors the actuarial soundness of local government retirement systems.

Pursuant to ss. 121.021(5) and 121.025, F.S., the secretary of DMS is the administrator of the retirement and pension systems and has authority to sign contracts necessary to carry out the duties and responsibilities assigned the department.

The Division of Retirement (Division) is also created in s. 121.1905, F.S. The mission of the Division is to provide quality and cost-effective retirement services as measured by member satisfaction and by comparison with administrative costs of comparable retirement systems. The Division is responsible for administering the Florida Retirement System (FRS). The FRS is a multi-employer, non-participatory defined benefit pension plan providing a monthly annuity pension benefit for employees of approximately 800 state, county, municipal, school board, and special district employers. The Division is currently responsible for the State University System Optional Retirement Program pursuant to s. 121.35, F.S., and the Senior Management Service Optional Annuity Program, pursuant to s. 121.055(6), F.S. Key responsibilities include[1]:

- Enrollment functions: determining eligibility for retirement system membership and disability and survivor benefits; enrolling new members; enrolling local government employers who wish to join the FRS; maintaining retirement records.
- Benefit determination functions: calculating estimates and final benefits due to each member and monitoring reemployment after retirement.
- Accounting and payroll functions: collecting employer contributions and transferring these monies to the State Board of Administration for investment; determining benefit payments to retirees and persons receiving disability or survivor benefits and transmitting these data to the State Comptroller's Office, which distributes payments to beneficiaries; distributing insurance deductions from benefit payments to various insurance companies; conducting audits of employers' payroll records; compiling and distributing retirees' annual tax information; performing accounting activities for the Florida Retirement System Trust Fund.
- Customer service functions: counseling members on their retirement rights and benefits; educating members and employers.
- Other administrative functions: administering the Retiree Health Insurance Subsidy program; resolving benefit appeals through a hearing process, which includes providing support to the State Retirement Commission.

The Division employs 202 full-time employees (FTE). The cost incurred from their employment in addition to the cost incurred from running the Division is $26,835,607.[2]

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[1] Office of Program Policy Analysis and Government Accountability Report No. 01-12.
[2] $9,698, 912 is funded from the general revenue fund, and $17,136,695 is funded from trust funds. Section 6 of the Conference Report on HB 27 E, 2002. This year's House appropriations bill proposes eliminating three FTE positions (s. 6 of HB 1789, 1st ENG.), and the Senate appropriations bill proposes eliminating two FTE positions (s. 6 of SB 2500, 1st ENG.). The general-revenue funded functions of the Division will remain with the Department of Management Services.

The State Board of Administration

The State Board of Administration (SBA) is created in Article IV, s. 4(e) of the State Constitution, and governed by a Board of Trustees. That provision states:

> The governor as chair, the chief financial officer, and the attorney general shall constitute the state board of administration, which shall succeed to all the power, control, and authority of the state board of administration established pursuant to Article IX, Section 16 of the Constitution of 1885, and which shall continue as a body at least for the life of Article XII, section 9(c).

The Board of Trustees has fiduciary responsibility for the management and oversight of the SBA.[3]

The Legislature has given responsibility for managing financial funds and instruments to the SBA. The SBA's primary responsibilities are in investment and debt management.

The FRS's defined benefit and defined contribution plans' assets are managed by the SBA. Additionally, the SBA manages assets for the Local Government Surplus Funds Trust Fund, Florida Division of Bond Finance, Florida Hurricane Catastrophe Fund, Lawton Chiles Endowment Fund, and other small non-qualified governmental entities. Total assets under management are approximately $115 billion, which includes the FRS's $80 billion pension fund. Most assets under management are divided among six asset classes: domestic equities, international equities, fixed income, real estate, alternative investments, and cash.[4]

Additionally, administrative support is provided by the SBA to the Florida Prepaid College Program and the Florida Division of Bond Finance. The SBA also operates the Inland Protection Financing Corporation, the Florida Water Pollution Control Financing Corporation, and the Investment Fraud Restoration Financing Corporation.

The mission of the SBA is to maximize the return on investment while prudently managing risk, effectively carry out assigned responsibilities while controlling costs, and perform its duties ethically and with integrity.

Report of the SBA/DOR Joint Team on Merger

The SBA and the Division were asked by the Governor to evaluate the impact of a merger of the two entities.[5] The specific charge was to develop a business case on the costs and benefits of merging the Division and the SBA. A team of members from each entity was created[6] and held three meetings. Its written report was issued March 3, 2003.

The report notes that the core missions of the two entities are fundamentally different: institutional investment at the SBA and benefit administration at the Division.[7] There are, however, a number of circumstances under which the two organizations must work together in order to perform most effectively. These include:

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[3] The SBA is the fourth and eight largest pension fund in the country and the world, respectively.
[4] http://www.fsba.state.fl.us/about.asp.
[5] Page 1, *Report of the SBA/DOR Joint Team on Merger*, March 3, 2003.
[6] Members from the SBA were: James Francis (Chair), Senior Investment Policy Officer and Economist; Bill Beck, Deputy General Counsel; Chuck Bunker, Senior Operating Officer; Teresa Butler, Budget Manager; Eric Nelson, Senior Operating Officer; Ron Poppell, Director of Educational Services. Members from the Division were: Jerry Haynes, Administration/Budget; Pat Connolly, Bureau Chief Retired Payroll; Larry Hunicutt, Administrator Calculations; Mark Morton, Auditor; Sarabeth Snuggs, Bureau Chief Enrollment/Contributions.
[7] Page 6 of *Report of the SBA/DOR Joint Team on Merger*.

- Monitoring, accounting for and anticipating cash inflows and outflows of the Florida Retirement System Trust Fund (FRSTF).
- Directing actuarial analysis and working with actuarial information in order to meet FRS objectives.
- Insuring that recordkeeping for member enrollment for the FRS Pension Plan and FRS Investment Plan is consistent, accurate and processed timely.
- Insuring that members and employers receive adequate and coordinated support under the two FRS retirement plans, both administratively and educationally.
- Insuring that the various defined contribution plans authorized under Florida law are well-formulated and effectively implemented.[8]

The report notes that, due to the difference in core missions of each organization, some inconsistencies have arisen in the following areas:

- Educational materials for FRS members.
- Service philosophies for FRS members.
- Policy development and oversight for defined contribution programs.
- Preferred drivers for the actuarial valuation model.
- Levels of access to the state actuarial firm.
- Measured levels of FRSTF cash flows.

The report made the following findings:

- Merger would lead to enhanced coordination and efficiency in the FRS that cross areas of responsibility.
- Combining the SBA and the division would provide a common focus on the FRS, leading to enhanced efficiencies and effectiveness.
- Combining SBA and the division would be partially consistent with a common business model for large retirement systems.
- The investment management responsibilities of the SBA may be compromised as a result of merger.
- Combining SBA and the division would be inconsistent with the business model for investment boards that have diverse investment management responsibilities.
- The benefits of the merger will not accrue unless benefit administration responsibilities are managed under the same operational and financial flexibility as the SBA.

The report concludes, "In the team's judgment, the consequences of merger may be essentially neutral in the short term and positive in the long term. The direct financial costs that have been quantified combined with the upside risk on payroll expense are likely to be offset by savings with respect to information technology support. In the long run, however, we expect the net impact of merger to be positive based on indirect gains from post-merger re-engineering and from a singular executive focus on all aspects of the Florida Retirement System."

Proposed Changes:

This bill transfers the Division of Retirement (Division) in the Department of Management Services (DMS) to the State Board of Administration (SBA) by a type one transfer. It removes the Division of Retirement from the organizational structure of the DMS and creates the Division of Retirement in the

[8] The SBA is required to make recommendations on the investment options offered under the State University System Optional Retirement Program and the Senior Management Service Optional Annuity Program, both of which the division has been delegated administrative responsibility to operate. The SBA and the DOR are required to coordinate activities with respect to the Public Employees Optional Retirement Plan, for which the SBA is responsible.

SBA. The Division is subject to the executive director of the SBA, and the executive director is considered the agency head for purposes of ch. 120, F.S., the Administrative Procedure Act.

All officers and employees of the Division are given Selected Exempt Service status.

The State Retirement Commission is assigned to and administratively housed within the Division.

The bill makes numerous reference changes in the Florida Statutes to reflect the transfer of powers from the Division in its current location at the DMS to the transferred location at the SBA.

C. SECTION DIRECTORY:

Section 1: Provides for the type one transfer of the Division of Retirement (Division) to the State Board of Administration (SBA).

Section 2: Amends s. 20.22, F.S., to remove the Division from the Department of Management Services.

Section 3: Amends s. 20.28, F.S., to establish the Division under the SBA.

Section 4: Amends s. 110.205, F.S., to provide Selected Exempt Service status to Division employees.

Sections 5-61: Amend various statutes to revise references to the Department of Management Services, the Division, and the SBA to be conforming, including ss., 112.05, 112.3173, 112.352, 112.354, 112.356, 112.358, 112.361, 112.362, 112.363, 112.625, 112.63, 112.64, 112.658, 112.661, 112.665, 121.021, 121.025, 121.031, 121.051, 121.0511, 121.0515, 121.052, 121.055, 121.081, 121.085, 121.091, 121.101, 121.111, 121.133, 121.135, 121.136, 121.1815, 121.1905, 121.192, 121.193, 121.22, 121.23, 121.24, 121.30, 121.35, 121.40, 121.45, 121.4501, 121.403, 121.591, 121.5911, 121.72, 121.73, 121.74, 175.032, 175.1215, 175.341, 185.02, 185.105, 185.23, 215.28, 215.44, 215.50, 215.52, 238.01, 238.05, 238.06, 238.171, 238.181, 238.32, and 650.02, F.S.

Section 62: Creates an unnumbered section of law to allow the Department of Management Services to contract with the State Board of Administration for the administration of certain retirement plans.

Section 63: Creates an unnumbered section of law to allow the SBA to issue benefit payments directly or through a third-party agent, rather than through the Department of Financial Services.

Section 64: Provides an effective date of July 1, 2003.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues: None.

2. Expenditures: According to the Report of the State Board of Administration/Division of Retirement Joint Team on Merger dated March 3, 2003, the following costs, funded out of trust funds, are

associated with the transfer of the Division to the SBA (amounts are shown in current dollars [i.e., no adjustments for inflation or growth]):[9]

SBA/DOR Merger Cost Impact Summary			
	(1) Current Costs (Trust fund): Division of Retirement in DMS	**(2) Estimated Costs (Trust fund): Division of Retirement in SBA**	**(3) Change in Costs (Trust fund):**
A. Recurring Costs			
1. Match SBA benefit levels for Division employees	$ 9,268,311	$ 9, 644,166	$ 375, 855
2. Impact from combining defined contribution program responsibilities	106,057	-	(106,057)
3.Efficiencies in administrative & executive support[10]	712,217	297,312	(414,905)
4. Rental costs[11]	712,000	1,107,015	395,015
Total Recurring (Trust fund)	**$ 10, 798,585**	**$ 11,048,493**	**$ 249,908**
B. Non-Recurring Costs[12]			
1. Transition costs for personnel checks – 1 year		$ 10,000	
2. Cost of physical move & set-up		$ 1,762,200	
Total Non-recurring (sum over 2 years)(Trust fund)		**$ 1,772,200**	

Potential sources of future cost saving that were not quantified include that SBA information technology staff assume responsibility for the Division (the Division currently outsources its information technology support to a private sector firm for a $3.5 million annual cost). There may be other savings relating to new efficiencies in operational support, document processing, and the educational program. However, there are other potential costs. In the transfer of the Division to the SBA, Division employees who are currently career service will become select exempt. There could be additional costs as a result of this employee status modification due to differences in leave accrual rates, method of accrual, leave caps, and compensation for overtime. The potential costs for leave and compensation payouts could be significant. Approximately 200 employees will be affected by the transfer; these positions will be moved from the operating to the non-operating budget. While this may

[9] According to the *Report of the SBA/DOR Joint Team on Merger*, a number of qualifications and assumptions should be noted with respect to the estimates. First, they are in current dollars, meaning that future inflation, workload growth and other factors that influence the level of spending over time are not included. It is assumed that Division employees would be treated no differently with respect to benefits than current SBA employees. However, no estimate is included for how Division salaries might change. It is anticipated that the same competitive pay analyses that govern adjustments to SBA salary levels would apply to Division personnel. These adjustments could be significant. SBA's costs to expand its executive management and administrative services operations to include DOR fall into new positions and allocated costs for existing positions. Rental and moving costs are based upon the assumption that DOR would be housed in facilities adjacent to the Hermitage Building.

[10] Assumes no impact on current level of Division salaries.

[11] Longer-term savings are expected from operational efficiencies and business process enhancements. However, the magnitude cannot be estimated at this time.

[12] There will be a non-recurring allocated (non-monetary) SBA staff cost of $333,363 in year 1 and $417,175 in year 2.

result in there appearing to be 200 fewer positions in the budget, these positions will nevertheless exist in the SBA.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues: None.

2. Expenditures: None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR: The Division currently outsources its information technology support to a private firm; however, the SBA believes that it could potentially provide this service with its own staff at a significant savings. Thus the private firm delivering these services could be impacted if the Division discontinues use of its services.

D. FISCAL COMMENTS: None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision: None.

2. Other: None.

B. RULE-MAKING AUTHORITY: Since a type one transfer is involved, the administrative rules of the Division which are in effect immediately before the transfer remain in effect until specifically changed.

C. DRAFTING ISSUES OR OTHER COMMENTS:

The DMS will have to engage in impact bargaining post-transfer as a result of the bill because the bill modifies the current status of Division employees who are career service and makes them select exempt.

Use of a type one transfer instead of a type two transfer provides less flexibility to the agency that receives the transferred entity. Further, a type one transfer is, by its definition, the *transferring intact* of an *existing agency or department* so that the agency or department *becomes a unit* of another agency or department, whereas a type two transfer is the *merging* into another agency or department of an *existing agency or department or a program, activity, or function* thereof. As the Division of Retirement is a division within the Department of Management Services, its transfer as a division to another entity would usually be a type two transfer.

Retiree monthly checks are processed through the Bureau of State Payrolls in the Department of Financial Services. Because the SBA is an off-budget entity, its payroll is executed outside of the Bureau of State Payrolls. To provide minimal organizational disruption, including the disruption of electronic fund transfer, the board may need to contract with the Bureau of State Payrolls for the preservation of the current payment.

IV. AMENDMENTS/COMMITTEE SUBSTITUTE CHANGES

This bill was amended by the Committee on State Administration on April 14, 2003. The strike-all amendment makes many stylistic and technical changes. Substantive changes include:

- Providing that the State Board of Administration (SBA) rather than the Legislature will determine the amount to be deducted from employer contributions to pay for administration of the Senior Management Service Optional Annuity Program and the Optional Retirement Program.
- Exempting additional types of purchases from the requirements of state law regarding purchasing.
- Repealing a provision of state law regarding moving funds out of the Florida Retirement System Trust Fund that violates federal law.
- Allowing the Department of Management Services to contract with the SBA for the administration of a few small, older retirement plans so that these general-revenue funded plans may be administered by the SBA, even though the SBA does not receive general revenue funding.
- Allowing the SBA to issue benefit payments directly or through a third-party agent, rather than through the Department of Financial Services.
- Expanding the SBA's rulemaking authority.

The bill was reported favorably with a committee substitute.