

## HOUSE OF REPRESENTATIVES STAFF FINAL BILL ANALYSIS

**BILL #:** CS/CS/HB 1121 Florida Retirement System

**SPONSOR(S):** State Affairs Committee and Constitutional Rights, Rule of Law & Government Operations Subcommittee, Bartleman, Tomkow and others

**TIED BILLS:** **IDEN./SIM. BILLS:** CS/SB 1156

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**FINAL HOUSE FLOOR ACTION:** 109 Y's      0 N's      **GOVERNOR'S ACTION:** Approved

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### SUMMARY ANALYSIS

CS/CS/HB 1121 passed the House on April 28, 2023, and subsequently passed the Senate on April 28, 2023.

The Florida Retirement System (FRS) is a multiple-employer, contributory plan that provides retirement income benefits for employees of state and county government agencies, district school boards, state colleges, and universities. It also serves as the retirement plan for employees of the cities and special districts that have elected to join the system. Members of the FRS have two plan options available for participation: the pension plan, which is a defined benefit plan, and the investment plan, which is a defined contribution plan.

A member of the FRS must terminate employment in order to begin receiving benefits. Termination occurs when a member ceases all employment relationships with his or her FRS employer. Termination is void if any FRS-participating employer reemploys a member during a specified period.

The bill authorizes a person who has retired from the FRS to provide volunteer services to an FRS employer without violating the provision of law requiring termination from employment. Specifically, the bill authorizes an FRS employer to establish a post-employment volunteer program that allows retirees to provide civic, charitable, and humanitarian services during the first 12 months following retirement. The volunteer program must operate pursuant to specified criteria.

The bill provides that the Department of Management Services or the State Board of Administration may require any evidence of termination necessary to determine compliance with Florida laws and regulations.

The bill does not appear to have a fiscal impact on the state or local governments.

The bill was approved by the Governor on June 30, 2023, ch. 2023-316, L.O.F., and will become effective on July 1, 2023.

## I. SUBSTANTIVE INFORMATION

### A. EFFECT OF CHANGES:

#### Present Situation

##### Florida Retirement System

The Florida Retirement System (FRS) was established in 1970 when the Legislature consolidated the Teachers' Retirement System, the State and County Officers and Employees' Retirement System, and the Highway Patrol Pension Fund. In 1972, the Judicial Retirement System was consolidated into the FRS, and in 2007, the Institute of Food and Agricultural Sciences Supplemental Retirement Program was consolidated under the Regular Class of the FRS as a closed group. The FRS was amended in 1998 to add the Deferred Retirement Option Program (DROP) under the defined benefit plan and amended in 2000 to provide a defined contribution plan alternative to the defined benefit plan for FRS members effective July 1, 2002.<sup>1</sup>

The FRS is a multi-employer, contributory plan<sup>2</sup> governed by the Florida Retirement System Act.<sup>3</sup> As of June 30, 2022, the FRS had 629,073 active members,<sup>4</sup> 448,846 retired members and beneficiaries, and 28,827 members in DROP.<sup>5</sup> It is the primary retirement plan for employees of state and county government agencies, district school boards, state colleges, and state universities. The FRS also serves as the retirement plan for employees of the 180 municipalities, 153 special districts, and two independent hospitals that have elected to join the system.<sup>6</sup>

The membership of the FRS is divided into five membership classes:

- The Regular Class<sup>7</sup> has 537,128 active members and 7,806 in renewed membership.
- The Special Risk Class<sup>8</sup> has 72,925 active members and 1,100 in renewed membership.
- The Special Risk Administrative Support Class<sup>9</sup> has 104 active members and one in renewed membership.
- The Elected Officers' Class<sup>10</sup> has 2,075 active members and 109 in renewed membership.
- The Senior Management Service Class<sup>11</sup> has 7,610 active members and 210 in renewed membership.<sup>12</sup>

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<sup>1</sup> Florida Retirement System Pension Plan and Other State Administered Retirement Systems Comprehensive Annual Financial Report Fiscal Year Ended June 30, 2022, at 35, *available at*: [https://employer.frs.fl.gov/forms/2021-22\\_ACFR.pdf](https://employer.frs.fl.gov/forms/2021-22_ACFR.pdf) (last visited February 20, 2023).

<sup>2</sup> Prior to 1975, members of the FRS were required to make employee contributions of either four percent gross compensation for Regular Class members or six percent for Special Risk Class members. Members were again required to contribute to the system after June 30, 2011, at three percent.

<sup>3</sup> Ch. 121, F.S.

<sup>4</sup> As of June 30, 2022, the FRS Pension Plan had 444,150 members and the investment plan had 184,923 members. FRS Comprehensive Annual Report, *supra* note 1 at 260.

<sup>5</sup> FRS Comprehensive Annual Report, *supra* note 1 at 42.

<sup>6</sup> *Id.* at 298.

<sup>7</sup> The Regular Class is for all members who are not assigned to another class. S. 121.021(12), F.S.

<sup>8</sup> The Special Risk Class is for members employed as law enforcement officers, firefighters, correctional officers, probation officers, paramedics and emergency technicians, among others. S. 121.0515, F.S.

<sup>9</sup> The Special Risk Administrative Support Class is for a special risk member who moved or was reassigned to a nonspecial risk law enforcement, firefighting, correctional, or emergency medical care administrative support position with the same agency, or who is subsequently employed in such a position under the FRS. S. 121.0515(8), F.S.

<sup>10</sup> The Elected Officers' Class is for elected state and county officers, and for those elected municipal or special district officers whose governing body has chosen Elected Officers' Class participation for its elected officers. S. 121.052, F.S.

<sup>11</sup> The Senior Management Service Class is for members who fill senior management level positions assigned by law to the Senior Management Service Class or authorized by law as eligible for Senior Management Service designation. S. 121.055, F.S.

<sup>12</sup> FRS Comprehensive Annual Report, *supra* note 1 at 263.

## Plan Choice

Members of the FRS have two primary plan options available for participation:

- The defined contribution plan, also known as the FRS Investment Plan; and
- The defined benefit plan, also known as the FRS Pension Plan.

When an employee is initially hired in an FRS-covered position, the member has eight months after the month of hire to choose to participate in either the pension plan or the investment plan. If the employee does not choose within that period, a member in the Special Risk Class is deemed to have chosen to participate in the pension plan and all other members are deemed to have chosen to participate in the investment plan. After a member has made an active election to participate in a plan or the member's choice window has expired, the member has one additional opportunity to choose to switch between plans; this is referred to as the second election.<sup>13</sup>

## Investment Plan

In 2000, the Legislature created the Public Employee Optional Retirement Program (investment plan), a defined contribution plan offered to eligible employees as an alternative to the pension plan. The earliest that any member could participate in the investment plan was July 1, 2002. The State Board of Administration (SBA) is primarily responsible for administering the investment plan.<sup>14</sup> The SBA is comprised of the Governor as chair, the Chief Financial Officer, and the Attorney General.<sup>15</sup>

Benefits under the investment plan accrue in individual member accounts funded by both employee and employer contributions and investment earnings. Benefits are provided through employee-directed investments offered by approved investment providers. The amount of money contributed to each member's account varies by class as follows:<sup>16</sup>

<b>Membership Class</b>	<b>Percentage of Gross Compensation<sup>1</sup></b>
Regular Class	9.30%
Special Risk Class	17.00%
Special Risk Administrative Support Class	10.95%
Elected Officers' Class	
• Justices and Judges	16.23%
• County Elected Officers	14.34%
• Others	12.38%
Senior Management Service Class	10.67%

<sup>1</sup> Includes the 3 percent employee contribution.

A member vests immediately in all employee contributions paid to the investment plan.<sup>17</sup> With respect to the employer contributions, a member vests after completing one work year with an FRS employer.<sup>18</sup> Vested benefits are payable as a lump-sum distribution, direct rollover distribution, or periodic distribution.<sup>19</sup> Benefit payments may not be made, however, until the member has been terminated for at least three calendar months, except a distribution of up to 10 percent of the member's account may

<sup>13</sup> S. 121.4501(4)(b), F.S.

<sup>14</sup> S. 121.4501(8), F.S.

<sup>15</sup> Art. IV, s. 4(e), FLA. CONST.

<sup>16</sup> S. 121.72(6), F.S.

<sup>17</sup> S. 121.4501(6)(a), F.S.

<sup>18</sup> If a member terminates employment before vesting in the investment plan, the nonvested money is transferred from the member's account to the SBA for deposit and investment by the SBA in its suspense account for up to five years. If the member is not reemployed as an eligible employee within five years, any nonvested accumulations transferred from a member's account to the SBA's suspense account are forfeited. S. 121.4501(6)(b) – (d), F.S.

<sup>19</sup> S. 121.591, F.S.

be authorized after one month if the member has reached his or her normal retirement date discussed below under the pension plan.<sup>20</sup>

### Pension Plan

The pension plan is a defined benefit plan administered by the secretary of the Department of Management Services (DMS) through the Division of Retirement (division).<sup>21</sup> Investment management is handled by the SBA.

Any member initially enrolled in the pension plan before July 1, 2011, vests in the pension plan after completing six years of service with an FRS employer.<sup>22</sup> For members initially enrolled on or after July 1, 2011, the member vests in the pension plan after eight years of creditable service.<sup>23</sup> A member vests immediately in all employee contributions paid to the pension plan.

Benefits payable under the pension plan are calculated based on the member's years of creditable service multiplied by the service accrual rate multiplied by the member's average final compensation.<sup>24</sup> For members of the pension plan initially enrolled before July 1, 2011, normal retirement, which is when a member is first eligible for unreduced benefits, occurs at the earlier of 30 years of service or age 62.<sup>25</sup> For members in the Special Risk and Special Risk Administrative Support Classes<sup>26</sup> enrolled before July 1, 2011, normal retirement is the earlier of 25 years of service or age 55.<sup>27</sup> Members initially enrolled in the pension plan on or after July 1, 2011, must complete 33 years of service or attain age 65, and members in the Special Risk and Special Risk Administrative Support Classes must complete 30 years of service or attain age 60.<sup>28</sup>

### Deferred Retirement Option Program

All membership classes in the FRS Pension Plan may participate in DROP.<sup>29</sup> The program allows an eligible member<sup>30</sup> of the FRS to defer receipt of retirement benefits while continuing employment with the FRS employer. The deferred monthly benefits accrue, plus interest, in the FRS on behalf of the member for the period the member participates in DROP. Upon termination of employment, the member receives the total DROP benefits and begins to receive the previously determined normal retirement benefits.<sup>31</sup>

Eligible members may elect to participate in DROP for a period not to exceed a maximum of 60 calendar months.<sup>32</sup> However, instructional personnel employed by the Florida School for the Deaf and the Blind, instructional personnel in grades K-12, and personnel employed by a developmental research school may participate in DROP for up to 36 calendar months beyond the 60-month period.<sup>33</sup> In addition, a member of the Special Risk Class who is a law enforcement officer and who is a DROP

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<sup>20</sup> S. 121.591(1)(a), F.S., and r. 19.11.003, F.A.C.

<sup>21</sup> S. 121.025, F.S.

<sup>22</sup> S. 121.021(45)(a), F.S.

<sup>23</sup> S. 121.021(45)(b), F.S.

<sup>24</sup> S. 121.091(1), F.S.

<sup>25</sup> S. 121.021(29)(a)1., F.S.

<sup>26</sup> Service in the administrative support position applies towards satisfaction of the special risk normal retirement date if, while in such position, the member remains certified as a law enforcement officer, firefighter, correctional officer, emergency medical technician, or paramedic; remains subject to reassignment at any time to a position qualifying for special risk membership; and completes an aggregate of the years of service as a designated special risk member before retirement which is equal to or greater than the years of service required to be vested. S. 121.0515(8)(a), F.S.

<sup>27</sup> S. 121.021(29)(b)1., F.S.

<sup>28</sup> S. 121.021(29)(a)2. and (b)2., F.S.

<sup>29</sup> A member in the FRS Investment Plan may not participate in DROP. Investment Plan members are considered retired from the FRS when the member takes a distribution from his or her account.

<sup>30</sup> See s. 121.091(13)(a), F.S.

<sup>31</sup> S. 121.091(13), F.S.

<sup>32</sup> S. 121.091(13)(b), F.S.

<sup>33</sup> S. 121.091(13)(b)1.a., F.S.

participant on or after July 1, 2022, may participate for up to 36 calendar months beyond the 60-month period if the participant enters DROP on or before June 30, 2028.<sup>34</sup>

### Employment after Retirement

A member of the FRS is required to terminate employment to begin receiving benefits or begin participation in DROP. Termination occurs when a member ceases all employment relationships with his or her FRS employer.<sup>35</sup> Termination is void if any FRS-participating employer reemploys a member during a specified period.<sup>36</sup> However, an FRS retiree can work for any private employer, for any public employer not participating in the FRS, or for any employer in another state without affecting his or her FRS benefits.<sup>37</sup>

A member who retires from the FRS may not be reemployed by an FRS employer until month seven after retiring or after the member's DROP termination date. If the retiree is reemployed during months seven through 12, the retiree may not receive his or her pension benefit until month 13.<sup>38</sup> However, a retired law enforcement officer may be reemployed as a school resource officer by an FRS-covered employer during months seven through 12 after retirement or DROP termination and receive both a salary and pension benefit.<sup>39</sup>

A retiree employed in violation of the reemployment limitation and the FRS employer are jointly and severally liable for reimbursement to the retirement trust fund from which the benefits were paid. Pension benefits remain suspended until repayment has been made. Benefits suspended beyond the reemployment limitation are applied towards repaying the benefits received in violation of the reemployment limitation.<sup>40</sup>

### Internal Revenue Code

Contributions in the FRS, a 401(a) qualified plan, are exempt from income, social security, and Medicare taxes.<sup>41</sup> In order to maintain this tax qualification, the Internal Revenue Code (IRC) requires a 401(a) retirement plan, such as the FRS, to limit a member's ability to take a distribution prior to termination of employment.<sup>42</sup> The Internal Revenue Service, the federal agency responsible for administering the IRC, has not provided an objective test for determining whether a termination from employment has occurred. Rather, such determination is based on whether the facts and circumstances indicate that the employer and employee reasonably anticipated that no further services would be performed after a certain date or that the services the employee would perform after such date would permanently decrease to no more than 20 percent of the average level of bona fide services performed over the immediately preceding 36-month period.<sup>43</sup> Facts and circumstances considered in such determination include, but are not limited to, the following:

- The individual is no longer treated as an employee for other purposes such as continuation of salary and participation in employee benefit programs.
- Similarly situated employees have been treated consistently.

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<sup>34</sup> Ch. 2022-156, Laws of Fla., codified in S. 121.091(13)(b)1.c., F.S.

<sup>35</sup> S. 121.021(39)(a), F.S.

<sup>36</sup> *Id.*

<sup>37</sup> See s. 121.091(9)(a), F.S.

<sup>38</sup> S. 121.091(9)(c), F.S.

<sup>39</sup> S. 121.091(9)(f), F.S.

<sup>40</sup> S. 121.091(9)(b)1. and (9)(c)3., F.S.

<sup>41</sup> IRS, *Government Retirement Plans Toolkit*, available at: <https://www.irs.gov/government-entities/federal-state-local-governments/government-retirement-plans-toolkit> (last visited March 18, 2023).

<sup>42</sup> See IRC s. 401(a)(36).

<sup>43</sup> The 20 percent level establishes a presumption of termination. In addition, a plan may treat another level of reduction in bona fide services as a separation from service, provided that the level of reduction required is designated in writing as a certain percentage that is greater than 20 but less than 50 percent of the average level of service provided in the immediately preceding 36 months. An employee is presumed not to have terminated employment where the services performed continue at a level greater than 50 percent of the average level of service during the preceding 36-month period. 26 C.F.R. s. 1.409A-1(h)(1)(ii).

- Whether the employee is permitted and realistically available to perform services for other service recipients in the same line of business.<sup>44</sup>

There should be no indication that the employee and employer intended or anticipated for the employee to return to provide any service for the employer when he or she terminated employment. A termination must be bona fide, meaning it is not a mere subterfuge to initiate an otherwise impermissible benefit distribution. Such action would violate s. 401(a) of the IRC and result in disqualification of the retirement plan.<sup>45</sup>

A retirement plan must comply with its terms, even if those terms are stricter than the IRC. Thus, if the plan requires a termination of employment to commence a benefit, such as the FRS, then a termination of employment is required to commence a benefit distribution. Violation of such a requirement would disqualify the plan for federal tax purposes unless corrected.<sup>46</sup>

## Effect of the Bill

The bill authorizes a person who has retired from the FRS to provide volunteer services to an FRS employer without violating the provision of law requiring termination from employment. Specifically, the bill authorizes an FRS employer to establish a post-employment volunteer program that allows retirees to provide civic, charitable, and humanitarian services during the first 12 months following retirement. The volunteer program must operate pursuant to the following criteria:

- Prior to the date of retirement, there was no agreement or understanding between the employer and the retiree that the retiree would provide any service for the employer;
- No form of compensation, including cash equivalents, may be provided to a volunteer for the volunteer services by the employer or any third party;
- Except as otherwise provided in law, no employee benefits, including health or life insurance benefits, may be provided to a volunteer. However, certain perquisites necessary for, and for the limited purpose of, completing tasks associated with the volunteer program, such as an assigned uniform or the provision of equipment, are permissible;
- The number of volunteer hours per week, including training, is limited to no more than 20 percent of the amount of time that was expected of the retiree per week prior to his or her date of retirement;
- A clear distinction between the duties of a volunteer and the duties of an employee is required;
- Volunteers must maintain control of their volunteer schedule, including the number of hours volunteered and assignments for which they agree to volunteer; and
- Adequate volunteer program record keeping must be maintained by both the employer and the volunteer to document adherence to the listed criteria. The records must be made available to DMS or the SBA upon request.

The bill modifies the definition of the term “termination” and provides that termination occurs when a member ceases all employment, including the provision of service, to all employers.

The bill provides that all terminations must be a termination of employment consistent with 26 C.F.R. s. 1.049A-1(h)(1)(ii). The federal regulation provides that whether a termination of employment has occurred is based on whether the facts and circumstances indicate that the employer and employee reasonably anticipated that no further services would be performed after a certain date or that the level

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<sup>44</sup> The regulation provides the following example: an employee may demonstrate that the employer and employee reasonably anticipated that the employee would cease providing services, but that, after the original cessation of services, business circumstances such as termination of the employee's replacement caused the employee to return to employment. Although the employee's return to employment may cause the employee to be presumed to have continued in employment because the employee is providing services at a rate equal to the rate at which the employee was providing services before the termination of employment, the facts and circumstances in this case would demonstrate that at the time the employee originally ceased to provide services, the employee and the service recipient reasonably anticipated that the employee would not provide services in the future. *Id.*

<sup>45</sup> Private Letter Ruling 201147038.

<sup>46</sup> See Rev. Proc. 2021-30, s. 5.01(2).

of bona fide services the employee would perform after such date would permanently decrease to no more than 20 percent of the average level of service performed in the preceding three-year period.

The bill provides that DMS or SBA may require any evidence of termination necessary to determine compliance with Florida laws and regulations.

Finally, the bill makes conforming changes.

## **II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT**

### **A. FISCAL IMPACT ON STATE GOVERNMENT:**

#### **1. Revenues:**

None.

#### **2. Expenditures:**

None.

### **B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

#### **1. Revenues:**

None.

#### **2. Expenditures:**

None.

### **C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

None.

### **D. FISCAL COMMENTS:**

None.