

# 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.)

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Prepared By: Governmental Oversight and Productivity Committee

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BILL: CS/SB 1568

SPONSOR: Governmental Oversight and Productivity Committee and Senator Aronberg

SUBJECT: Florida Retirement System

DATE: April 26, 2005

REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Vickers</u>	<u>Yeatman</u>	<u>CA</u>	<b>Favorable</b>
2.	<u>Wilson</u>	<u>Wilson</u>	<u>GO</u>	<b>Fav/CS</b>
3.	_____	_____	<u>WM</u>	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

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## I. Summary:

This bill amends the current definition of “compensation” for purposes of the Florida Retirement System (FRS) to include: (1) salary supplements made to firefighters, paramedics or emergency medical technicians for the successful completion of employer-approved educational training; and (2) salary supplements made to firefighters, paramedics or emergency medical technicians for additional job-related duties and responsibilities. The bill would allow specified nonrecurring payments to be treated as compensation for purposes of calculating retirement benefits.

There will be an indeterminate fiscal impact to the FRS resulting from additional compensation that would be allowed by this bill. However, the Division of Retirement reports that the fiscal impact is not anticipated to be sufficient to require a rate increase, and would be reflected in future valuations and experience studies of the FRS.

This bill substantially amends section 121.021 of the Florida Statutes.

## II. Present Situation:

**Florida Retirement System** - The FRS was created in December 1970 to consolidate then-existing state-administered retirement systems for state and county officers and employees, teachers, judges, and Highway Patrol officers. Today, the FRS is the fourth largest public retirement system in the United States, covering 633,489 active employees, 217,158 annuitants (retirees and their surviving beneficiaries), and 28,280 participants of the Deferred Retirement Option Program (DROP).

All state and county employees are compulsory members of the FRS, and as of June 30, 2004, about 141 Florida cities<sup>1</sup> were covering firefighters, police, and/or general employees under the FRS. On that date, there were also 166 independent special districts<sup>2</sup> with members in the FRS. As of June 30, 2004, state employees (including university employees) represent 21.8 percent of the FRS membership. Remaining members are employed by local agencies, including all counties (23.5%), district school boards (48.3%), and community colleges (2.8%), as well as cities and special districts (3.6%) that have opted to join the FRS.

The active membership of the FRS is divided into five membership classes: The Regular Class consists of 558,051 members (88.1% of the membership); the Special Risk Class includes 66,861 members (10.6%), the Special Risk Administrative Support Class has 92 members (0.014%), the Elected Officers' Class has 2,112 members (0.33%), and the Senior Management Service Class has 6,373 members (1.0%). Each class is separately funded based upon the costs attributable to the members of that class.

**Funding of FRS** - Retirement benefits are funded by monthly employer contributions made to the Florida Retirement System Trust Fund. The contribution for each employee is equal to a specified percentage of the member's gross monthly income. Contribution rates are set by law as a percentage of payroll (with different rates applicable to different classes and subclasses of the FRS). Rates are established at levels determined by system actuaries to be sufficient to prefund promised benefits, when made regularly throughout each covered employee's career. The statutory definitions of "compensation" and "bonus" limit what payments will or will not be included as income for retirement purposes.

Since 1976, Article X, Section 14 of the Florida Constitution has required that retirement benefit increases under public pension plans in the State of Florida must be concurrently funded on a sound actuarial basis, as set forth below:

SECTION 14. State retirement systems benefit changes.--A governmental unit responsible for any retirement or pension system supported in whole or in part by public funds shall not after January 1, 1977, provide any increase in the benefits to the members or beneficiaries of such system unless such unit has made or concurrently makes provision for the funding of the increase in benefits on a sound actuarial basis.

**Compensation** – Section 121.021(22), F.S., currently defines "compensation" to mean the monthly salary paid a member by his or her FRS employer for work performed arising from that employment.<sup>3</sup> Specifically, compensation includes the following:

- overtime payments;
- accumulated annual leave payments;
- payments in addition to the member's base rate of pay, if certain requirements are met;

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<sup>1</sup> In January 1, 1996, many cities and special districts were authorized by law to "opt out" of the FRS for new employees. Many chose to do so, and since that time, some have elected to rejoin the FRS. As of June 30, 2004, among the 141 cities participating in the FRS, there are 48 cities that have chosen to withdraw from the system and do not cover new members under the FRS.

<sup>2</sup> This number includes 18 independent special districts closed to new FRS members since January 1996.

<sup>3</sup> Section 121.021(22), F.S.

- amounts withheld for tax sheltered annuities or deferred compensation programs;
- payments made in lieu of a permanent increase in the base rate of pay; and
- salary supplements made as a result of receipt of a National Board for Professional Standards certificate (effective July 1, 2002).<sup>4</sup>

Under current law, supplemental payments that do not meet the periodic payment criteria are considered bonuses and are not compensation for retirement purposes. Such payments should not be reported to the Division and would not be included in the calculation of retirement benefits.

**Average Final Compensation** - The average final compensation (AFC) is calculated using the average of the five highest fiscal years of salary (salary earned from July 1-June 30).<sup>5</sup> A member's compensation is included when determining that member's AFC. A member's years of creditable service at retirement are multiplied by the accrual rate,<sup>6</sup> and it is then multiplied by the AFC to derive the annual retirement benefit. Up to 500 hours of accrued annual leave may be added to the calculation to enhance, or "spike," the final benefit.

### III. Effect of Proposed Changes:

**Section 1** of the bill amends s. 121.021, F.S., to revise the current definition of "compensation" to include:

- salary supplements made to firefighters, paramedics or emergency medical technicians (EMTs) for the successful completion of employer-approved educational training; and
- salary supplements made to firefighters, paramedics or EMTs for additional job-related duties and responsibilities.

The bill would require employers currently making these types of supplemental payments to firefighters, paramedics or emergency medical technicians to include these payments in compensation reported for retirement. Employers would owe the Special Risk Class contribution rate<sup>7</sup> on these supplemental payments. Based on January 2005 payroll, the Division identified approximately 114 employers with approximately 6,055 employees that could be impacted by this bill. It is unknown how many agencies currently pay these types of supplemental payments, how many employees receive them, or the amount of such payments. The Division contacted a group of these employers whose employees represented over 25 percent of the estimated number of affected employees. Only one agency, with 218 eligible employees, paid supplemental payments as described by this bill that are not already reported to the FRS. The average of this supplemental payment for this agency, based upon its total number of employees, was slightly under \$157.00 per annum.

Any firefighter, paramedic or emergency medical technician whose average final compensation (highest 5 fiscal years of salary) is improved as a result of such payments, would receive higher retirement benefits. Payments which begin late in an employee's career and result in higher

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<sup>4</sup> Section 121.021(22)(a), F.S.

<sup>5</sup> Section 121.021(24), F.S.

<sup>6</sup> The accrual rate is the percentage value awarded for each year of service as determined by the member's class of membership.

<sup>7</sup> This rate is 17.34 % for the 2005-06 fiscal year, excluding the 0.08% PEORP admin fee and 1.11% HIS contribution rate.

retirement benefits could potentially increase the normal cost for the class and could result in additional unfunded liability. These impacts would be reflected in future experience studies and/or valuations of the FRS. Rate increases recommended by future valuations would reflect the fiscal impact of these payments and would affect all employers with Special Risk Class members.

**Section 2** provides the bill shall take effect July 1, 2005.

**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:

None.

C. Government Sector Impact:

The Division reports that under current law, the supplemental payments covered by this bill are not reported to the Division of Retirement, so the employer contribution portion of the cost impact cannot be directly determined. Also, the bill does not require employers to create new programs for these payments, only to report these payments as compensation for the FRS if they exist on or after July 1, 2005. Each impacted employer would pay an additional 18.53 percent of such payments to cover the contributions for the FRS benefit. The Division identified approximately 114 employers with at minimum of 6,055 employees who could have additional compensation reported to the FRS under the bill.

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

The CS adds a statement of important state interest since the vast majority of firefighters are employed by units of local government.

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

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## **VIII. Summary of Amendments:**

None.

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