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Florida Supreme Court Upholds Right of Legislature to Prospectively Alter Public Employee Retirement Benefits

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On January 17, 2013, the Supreme Court of Florida reversed the decision of a trial court and upheld various legislative modifications to the Florida Retirement System (FRS).[1] The impact of this decision on Florida's budget is nearly $1 billion per year. However, this 4–3 decision also has a national impact, as the plaintiffs were arguing for a rule under the state constitution that would preclude the state and its municipalities from ever reducing the rate of future benefit accrual for employees in the system. A handful of states have adopted such a rule. If Florida shifted into this camp after over 30 years of jurisprudence to the contrary, it would undoubtedly have given an impetus to litigation in other states. As cities and states across the country attempt to reform their sometimes overly generous, underfunded, and expensive retirement plans, the ability to change future benefit accruals is critical to balancing their budgets. This article discusses the issues in *Scott v. Williams* and some of its broader implications.

The FRS is the state's retirement system utilized by various public employees including the state government and agencies, various cities and counties, school boards, colleges and universities, and other

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public entities. The FRS, in which participation is mandatory for the employees of covered employers, offers participants their choice between a defined benefit plan (the pension plan) and a defined contribution plan (the investment plan).

The plaintiffs, comprised of various public employees and public employee unions, filed suit against the defendants, Florida Governor Rick Scott, Attorney General Pam Bondi, Chief Financial Officer Jeff Atwater, and John P. Miles, the secretary of Florida's Department of Management Services, which administers the pension plan. The plaintiffs alleged that the legislation modifying the FRS, which took effect on July 1, 2011, facially violated multiple provisions of the Florida Constitution.

During its 2011 session the Florida Legislature enacted Senate Bill 2100, which was signed into law by Governor Scott and became Chapter 2011-68, Laws of Florida (hereafter, Senate Bill 2100). The Legislature enacted Senate Bill 2100 as a cost-savings measure as it entered its 2011 session facing a budget shortfall in excess of $3.6 billion. Senate Bill 2100 was estimated to produce $1.1 billion in annual savings, with more than $861 million coming just from the two elements of Senate Bill 2100 that were at issue in the litigation.

THE FRS

The FRS is a statutorily mandated retirement system for employees of participating public employers in the State of Florida.[2] As of the effective date of Senate Bill 2100, a total of 992 public employers in Florida, including various state agencies, counties, cities, colleges and universities, school boards, hospitals, and other public entities, participated in the FRS.[3] FRS participation is mandatory for most employees.[4]

Most FRS members are enrolled in the pension plan. For those employees enrolled in the FRS pension plan as of July 1, 2011, benefits are calculated based upon the employee's average compensation during the five years in which they received their highest compensation (the average final compensation).[5] For each year of service, an FRS pension plan member accrues a statutorily-determined percentage of their salary based upon their class of service (the value percent).[6] The value percent ranges from 1.60 percent of salary for "regular class" employees to 3.33 percent of salary for judges.[7] The value percent is multiplied by the number of years for which the member has been an active participant in the pension plan, to determine the total accrued percentage.[8] The annual benefit payable at retirement is calculated by multiplying the accrued percentage by the average final compensation.[9]

As an example, if an employee had a value percent of 3 percent and 30 years of credited service, that employee's accrued percentage would be 90 percent. If the employee's average final compensation was $100,000, the employee's starting annual benefit would be

$90,000 per year (calculated as 90 percent of $100,000). This benefit came with a 3-percent annual cost-of-living adjustment (COLA) until Senate Bill 2100 started to slowly reduce the COLA for employees who retire after July 1, 2011.

In lieu of participation in the defined benefit pension plan, covered employees have the option to participate instead in the defined contribution investment plan.[10]

SENATE BILL 2100

There were two aspects of Senate Bill 2100 that were at issue in the litigation. The first related to the funding mechanism for the FRS. Prior to Senate Bill 2100, FRS was entirely funded by employer contributions. Senate Bill 2100 changed that, requiring all active FRS members to contribute 3 percent of their gross compensation earned on and after July 1, 2011, to the FRS.[11]

Additionally, prior to Senate Bill 2100, beginning with their second year of receiving benefits, pension plan members received a COLA equal to 3 percent of their benefit during the previous year.[12] Senate Bill 2100 changed the COLA for employees who continued to work after July 1, 2011. It provided a pro rata COLA to a member's entire benefit based upon that portion of their employment that was performed prior to July 1, 2011.[13]

For example, if an employee worked for 30 years—from July 1, 1991, through June 30, 2021—then two-thirds (20 out of 30 years) of that employee's work would be prior to the effective date of Senate Bill 2100. In this example, the employee would receive a COLA of 3 percent multiplied by that portion of his or her work that was performed prior to July 1, 2011. Thus, the member would receive a 2 percent COLA, calculated as 3 percent multiplied by 20/30. At trial, our actuarial expert testified that for each plaintiff, the value of pension benefits would increase with future service, even as the COLA percentage decreased, so that there was no reduction in benefits already accrued as of July 1, 2011.

THE LITIGATION

The plaintiffs charged that Senate Bill 2100 violated three provisions of the Florida Constitution. First, the plaintiffs claimed that Florida statutes granted them contractual rights to the FRS system as it existed prior to the enactment of Senate Bill 2100 and that, therefore, the Florida Legislature violated that contract with the enactment of Senate Bill 2100 in violation of Article I, Section 10 of the Florida Constitution, which prohibits laws "impairing the obligation of contracts." Second

and relatedly, the plaintiffs alleged that because of this alleged contractual right, they had a property interest in their future benefits and that, as a result, Senate Bill 2100 operated as a taking of their property without compensation in violation of Article X, Section 6 of the Florida Constitution. Finally, the plaintiffs alleged that because the legislature had enacted Senate Bill 2100 without first engaging in collective bargaining, the law operated as a deprivation of their right to collectively bargain pursuant to Article I, Section 6 of the Florida Constitution.

Of particular importance in the litigation was the "Preservation of Rights" section of the Florida statutes governing the FRS. That section provides that "the rights of members of the retirement system … are declared to be of a contractual nature, entered into between the member and the state, and such rights shall be legally enforceable as valid contract rights and shall not be abridged in any way."[14] The plaintiffs argued that this language granted them contractual rights not only to their previously earned benefits but also to receive at least the same level of benefits for any future work, even though it was acknowledged that FRS members do not have contractual rights to continued employment that provides them benefits in the first instance.

The defendants argued—and the Florida Supreme Court agreed—that the interpretation of this statute had been resolved by the Florida Supreme Court more than 30 years prior in *Florida Sheriffs Association v. Department of Administration*.[15] In *Florida Sheriffs,* the legislature had reduced the amount of pension credit that certain covered employees received for their retirement.[16] When those employees challenged that modification, arguing that they had a contractual right to continue to receive the higher level of credit, the *Florida Sheriffs* court rejected that argument, deciding that this language "was not intended to bind future legislatures from prospectively altering benefits which accrue for future state service," because "[t]o hold otherwise would mean that no future legislature could in any way alter future benefits of active employees for future services, except in a manner favorable to the employee."[17] The *Florida Sheriffs* court noted that this "would, in effect, impose on the state the permanent responsibility for maintaining a retirement plan which could never be amended or repealed irrespective of the fiscal condition of this state" and that "[s]uch a decision could lead to fiscal irresponsibility."[18] As a result, the *Florida Sheriffs* court "conclude[d] that the legislature has the authority to modify or alter prospectively the mandatory, noncontributory retirement plan for active state employees."[19]

The plaintiffs argued, with success at the trial court level,[20] that it was this final quoted language that justified distinguishing Senate Bill 2100 from the change at issue in *Florida Sheriffs*. Specifically, while *Florida Sheriffs* granted the legislature the authority "to modify or alter prospectively the mandatory, noncontributory retirement plan," the trial court held that "absolutely nothing in [*Florida Sheriffs*] can

be read as authorizing the legislature to change the fundamental nature of the plan itself."[21] In other words, the trial court held that while prospective changes within the confines of a noncontributory plan were allowed, the legislature was not permitted to change the nature of the system from noncontributory to contributory. While the trial court acknowledged that changes within a noncontributory plan were allowed, it also struck down the elimination of the COLA even though that was not dependent upon the conversion to a contributory system, describing the elimination of the COLA as a "qualitative change to the plan" rather than a "change to individual components of future accruals within the plan."[22]

A majority of the Florida Supreme Court justices, however, found no basis to distinguish Senate Bill 2100 from the changes at issue in *Florida Sheriffs*. Specifically, the Supreme Court held that "[t]he challengers and the trial court are incorrect in concluding that we intended our decision in *Florida Sheriffs* to apply only to prospective changes within a noncontributory plan."[23] In this regard, the Court reaffirmed that *Florida Sheriffs* held "that the preservation of rights statute was enacted to give contractual protection to those retirement benefits already earned as of the date of any amendments to the plan" and that, as a result, the legislature may "amend a retirement plan prospectively, so long as any benefits tied to service performed prior to the amendment date are not lost or impaired."[24]

In the alternative to arguing that the case over Senate Bill 2100 was distinguishable from *Florida Sheriffs*, the plaintiffs argued—and the three dissenting justices agreed[25]—that *Florida Sheriffs* was wrongly decided and that the relevant statute should be reinterpreted as providing contractual rights to future benefits. However, a majority of the Court declined to overturn that settled principle.[26]

As a result, the Florida Supreme Court upheld the constitutionality of Senate Bill 2100 because it only has the effect of altering benefits earned after it took effect. Thus, the Court held that it did not impair the plaintiffs' contractual rights, which were limited to those benefits they had previously earned and were unaffected by the legislation. Along the same vein, the Court also rejected the Plaintiffs' Takings Clause challenge to Senate Bill 2100 because, in the absence of a contractual right to future benefits, the plaintiffs had no property right to those benefits.[27]

The Court also quickly disposed of the plaintiffs' collective bargaining claims. Prior Florida Supreme Court precedent established that the right of public employees to collectively bargain is only unconstitutionally impaired if legislation affirmatively bars them from bargaining.[28] While Senate Bill 2100 was enacted without requiring the various participating employers to collectively bargain prior to implementation, the Court held that nothing in the legislation prohibited employees and their unions from seeking to bargain over their retirement benefits.[29]

As such, the law did not impermissibly impair their bargaining rights. Although the trial court did find a constitutional violation,[30] the absence of an impairment was relatively noncontroversial for the Supreme Court as only one of the three dissenting justices expressed a belief that there was such an impairment.[31]

THE IMPACT OF THE DECISION

While the Florida Supreme Court's decision resolves the question of prospective changes to public employee retirement benefits under Florida law, many state and local governments have been and will almost certainly continue to look at modifying their retirement systems as a way of achieving cost savings. Those states who have seen legal challenges to such modifications have resolved their questions in different ways. On one extreme, some states allow even retroactive changes to benefits at least until an employee's rights vest, perhaps as late as the date of retirement (indeed, this was the case in Florida prior to the enactment of the Preservation of Rights section).[32] On the other extreme, some states prohibit even prospective changes to benefits.[33]

The grouping in which the Florida Supreme Court held that Florida remains—*i.e.*, those states that permit only prospective changes to benefits—simply places public employees on the same footing as private employees who, under ERISA, only have their previously-earned benefits protected by law.[34]

Moreover, the decision is simply a logical and necessary one for state and local governments facing critical budgetary decisions. As governments face those decisions, if they are unable to reduce their future retirement costs, the alternative decision would likely be to lay off employees, which would eliminate the cost of providing salaries and retirement contributions and benefits. Thus, the push by public employees and their unions to bar states from having needed flexibility to modify retirement systems could amount to favoring some employees/union members over others.

Likewise, if governments were to be provided no flexibility in modifying future benefit accruals in their systems, a single imprudent legislature could effectively cripple a state for years to come. If, during good times, the legislature elected to provide generous benefits and the legislature had no option to reduce those benefits when the good times ended, the government could be forced to provide benefits that it could no longer afford. Indeed, the *Florida Sheriffs* court addressed this very issue when it noted that such a result "would, in effect, impose on the state the permanent responsibility for maintaining a retirement plan which could never be amended or repealed irrespective of the fiscal condition of this state" and that "[s]uch a decision could lead to fiscal irresponsibility."[35] In this regard, the push by public employees and their

unions to prevent such prospective modifications would likely have the effect of preventing legislatures from ever increasing benefits due to the risk that any increase, once provided, could never be revoked.

Undoubtedly, as legal challenges persist to modifications to public employee retirement systems, state and local governments will cite to the Florida Supreme Court's decision as persuasive authority for why they should be permitted–just as private employers are–to prospectively amend their retirement plans for benefits that their employees have not yet earned.

NOTES

1. Scott v. Williams, No. SC12-520, __ So. 3d __, 2013 WL 173955 (Fla. Jan. 17, 2013).

2. *See* Fla. Stat. §§ 121.001, *et seq*.

3. Department of Management Services, Division of Retirement, "Florida Retirement System: Participating Employers 2011."

4. Fla. Stat. § 121.051(1)(a).

5. *Id*. at § 121.021(24)(a)(1). Another change to the FRS resulting from Senate Bill 2100, which was not at issue in the litigation, changed the Average Final Compensation calculation or those employees whose participation in FRS began on or after July 1, 2011, from the five highest compensation years to the eight highest compensation years. *Id*. at § 121.021(24)(a)(2).

6. *Id*. at § 121.091(1).

7. *Id*.

8. *Id*.

9. *Id*.

10. *Id*. at § 121.4501(1).

11. *Id*. at §§ 121.70(2)-(3).

12. *Id*. at § 121.101(3).

13. *Id*. at § 121.101(4).

14. *Id*. at § 121.011(3)(d).

15. 408 So. 2d 1033 (Fla. 1981).

16. *Id*. at 1034.

17. *Id*. at 1037.

18. *Id*. at 1037.

19. *Id*. at 1037.

20. Specifically, the trial court held that "[w]hile *Sheriffs* does authorize the legislature to make prospective alterations to benefits which accrue for future state service *within* the 'mandatory, noncontributory retirement plan,' absolutely nothing in it can be read as authorizing the legislature to change the fundamental nature of the plan itself." Williams v. Scott, No. 2011 CA 1584 (unpublished) (Fla. Cir. Ct. Mar. 6, 2012) (emphasis in original).

21. *Id.*

22. *Id.*

23. Scott v. Williams, No. SC12-520, __ So. 3d __, 2013 WL 173955, *8 (Fla. Jan. 17, 2013).

24. *Id.*

25. *Id.* at *18 (Perry, J., dissenting).

26. *Id.* at *8.

27. *Id.*

28. *See, e.g.*, City of Tallahassee v. PERC, 410 So. 2d 487, 489 (Fla. 1981) (holding that legislation prohibiting public employees from bargaining over "any provisions of the Florida Statutes or appropriate ordinances relating to retirement" violated the constitutional right to collectively bargain); Chiles v. State Employees Attorneys Guild, 734 So. 2d 1030, 1031 (Fla. 1999) (striking down legislation that amounted to a "wholesale ban on collective bargaining by government lawyers.").

29. Scott v. Williams, 2013 WL 173955 at *9.

30. The trial court held that "Senate Bill 2100 abridges Article I, Section 6 by effectively removing the subject of retirement from the collective bargaining process and rendering negotiations after the fact futile." Williams v. Scott, No. 2011 CA 1584 (unpublished) (Fla. Cir. Ct. Mar. 6, 2012).

31. Scott v. Williams, 2013 WL 173955 at *16-17 (Lewis, J., dissenting).

32. *See Florida Sheriffs*, 408 So. 2d at 1037 ("Under the prior case law, if the retirement system was mandatory as it is now, the legislature could at any time alter the benefits *retroactively* or *prospectively* for active employees. … That rule of law has now been changed by the 'preservation of rights' section which … vests all rights and benefits already earned under the present retirement plan so that the legislature may now only alter retirement benefits *prospectively*.") (emphasis in original).

33. *See, e.g.*, Birnbaum v. Teachers Ret. Sys., 152 N.E.2d 241, 245 (N.Y. 1958) (holding that an amendment to the New York Constitution "fix[ed] the rights of the employee at the time he became a member of the system.").

34. *See* ERISA § 204(g), 29 U.S.C. § 1054(g) (the anticutback provision).

35. 408 So. 2d at 1037.