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PROFESSIONAL ASSOCIATION  
ATTORNEYS AT LAW

**MEMORANDUM**

**TO: INTERESTED PENSION CLIENTS**

**FROM: KLAUSNER & KAUFMAN, P.A.**

**RE: BENNETT BILL (SB 1902) & GRADY BILL (HB 1319)**

**DATE: 3/1/2010**

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The purpose of this memo is to summarize pending pension legislation regarding Chapters 175 & 185, Florida Statutes. Senate Bill 1902 (“S.B. 1902”) and House Bill 1319 (“H.B. 1319”) contain substantially similar provisions, but with several important differences, regarding municipal police and fire pensions. S.B. 1902 is primarily focused on Chapters 175 and 185. By contrast, H.B. 1319 adds approximately twenty pages of amendments regarding the Florida Retirement System (“FRS”). H.B. 1319 also requires an extra 1% employee contribution for all public defined benefit plans, and creates a new Chapter 214, Florida Statutes, entitled the “Trust in Accounting Act”. Both bills amend Chapter 112 relating to actuarial projections, reporting, and maximum benefit limitations. H.B. 1319 is entitled the “Public Employee Retirement Preservation Act.” To date, S.B. 1902 lacks a title.

S.B. 1902 was filed by Senator Mike Bennett and referred to the following Senate Committees on February 17<sup>th</sup>: Community Affairs, Governmental Oversight and Accountability, General Government Appropriations, and the Policy & Steering Committee on Ways and Means. Senator Bennett sits on the Police and Steering Committee on Ways and Means and is the Chair of the Community Affairs Committee. At the moment, a companion bill has yet not been introduced in the House. H.B. 1319 was filed by Representative Tom Grady on February 25.

This memo, which is not exhaustive, is intended to highlight the primary provisions of the current drafts of S.B. 1902 and H.B. 1319. This memo will avoid editorializing or otherwise predicting the bills’ chances of passage. Rather, the memo will attempt to dispassionately identify the bills’ far reaching provisions. Recognizing that it is very early in the legislative process, it will be important for readers to follow the bills for any subsequent amendments or future developments.

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Without performing a detailed legal review, it is clear that multiple provisions will invite litigation due to the unanswered questions raised by several of the proposed amendments. Many provisions also raise local autonomy and control issues.

Because it is early in the legislative process, the bills have not yet been summarized by staff. Likewise, the Division of Retirement has not yet commented on the bills. S.B. 1902 will be summarized in the first half of this memo, followed by H.B. 1319. Unless provided otherwise, both bills have July 1, 2010 effective dates.

If adopted in its current form, S.B. 1902 would provide as follows:

- **5 year cost projections:** Section 1 of S.B. 1902 would create a new Section 112.63(1)(g), Fla. Stat., requiring 5 year projections of the plan sponsor's annual required contributions for each of the next 5 years, based on the actual experience of the preceding 5 years. The bill requires that the projections be based on the "actual experience" for the preceding 5 year period and the plan's current assumptions and cost methods.
- **actuarial experience studies:** Section 1 of S.B. 1902 would also create a new Section 112.63(7), Fla.Stat, requiring all retirement plans to prepare an actuarial experience study at least every five years. The required study must compare actual plan experience with key assumptions, including but not limited to investment returns, payroll growth, salaries, retirement rates and turnover. If a plan's actual experience materially varies from a plan assumption, the actuary will be required to explain the variance and provide recommendations.
- **limitation of benefits:** Section 2 of S.B. 1902 would amend Section 112.65, Fla.Stat, by imposing maximum benefit limitations for non-vested employees who have not attained 10 years of service by July 1, 2010. For plans where employees are covered by Social Security, benefits would be capped at 70% of "highest annual base pay," excluding overtime and other additional compensation. The cap would be 90% for employees not covered by Social Security.
- **detailed expense reporting and accounting:** Section 3 of S.B. 1902 would amend Section 112.66, Fla.Stat, by mandating additional accounting and expense reporting by public pension plans. A detailed annual accounting report would need to set forth all administrative expenses, including legal, actuarial, consulting, and travel charges. While such information is already covered by the Sunshine Law, the report would need to be made available to every member of the plan, the plan sponsor and the Department of Management Services.
- **preapproval of an annual expense budget:** Section 3 of S.B. 1902 would also amend Section 112.66, Fla.Stat, to require the preparation of an annual expense budget. The proposed budget would need to be submitted to the plan sponsor for approval at least 120 days prior

to the beginning of the fiscal year. The budget would “regulate” administrative expenses by the pension board, who may not amend the budget without prior approval of the plan sponsor.

- purchasing past special risk service at 3% FRS special risk rate: Section 4 of S.B. 1902 would amend Section 121.0515, Fla.Stat., to permit FRS members to upgrade past special risk service. By paying the full actuarial cost of the upgrade, past service could be upgraded from the current 2% rate to the 3% benefit accrual rate applied on current service. FRS members would have the flexibility to purchase past service at a rate lower than 3%, but the member or employer would need to make the contribution immediately upon notification by the Division of the cost.

Sections 5 thru 19 would amend Chapters 175 and 185 as follows:

- permitting the payment of premium taxes after plan closing/termination: Sections 5 and 13 of S.B. 1902 would amend Sections 175.041 and 185.03, Fla.Stat., to permit the continued receipt of premium tax revenue after a plan has been closed or terminated. Municipalities providing services pursuant to an interlocal agreement would not need to wait 12 months to become eligible to receive premium tax funding.
- revising the definition of pensionable compensation for police: Section 12 of S.B. 1902 would amend Section 185.02, Fla.Stat., to revise the definition of pensionable “compensation” or “salary”. Currently, Chapter 185 treats total cash remuneration including up to 300 hours of overtime as pensionable. S.B. 1902 would redefine pensionable compensation/salary as “fixed monthly” remuneration.
- regulating composition of public safety pension boards: Sections 6 and 14 of S.B. 1902 would amend Sections 175.061 and 185.05, Fla.Stat., to prohibit the majority of the seats on a pension board of trustees from being held by active members or retirees of the plan.
- permitting higher member contributions: Sections 7 and 15 of S.B. 1902 would amend Sections 175.091 and 185.07, Fla.Stat., to permit the membership of the plan to vote to authorize higher member contribution rates. If approved by a majority of the membership, member contributions could be increased without any corresponding increase in benefits.
- deleting requirements to use “additional” premium tax revenue to purchase “extra” benefits: Sections 8 - 9 and 16 -17 of S.B. 1902 would amend Sections 175.162, 175.351, 185.16, and 185.35, Fla.Stat., to allow premium tax revenue to be used for various purposes, including establishing new plans, funding existing plans or for funding FRS contributions. As long as the value of existing benefits “in the aggregate” is equal to or greater than the value of the premium tax received, new “extra benefits” would not need to be funded with future premium tax revenue. It is unclear whether and how this amendment would apply to existing share/supplemental plans.

- permitting continued receipt of premium tax revenue following plan closing/termination: Sections 10-11 and 18-19 of S.B. 1902 would amend Sections 175.371, 175.372, 185.38, and 185.381, Fla.Stat., to permit continued receipt of premium tax revenue following the transfer, merger, or consolidation of services or the decision by a plan sponsor to participate in FRS. In the event that a closed plan became fully funded, the plan sponsor would be permitted to continue using premium tax revenue to reduce contributions for a new retirement system, including FRS.
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H.B. 1319:

If adopted in its current form, H.B. 1319, the “Public Employee Retirement Preservation Act” would provide as follows:

- extra 1% employee contribution: Section 2 of H.B. 1319 would create a new Section 112.049, Fla.Stat., imposing an extra 1% employee contribution for all public employees hired on or after July 1, 2011. The 1% contribution would also apply to DROP participants beginning DROP participation on or after July 1, 2011. The 1% contribution would be applied to gross income and shall be made “before any benefit improvement.”
- 5 year cost projections: Section 3 of H.B. 1319 is substantially similar to Section 2 of S.B. 1902. It would create a new Section 112.63(1)(g), Fla. Stat., requiring 5 year projections of the plan sponsor’s annual required contributions for each of the next 5 years, based on the actual experience of the preceding 5 years. The bill requires that the projections be based on the “actual experience” for the preceding 5 year period and the plan’s current assumptions and cost methods. Unlike S.B. 1902, H.B. 1319 exempts plans with fewer than 20 members. While not required to provide the detailed 5 year cost projections, H.B. 1319 provides that such smaller plans shall be closed if the State Board of Administration determines that the plan sponsor fails to adequately plan for future expenses for 3 consecutive years.
- actuarial experience studies: Section 3 of H.B. 1319 is substantially similar to Section 3 of S.B. 1902. It would create a new Section 112.63(7), Fla.Stat, requiring all retirement plans to prepare an actuarial experience study at least every five years. The required study must compare actual plan experience with key assumptions, including but not limited to investment returns, payroll growth, salaries, retirement rates and turnover. If a plan’s actual experience materially varies from a plan assumption, the actuary will be required to explain the variance and provide recommendations. Unlike S.B. 1902, H.B. 1319 exempts plans with fewer than 20 members. Such smaller plans shall be closed if the State Board of Administration determines that the plan sponsor fails to adequately plan for future expenses for 3 consecutive years.

- limitation of benefits: Section 4 of H.B. 1319 is substantially similar to Section 2 of S.B. 1902. It would amend Section 112.65, Fla.Stat, by imposing maximum benefit limitations for non-vested employees who have not attained 10 years of service by July 1, 2010. Unlike S.B. 1902, which creates different caps depending on whether employees are covered by Social Security, H.B. 1319 imposes a flat 80% cap for all employees based on “average final compensation.” By contrast, S.B. 1902 applies its 70% and 90% caps to highest “annual base pay”. Both bills exclude overtime. H.B. 1319 further provides that “other compensation beyond base hourly or annual salary” may not be factored into any pension benefit.
- detailed expense reporting and accounting: Section 5 of H.B. 1319 is substantially similar to Section 3 of S.B. 1902. It would amend Section 112.66, Fla.Stat, by mandating additional accounting and expense reporting by public pension plans. A detailed annual accounting report would need to set forth all administrative expenses, including legal, actuarial, consulting, and travel charges. While such information is already covered by the Sunshine Law, the report would need to be made available to every member of the plan, the plan sponsor and the Department of Management Services.
- preapproval of an annual expense budget: Section 5 would also amend Section 112.66, Fla.Stat, to require the preparation of an annual expense budget. The proposed budget would need to be submitted to the plan sponsor for approval at least 120 days prior to the beginning of the fiscal year. The budget would “regulate” administrative expenses by the pension board, who may not amend the budget without prior approval of the plan sponsor.
- FRS benefit reductions: Sections 6 through 13 would amend Chapter 121 to reduce FRS benefits as follows:
  - (a) Revise the definition of “compensation” to exclude items in excess of base pay, including but not limited to overtime and accumulated leave;
  - (b) Revise the definition of “average final compensation” to use career earnings rather than the 5 highest years. If records are not available, average final compensation shall be based on the years for which records exist;
  - (c) Revise the definition of “normal retirement date” for persons employed on or after July 1, 2011. Normal retirement would be lowered to age 65 or 33 years of service for the regular class. For the special risk class, normal retirement would be lowered to age 60 with 6 or more years of special risk service, 33 years of special risk service, or age 60 with 25 with years of service, which may include a maximum of 4 years of military service;
  - (d) Impose a maximum cap on FRS benefits to not exceed 80% of final average compensation for members who have not attained 6 years of credited service on or before July 1, 2010;
  - (e) Reduces the regular class multiplier from 1.6% to 1.44% for all service after September 30, 2011;

- (f) Creates an early retirement incentive by increasing the regular class multiplier, expiring on July 1, 2011, to encourage early retirement by those eligible for normal retirement as follows: upon completion of the first year after normal retirement eligibility the multiplier shall increase by 1.87%; 3.125% following the second year after normal retirement eligibility; and 5% following the third year after normal retirement eligibility;
- (g) Reduces the special risk multiplier from 3% to 2.75% for all service after September 30, 2011;
- (h) Reduces the senior management multiplier from 2% to 1.8% for all service after September 30, 2011, up to the member's normal retirement date;
- (i) Revises DROP eligibility for the respective classes based on the new definitions of normal retirement; and
- (j) Revises retirement eligibility for the FRS investment plan (otherwise known as the Public Employee Optional Retirement Program) for persons employed on or after July 1, 2011;

These detailed amendments in H.B. 1319 are not contained in S.B. 1902. Unlike S.B. 1902, H.B. 1319 does not permit the upgrading of past special risk service at the 3% FRS special risk rate.

- benefit reductions for 175 & 185: Sections 14 and 19 would amend Chapters 175 and 185 by revising the definition of "average final compensation" to "all" years of creditable service rather than using a shorter average. If no records exist, average final compensation would mean the compensation for the total number of years for which records exist. The definition of "compensation or salary" is revised to include only base pay. Similar provisions are absent from S.B. 1902.
- regulating composition of 175/185 boards: Sections 15 and 20 of H.B. 1319 are substantially similar to S.B. 1902. Both bills would amend Sections 175.061 and 185.05, Fla.Stat., to prohibit the majority of the seats on a pension board of trustees from being held by active members or retirees of the plan. H.B. 1319 would do so by preventing retirees from being appointed as "5<sup>th</sup>" trustees on 175/185 boards.
- permitting higher member contributions for 175/185 plans: Sections 16 and 21 of H.B. 1319 would amend Sections 175.091 and 185.07, Fla.Stat., to permit the membership of the plan to vote to authorize higher member contribution rates. If approved by a majority of the membership, employee contributions could be increased without any corresponding increase in benefits. This amendment is substantially similar to Sections 7 & 15 of S.B. 1902.
- lower retirement ages for 175/185 plans: Sections 17 and 22 of H.B. 1319 would amend Sections 175.162 and 185.16, Fla.Stat., to lower normal retirement eligibility as follows: (a) to age 60 with 15 years of service, from age 55 and 10 years of service; and (b) to age 57 with 30 years of service, from age 52 and 25 years of service. The bill would raise early

retirement to age 55 with 15 years of service from age 50 with 10 years of service. The normal form of benefit, currently a 10 year certain and life benefit, would be extended to a 15 year certain and life benefit. These amendments are not found in S.B. 1902.

- permitting continued receipt of premium tax revenue following plan closing: Sections 18 and 23 of H.B. 1319 would amend Sections 175.351 and 185.35, Fla.Stat., to permit the continued receipt of premium tax revenue to fund Chapter 175/185 plans until fully funded. These amendments are similar to Section 10-11 and 18-19 of S.B. 1902, but S.B. 1902 would permit the use of premium taxes to fund a DC plan or to pay FRS contributions. H.B. 1319 would not.
- “Truth in Accounting” reporting: Sections 24 through 26 would create a new Chapter 214 titled the “Truth in Accounting Act”. Section 24 of H.B. 1319 would create a new Section 214.101, Fla.Stat, defining terms including but not limited to “amounts due other postemployment benefit plan”, “amounts due pension fund”, “benefit enhancements”, “fiduciary funds”, and “governmentwide generally accepted accounting principles”. Among other things, the definitions would refer to Governmental Accounting Standards Board (GASB) standards 25, 27, 34, 45 and 50. Section 25 would create a new Section 214.102, Fla.Stat, imposing new reporting requirements on the State Chief Financial Officer and the CFO for political subdivisions. Annual reports shall identify items, including but not limited to: fiscal balances, off-balance-sheet pension and OPEB liability, fiscal deficits, benefit enhancements, and the estimated financial state of the employer. The reports would need to be filed with the State’s Chief Financial Officer, the Speaker of the House, and the President of the Senate on or before February 28 of each year, or no later than 120 days prior to the beginning of the fiscal year. The reports shall also be posted online.
- postponing compliance based on good faith determination that costs exceed savings: Section 27 would enable public employers to postpone compliance based on a good faith determination that complying with the provisions of the Act would exceed the estimated savings. For this purpose, “additional administrative cost” would be compared with the savings estimated by the increased employee contributions. Compliance could be postponed until such time as it is determined that the estimated benefits will exceed the estimated costs.

When the Florida Legislature convenes this year on March 2, we anticipate that the legislative session will be dominated by election year politics and the projected \$2.6 - \$3 billion state budget shortfall. Readers may also want to monitor SB 660 which would convert the Florida Retirement System from a defined benefit (DB) plan into a defined contribution (DC) plan for new employees.