

Unfunded Mandates: The Florida Experience

by J. Stanley Marshall
Chairman of the Board
The James Madison Institute

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EXECUTIVE SUMMARY

- The Florida Institute of Government and The James Madison Institute recently asked Florida city and county managers, “What problem does your jurisdiction encounter most when dealing with state agencies?” More than 70 percent cited unfunded mandates.
- According to Florida Statutes, a mandate is any state action that imposes a cost upon local government by: (1) requiring local government to provide a service or facility without commensurate funding; (2) reducing local government fiscal powers without a corresponding reduction in responsibilities; or (3) requiring a local government to perform an activity that directly or indirectly proves costly.
- In 1990, citizens added Sections 18(a) and 18(b) to Article VII of the state constitution. The amendment states that local governments may reject laws that are in effect unfunded mandates unless certain requirements are met. It also limits the power of the legislature to reduce local governments’ revenue-generating authority and the level of revenues shared with the state.
- House Bill 3075, which increases minimum benefits for firefighter and police officer pension funds, was passed by the legislature in 1998. It rewrites chapters 175 and 185 of the Florida Statutes and significantly changes the requirements that municipalities and special districts must meet to administer police officer and firefighter pension plans.
- HB 3075 requires an increase in the benefits of local pension plans but provides no assurance current revenue sources will be able to pay for this increase.
- Most cities with police and fire pension plans have negotiated special agreements with their departments depending on local preferences and resources. But HB 3075 puts a “floor” under benefits and ignores existing “ceilings.”
- If reintroduced, enacted, and implemented, HB 3075 would use local dollars to pay for benefits mandated by the state. This would allow Florida’s police and firefighters’ unions to do an end run on the city commissions and local citizenries.
- Governor Chiles vetoed HB 3075 but leaders in the legislature have said they may consider it again in 1999, when it will be no less an unfunded mandate.

Unfunded Mandates: The Florida Experience

Unfunded mandates are widely regarded as unwise, unfair, and unpopular. Legislative imposition of government service programs on local governments without the provision of funds to implement such programs causes intergovernmental conflict, obscures the connection between the taxes citizens pay and the services they receive, and denies citizens the right to determine how their tax monies are spent. The federal government has, for many years, imposed requirements on state governments without providing funds commensurate with the added responsibilities. At the same time, states have passed obligations for services on to local governments without either the necessary revenue or sufficient revenue-generating powers. Local governments all too often end up with new obligations but without new monies.

The concerns of local governments over state mandates center on two issues: autonomy and accountability. Local government officials interpret mandates from state government as direct attempts to intrude into their powers and their agendas. They maintain that such mandates are direct violations of the principle of home rule (authority). They point out that if a service or facility is important enough for the legislature to mandate, then it should be important enough to fund, and that the failure of the legislature to provide the necessary funds violates the most basic notion of accountability. Local governments must respond to unfunded mandates either by raising taxes or by reducing services to pay for the new obligations to which they are unwittingly committed. Because someone has to pay for the added government services, an unfunded mandate can justly be called a hidden tax.

The concern over federal mandates imposed on the states is identical to that expressed by local governments on mandates imposed by the states. The issues are still autonomy and accountability. While the U. S. Constitution explicitly limits the authority of the federal government over the states, an overreaching Congress has increasingly extended the federal authority over the states and the progressive enactments of federal jurisdiction have often been expressed as legislative mandates.

What is a Mandate?

Florida statutes define a mandate in clear and concise language. A mandate is any state action that imposes a cost upon local government by requiring local government to provide a service or facility without commensurate funding; by reducing local government fiscal powers without a corresponding reduction in responsibilities; or by requiring a local government to perform an activity that directly or indirectly proves costly.

In 1990, the citizens of Florida adopted a constitutional amendment to Article VII providing local governments the power to resist unfunded mandates. The amendment states that local governments may reject laws that are, in effect, unfunded mandates unless certain requirements are met. The amendment also limits the power of the legislature to reduce local governments' revenue-generating authority and the level of revenues shared with the state. But the definition of an unfunded mandate in the constitution is very general and has been the subject of conflicting interpretations. That seems to encourage special interest groups to slide through the loopholes, making end-runs around the cities and counties who must, in the end, pay the bills.

Mandates

by the Federal Government

Since the 1930s, the government in Washington has used a variety of subsidies to advance federal policies in the states. Under the Johnson administration, for example, federal subsidies were used to fund Great Society programs for job training, special education, health care, and other social programs. Those grants came with strings attached, enabling the federal government to determine how the programs were administered. In the early 1970s, the government began to expand regulatory mandates as the federal budget became tighter and federal grants dried up. Through subsidies, the government focused on the incentives it could provide to motivate local governments to embrace federal policy. Using this approach, the federal government was thus able to impose sanctions on state and local governments for their failure to comply with federal mandates.

The federal government has expanded this use of unfunded mandates for two principal reasons:

1. They offer the government a mechanism for implementing programs popular with voters without raising federal taxes. This is an attractive option for members of Congress, since voters typically favor expanded social programs but oppose increases in taxes.
2. The federal government can justify the imposition of mandates by claiming that states and local governments have not fulfilled their responsibilities under the U. S. Constitution.

Unfunded Mandates in Florida

Unfunded mandates by state government were precisely the actions that the people of Florida intended to discourage when they

added Sections 18(a) and 18(b) to Article 7 of the Florida Constitution in 1990. Section 18(a) states that cities and counties are not bound by the state's general laws unless such laws meet several tests. Among these is a requirement that for any law involving an expenditure of local monies, "funds have been appropriated that have been estimated at the time of enactment to be sufficient to fund such expenditures." Section 18(b) requires a two-thirds vote by both houses of the legislature to "enact, amend, or repeal any general law if the anticipated effect of doing so would be to reduce the authority that municipalities or counties have to raise revenues in the aggregate, as such authority exists on February 1, 1989."

The unfunded mandates amendment to the Florida Constitution was one of the most popular amendments ever adopted. Every county in the state voted for its adoption.

Unfunded Mandates in the 1998 Legislature

The Legislative Committee on Intergovernmental Relations (LCIR) of the Florida Legislature reports mandates passed at each legislative session. The mandates reported either have or do not have fiscal impact. The purpose of the LCIR report is to disclose mandate provisions passed by the state. The LCIR had not, at the time this *Backgrounder* was prepared, released its report on the 1998 legislature. The James Madison Institute's analysis of bills passed by the 1998 session, however, identified a number of bills that, by any reasonable definition, would be considered unfunded mandates. The estimates were gathered from house and senate fiscal analysis, as produced by legislative analysts. For example:

- HB 1093 provides an ad valorem tax exemption of \$25,000 for each unit in a certified continuing-care facility. The

negative fiscal impact on local government is estimated at \$1.5 million. The bill was passed by more than a two-thirds vote of the house and senate.

- HB 3491 significantly impacts the Florida retirement system. It requires the employer of each member of a state-administered retirement plan to contribute 0.94 percent of gross compensation each pay period. This represents an increase of 0.28 percent, which will be used to fund the retiree health-insurance subsidy increase. \$38.4 million of the subsidy falls upon local governments.
- HB 3229 provides sales and use tax exemptions for equipment used for pollution control related to tangible personal property. The fiscal impact is estimated to be \$900,000 in fiscal year 1998/99 and \$2 million each year thereafter.
- HB 3075 increases minimum benefits for fire and police pension funds. The state has not officially carried out an actuarial study of the fiscal impact on local governments. An estimate by the Florida League of Cities sets an approximate cost at \$50 million.

JMI's Interest in the 1998 Unfunded Mandates

In our customary review of the proceedings of the Florida Legislature, our attention was directed to several bills considered in the 1998 session that appear to be unfunded mandates. Among that group, HB 3075 stood out. In line with the Institute's mission of informing Floridians about their government and calling attention to actions by government

that we believe do not represent the best interests of citizens, our researchers considered the following questions in their analysis of HB 3075:

- Does HB 3075 conform to the Florida Constitution in letter or in spirit?
- In lobbying legislators, have the sponsors of HB 3075 presented reliable information on the funding sources and mechanisms for the benefits provided by the bill? Have its adverse effects been overstated or underestimated?
- Are the estimates of costs by the bill's proponents realistic? Has the state officially released an estimate cost?
- Is it reasonable to expect that the growth in state taxes would be sufficient to fund the increased expenditures? Was other legislation passed in the 1998 session that affects the revenues generated by the insurance premium tax?
- Is there evidence that pension benefits for police and firefighters are inadequate when compared with those for other city employees?
- Are management mechanisms – decisions by boards of trustees of pension plans, for example – facilitated by the legislation?

In the light of these and other questions about these unfunded mandates, the Institute has reviewed HB 3075 and has produced this report to call the attention of government

officials to legislation that we believe is both bad public policy and bad politics.

The Institute does not express a view as to whether enhancements in the pension plans of police and fire personnel are desirable. That question is beyond the scope of this *Backgrounder*. Our interest is in unfunded mandates generally, and HB 3075 specifically, as we consider whether this legislation is the kind of public policy Florida voters would approve if they were fully informed about its impact on city governments.

We believe that accurate and reliable information has not been made available to the general public in regards to both the benefits and adverse effects of HB 3075. In retrospect, it appears that the votes to approve the pension bill in both the Florida House and Senate may have been based on unclear and distorted assumptions. The purpose of this report is to improve the level of understanding of this issue and, therefore, the quality of Florida government.

HB 3075: The Worst of the Unfunded Mandates

HB 3075 was passed by the Florida Legislature in 1998 after a fierce battle between Florida cities and the police and firefighter unions. According to the unions, the bill's main purpose is to establish uniform benefits for police officers and firefighters statewide. It essentially rewrites the two chapters of the Florida Statutes (175 and 185), and makes significant changes to the requirements that municipalities and special districts must meet to administer police officer and firefighter pension plans.

Florida now has approximately 383 such plans in operation: 36 of these are referred to as chapter plans and 347 are called local law plans. The distinctions between these two is not important in this report

except to note that local law plans have greater latitude in developing their own unique pension programs. (The table shows how many local law plans and chapter plans existed as of November 1998.) The impact on 234 cities throughout the state having local law plans would very likely be increased pension costs, lessened city control over pensions, and increased local taxes to fund the increased pension benefits. The impact on Florida cities has been estimated at \$50 million a year¹.

Table
Chapter Plans and Local Law Plans in
Florida

Source: State of Florida, Division of Retirement, Current Actuarial Valuations and Plan Documents, 1998.

HB 3075 gives the pension boards that administer municipal police and firefighter pensions the power to divert the income from premium tax funds into a separate supplemental plan to pay extra benefits to firefighters and police officers.² HB 3075 also requires that the additional premium tax funds awarded be used in their entirety to provide extra benefits to firefighters and police officers.³ These are defined as benefits in addition to or greater than those provided to other city employees. This change would significantly impact the cities' current funding mechanisms.

HB 3075 also makes extensive changes to the definitions of compensation and credited service for time in the military. It also redefines the terms “police officer” and “firefighter” to permit optional participation by police and fire chiefs. These and other definitional changes significantly impact the operation and funding of many of the plans.

The bill also states that the minimum benefits and minimum standards contained in it cannot be reduced or offset by any other local, state, or federal law that might include firefighters or police officers in its operation. Social security benefits, for example, are sometimes coordinated with pension benefits; such plans would have to be modified under this bill.

Under HB 3075, all local law plans would have to accept new standards for disability determinations as to when police officers or firefighters are unable to perform their duties, permitting injured police and fire fighters to be placed in less strenuous jobs rather than requiring their retirement.

And finally, Florida statutes require that an actuarial impact statement be prepared before any state or local government entity can amend its defined benefit pension plans. HB 3075 implements wholesale significant amendments without the benefit of any actuarial studies or cost estimates.

Issues, Concerns, and Flaws

The pension legislation (HB 3075) contains significant flaws, misconceptions, and unrealistic assumptions. Among the shortcomings of the law are provisions that would make its enforcement difficult, would erode the connection between citizens and their government, and would impose a significant tax burden on many of Florida’s cities by mandating benefits for a few to be paid for by the citizens at large. In addition, passage of the act would condone and reward an exercise in

raw political pressure by the fire and police unions of a kind that citizens have a right to expect their legislators to resist. The following points represent some facets of the bill that are subject to debate and criticism.

When the legislature first considered the pension bill, it lacked clear information on the bill’s implications. The analysis by the senate staff of the companion bill (SB 270) concluded that the bill imposed an unfunded mandate on local governments. The house staff reached a different conclusion. Various interest groups also offered conflicting opinions. The police and fire unions claimed that money to fund the pension enhancements is, or will become, available through revenue growth from an existing tax on insurance premiums (the insurance premium tax). Revenues from this tax fund make up 16 percent of the fire and police pensions. Advocates for Florida’s cities and fire districts countered that these revenues are already assigned to cover existing pension benefits.

The central question dividing analysts, interest groups, and legislators is whether the legislation is or is not an unfunded mandate. The question centers on two issues.

- First, the definition of unfunded mandates as stated in the constitution should be applied.
- Second, if issues related to pension funds are the subject of an unfunded mandate dispute, then researchers should inquire as to the legislative language related to Florida’s insurance premium tax.

Under existing legislation, pension plans for firefighters are supported in part by a 1.85 percent levy on property insurance premiums. Police plans are partially funded by a 0.85 percent tax on casualty insurance premiums.

As a general rule, both of these revenue sources amount to less than 20 percent of the pension plans' total cost. The other revenue sources include employee contributions, city payments, investment earnings, gifts, and employee fines.

Another issue is whether the insurance premium tax is a state revenue source, and opinions on this question differ sharply. Depending on perspective and interpretation, the labeling of these funds is central to the issue of unfunded mandates. If the position taken supports identifying these funds as shared resources, then the implications suggest that local governments also have a say on the expenditure of these funds. If the position is taken that supports labeling these funds as pure state revenues, then the implications suggest that the state is the sole decision maker on the expenditure of these monies. In fact, the state does collect the tax, but does so on behalf of the cities. The taxes are actually levied by ordinance at the city level; the state collects the revenue statewide and then remits to the participating cities the monies generated in those cities. If the insurance premium tax is not a local revenue source, then certainly it should be considered a shared source.

In essence, HB 3075 proposes the following:

- It requires significant changes to current standards and processes. Modifications to current law include, but are not limited to, increased pension payouts required by changes in the definition of salary, and funding and contribution changes lowering the minimum employee contribution from 1 percent to .5 percent.
- HB 3075 would further erode the connection between citizens and their governments. Representative government depends on accountability. Gov-

ernment officials, especially elected officials, must be forthright in advocating taxes and in showing what benefits the revenues from these taxes will provide. Only when this connection is visible to voters are they able to make informed decisions about taxes and benefits. HB 3075 places government officials in a position to which most seriously object. It forces an erosion of accountability and thus is not just bad policy; it is bad politics.

No matter how HB 3075 is interpreted, one thing is very clear when it comes to costs: the bill requires an increase in the benefits of local pension plans and yet provides no assurance that current revenue sources will be able to pay for this increase. Under Section 18(a) of the Florida Constitution, the burden of proof that the funding will be adequate rests with the pension bill's proponents. Without such an analysis, the legislature is being asked to decide on the basis of a wish about future economic and fiscal circumstances. This is not the way sound public policy is made.

If HB 3075 were sound policy, legislators might want to support it even though it is an unfunded mandate. Section 18(b) of Article VII of the Constitution allows for this possibility. If two-thirds of both houses of the legislature support the bill, then the prohibitions in Section 18 are overridden. This was the case for HB 3075 in the 1998 legislative session; the bill received more than two-thirds of the vote in both the house and the senate. However, it seems clear that legislators were voting on the basis of incomplete and conflicting information.

Now that the legislation has been more carefully reviewed, its problems have become more apparent. The bill's principal weakness is that it is a one-size-fits-all policy. Pension

plans in Florida are quite diverse. Chapters 175 and 185 of the Florida Statutes authorize somewhat standardized plans. However, these chapter plans, as they are called, are comparatively few. Local law plans are adopted by resolution, by special acts of the legislature, or by municipal ordinance and are unique to each municipality. These plans are often agreed to by police or firefighter unions through the collective bargaining process.

Thus, most cities with police and fire pension plans have negotiated special agreements with their departments. Some may have, for example, lower benefits but higher salaries. Others may have extensive health benefits and pension benefits but lower salaries. Others may produce benefits that exceed chapter plan benefits in some categories but do not meet them in others. It all depends on local preferences and resources.

HB 3075 seeks to standardize local police and fire pension plans by establishing minimum standards and benefits for all plans funded by revenues from the insurance premium tax. The problem with this one-size-fits-all approach is that it would reconfigure all of these plans without regard to their special characteristics. A city that paid high salaries in return for lower pension benefits would be forced to increase the latter but would have little, if any, ability to offset this increase with corresponding salary reductions. Similarly, cities that have offered very high pension benefits in one area in return for lower benefits in another part of their pension plan would have the lower benefits increased but would not see benefit reductions elsewhere.

In short, HB 3075 puts a “floor” under benefits but pays no attention to existing “ceilings.”

Conclusion

HB 3075 is an unfunded mandate of the worst

sort. If enacted and implemented, it would use local dollars to pay for a benefit mandated by the state. In effect, this would be allowing Florida’s police and firefighters’ unions to do an end run on the city commissions and local citizenries. State legislators would get credit from the unions for delivering an expensive benefit, but they would not have to face the voters and ask whether they are willing to pay for this benefit with their tax dollars.

Unions representing police officers and firefighters have frequently attempted to use the mechanisms of state government to increase pension benefits for their members. The state agencies that administer and oversee public pension plans have also attempted to increase benefits on their own initiative, usually through administrative rule. When these efforts have failed, the unions have made frequent attempts to persuade the legislature to increase benefits. Most attempts have failed but the bill passed by the 1998 legislative session would have cost Florida cities an estimated \$50 million a year to pay for the increase in benefits mandated by HB 3075.

In summary, HB 3075 was enacted by the Florida Legislature to increase minimum benefits and standards for police and firefighters employed by cities. Gov. Chiles vetoed this legislation. But in his veto message, he stated that the bill “contains provisions which are confusing and frequently misleading,” including the proper use of state tax funds, the definition of extra benefits, and the clarification of the authority of pension boards of trustees. The governor ended his veto message by encouraging the affected parties to perform additional work and further refine the legislation to address its flaws. He seemed willing to sign the legislation if it were to appear before him again and if the bill corrected certain technical flaws but would leave intact its major provisions.

The Need for Pension Reform: Real or Contrived?

The main purpose of HB 3075 was to increase pension benefits for police and firefighters employed by the cities. It is appropriate then to ask whether the present benefits are adequate. Are police and firefighters denied benefits people in those vocations should expect to receive? Are there abuses in the present retirement plans? Do the state legislators who passed HB 3075 have different expectations from the local government officials who must pay the bill? And what tactics did union representatives use in lobbying for the bill?

Various sources, including the *St. Petersburg Times*, claim that the current system contains large loopholes that encourage abuse and fraud and these have cost taxpayers millions of dollars in undeserved benefit payments. Such abuses are encouraged by the pension fund's broad definition of disability. Here are some examples:

- In Delray Beach, a city of just under 50,000 people and a general revenue budget of about \$35 million, \$2 million is allocated for pension benefits. Its pension plan awards disability benefits to public safety officers who are 1 percent or more disabled; these officers may then retire at 75 percent of their current pay. Delray Beach has had six disability retirements during the past year. Because disability is so broadly defined, it is tempting for officers to claim it fraudulently.
- In the Tampa Bay area, more than 500 police and firefighters retired on disability pensions in 1996. In St. Petersburg, one in eight did so, and in Largo and in Clearwater, one in three. Physical impairment is not the only route in which a public safety officer can request disability pay; depression has become an increasingly popular ailment for claiming pension benefits. Those who make disability claims receive two benefits: a generous tax-free payment and the freedom to move to another municipality to resume one's career at full pay.
- A Clearwater firefighter who retired on a disability pension claiming a back injury now operates an antique shop in Dunedin where his duties include lifting and moving furniture. His pension is \$1,305 a month. A St. Petersburg fire officer retired with a monthly pension payment of \$2,020 because of injuries to his back, neck, and shoulder. He is now employed as chief of the Largo Fire Department where he receives a \$4,905 monthly salary.
- In Hallandale, a police officer filed a claim for disability retirement due to colitis. Colitis is documented medically as a hereditary abnormal condition, not caused but aggravated by stress. Nevertheless, this employee is claiming that the condition is caused by stress on the job and that she is entitled to 75 percent of salary under a job-related disability pension, in addition to workers' compensation and social security benefits.
- Another police officer had a hip replacement, which left him out of work for five months. He then was out for another three months due to stress and was under the care of a psychologist. The city determined that he had reached maximum medical improve-

ment (MMI) and told him that he was under disability termination. They added two weeks' separation pay in addition to terminal benefits, and during the two weeks, the officer had a heart attack. He will receive full benefits and is eligible for a 75 percent of salary job-related disability pension, plus workers' compensation and social security disability benefits. Workers' compensation, if under total and permanent disability (which heart disease and hypertension are), includes a 5 percent cost of living increase per year for life.

- A firefighter who smokes two packs of cigarettes a day is under medication for high blood pressure and obesity. Under Florida law, this employee is paid 75 percent of salary in addition to workers' compensation and social security. The law presumes that hypertension, tuberculosis, hepatitis, and heart disease are always job related.

The unions and other HB 3075 supporters lend a deaf ear to cases similar to these and maintain that pension provisions in current law are inadequate, especially benefits for disability. This bill broadens the application of disability and thus promotes further abuses.

Labor unions claim that HB 3075 will not incur new costs. They insist that if current state revenue contributions are not adequate to fund the additional benefits to meet the minimum requirements, the incremental increases will be provided only as state monies become available. The unions claim that normal revenue growth from the tax will cover the anticipated costs of the increased pension benefits, but that claim is

highly unrealistic.

Gov. Chiles' veto of the act has prevented the legislature from imposing an unfunded mandate on Florida's cities. Leaders in the legislature have said they may consider it again next year, but HB 3075 in 1999 will be no less an unfunded mandate.

Notes

- ¹ This estimate is provided by the Florida League of Cities.
- ² Insurance premium taxes are taxes collected by the state on insurance companies doing business in the state. The monies are then reverted back to the cities as a "credit," and the cities may choose whether to levy this credit.
- ³ For example, if one year a city is awarded \$10 million and the next fiscal year the same city is awarded \$15 million, then the difference of \$5 million is subject to the provisions of HB 3075. Even if only the growth dollars from the insurance premium tax were used to pay for the increased pension benefits mandated by HB 3075, there is no reason to expect these revenues to be adequate. The Florida Division of Economic and Demographic Research analyzed the tax's revenue history between 1980 and 1996, a period of rapid population growth in the state. The research found that revenues from the insurance premium tax grew on average by 8.12 percent annually. While this is a relatively high rate of growth, the growth of expenditures can be expected to be equally high. It is undeniable that revenue grows with inflation and population, but so do pension benefits and the number of local police officers and firefighters.

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