

SENATE THIRD READING
SB 278 (Leyva)
As Amended March 23, 2021
Majority vote

SUMMARY

Establishes requirements relating to the reporting of disallowed compensation by state, school or contracting agency employers to the California Public Employees' Retirement System (CalPERS) and retirement benefits paid to CalPERS retirees and their survivors or beneficiaries, among other provisions.

Major Provisions

- 1) Provides that if CalPERS determines that compensation reported by the state, school employer, or a contracting agency is disallowed compensation, CalPERS must require the state, school employer, or a contracting agency to discontinue reporting the disallowed compensation; however, this only applies to determinations made on or after January 1, 2017, if an appeal is filed and the member, retired member, survivor, or beneficiary has not exhausted their administrative or legal remedies.
- 2) Establishes that for an active CalPERS member, all contributions made on the disallowed compensation must be credited against future contributions to the benefit of the state, school employer, or contracting agency that reported the disallowed compensation, and any contribution paid by, or on behalf of, the member including contributions, must be returned to the member by the employer that reported the disallowed contribution.
- 3) Establishes for a retired member, survivor, or *beneficiary* whose final compensation at the time of retirement was predicated upon disallowed compensation, the contributions made on such compensation must be credited against future contributions to the benefit of the state, school employer, or contracting agency that reported disallowed compensation and CalPERS must permanently adjust the benefit of the affected retired member, survivor, or beneficiary to reflect the exclusion of the disallowed compensation.
- 4) Provides that if the immediately aforementioned conditions are not satisfied, the employer participating in CalPERS that reported the contributions on the disallowed compensation must: a) Pay to CalPERS, as a direct payment, the full cost of any overpayment of the prior paid benefit made to an affected retired member, survivor, or beneficiary resulting from the disallowed compensation; and, b) pay to the retired member, survivor, or beneficiary, as a lump sum or as an annuity based on that amount, the actuarial equivalent present value (AEPV) representing the difference between the monthly allowance that was based on the disallowed compensation and the adjusted monthly allowance calculated, as specified, for the duration that the allowance is projected to be paid by the system to the retired member, survivor, or beneficiary.

Here, the payment or payments must be made by the state, school employer, or contracting agency that reported the contributions on the disallowed compensation as an annuity unless the retired member, survivor, or beneficiary and that the state, school employer, or contracting agency, as may be applicable, mutually agree to a lump sum payment or payments. In addition, for educational entities participating in CalPERS, the final responsibility for funding prescribed payments is that of the educational entity that is the

actual employer of the employee. A county superintendent of schools must have final responsibility for funding payments for its own employees and not those of other educational entities that participate in CalPERS under the auspices of a county superintendent of schools pursuant to contract.

- 5) Authorizes a state or local public agency employer, including a school district, participating in CalPERS to submit an additional compensation item to the system for review that is proposed to be included, or contained, in an adopted memorandum of understanding (MOU) or collective bargaining agreement entered into on and after January 1, 2022, that is intended to form the basis of a pension benefit calculation, for consistency of the proposal with the Public Employees' Pension Reform Act, certain Sections of the Government Code relating to compensation earnable, and CalPERS' administrative regulations.

Here, the submittal is limited to only the compensation item language and a description of how it meets certain criteria along with any other supporting documents or requirements as deemed necessary by CalPERS to complete its review.

COMMENTS

- 1) Financial Clawbacks from Retirees and Permanent Reductions to a Lifetime Retirement Benefit... Even After Years Into Retirement.

The pension promise is a reasonable expectation that is a naturally inherent part of the components to public employment, and contract (i.e., offer, acceptance, and exchange of consideration), and requires satisfactory performance of the contractual obligations by each party to the agreement. To receive the pension promise, the promise remains only if the employee has vested (i.e., obtained a legal entitlement) by reaching the statutorily requisite minimum age and years of service to retire and receive a pension under historical and existing California law, and by long-standing and well-established judicial interpretation. In *Kern v. City of Long Beach* (1947) 29 Cal.2nd 848, the court stated that, "[a] pension right constitutes something more than a mere gratuity."

CalPERS, pursuant to existing law (and judicial interpretation, if applicable), determines whether certain compensation items reported and remitted to it by an employer are permissible (i.e., allowable). Any items deemed as impermissible (and removed from the retirement benefit calculation) are due to substantial changes to public employee retirement law resulting from enactment and effectuation of the Public Employee's Pension Reform Act (PEPRA) of 2013, other Sections of the Government Code, and judicial interpretation, to which CalPERS is obligated to abide.

- 2) Please see the policy committee analysis for a full discussion of this bill.

According to the Author

"[This bill] protects a retiree's already promised and paid-for collectively bargained benefits in cases where the benefit is disallowed by CalPERS after the member has already retired. It also sets parameters for resolving future disputes over active and retired employees' collectively-bargained pensionable compensation.

"In 2012, after serving the public for nearly 30 years, a firefighter employed by the City of Davis retired. Prior to retiring, the firefighter requested an official retirement estimate from CalPERS,

which provided a projection of retirement benefits as of the firefighter's estimated retirement date. Based on the information provided by CalPERS in their official retirement estimate, the firefighter made the decision to retire."

The author further states that, "[i]n 2017, CalPERS notified the long-retired firefighter that the City of Davis had reported certain disallowed compensation, which CalPERS believed was not pensionable compensation. Consequently, CalPERS sought to collect the overpayment reimbursement – not from the City of Davis that had mistakenly reported the special compensation, but from the retired firefighter. The reimbursement sought by CalPERS included a lump sum amount of \$42,000 and a sizable future reduction in the retired firefighter's monthly retirement allowance.

"Unfortunately, several other firefighters, law enforcement, and school retirees have also reported similar stories across multiple CalPERS employers."

Arguments in Support

Among other things, the California Professional Firefighters state that, "Generations of hard-working members of California's middle class have dedicated their careers to public service – often earning less over the course of their career when compared to their private industry counterparts – to earn and pay for the promise of a secure retirement.

"Employers have a legal and actuarial obligation to correctly report pension-eligible compensation to CalPERS as a result of employer bargaining. If an item of compensation is later determined to be improper, it is appropriate policy to require the employer to bear the actuarial liability of that promise made to their retiree. It is the employer's sole responsibility to ensure that any offers for compensation be consistent with state law and regulation for the express purpose of correctly calculating an employee's future service credit and final compensation for retirement. It is also the employer's obligation to meet and confer with the employee organization regarding the disputed item of compensation to immediately remedy the error with respect to active employees. [This bill] would protect the promised and paid for pensions of CalPERS retirees through a number of mechanisms, as well as putting in place steps to ensure that similar miscalculations do not happen again in the future."

Arguments in Opposition

A coalition of local public agency employers, including schools, state in part that, "[This bill] removes all responsibility by CalPERS to ensure benefits are reviewed, calculated and administered correctly. [The bill] places sole responsibility on the employer – even if the employer exercises their right to have CalPERS review their compensation proposal, [as provided in the bill]." In addition, "[g]iven [that] there are nearly 3,000 local government employers in CalPERS – many with multiple bargaining units with varying degrees of sophistication and understand of the compensation rules, the [provisions] would not provide any safeguards for retirees, active employees or public employers. The lack of accountability by the administrator of public retirement benefits would lead to more confusion and compliance challenges for public agencies."

The coalition further states that, this bill would "... create compliance and implementation issues" because "[employers] would now be issuing payments to retirees by diverting resources from their general funds. Even though direct payments to retirees would be made outside of the retirement system, such liabilities would trigger [General Accounting Standards Board] reporting requirements..." and "... agencies would have to track and report these liabilities. Such

additional responsibilities would require agencies to hire costly outside actuarial and legal experts to ensure that they follow federal reporting laws."

Opponents conclude by stating in part that, "... public agencies simply cannot continue to make payments directly to a retiree for an unlawful benefit. The moral hazard of assigning the financial liability of errors solely to the employer creates an incentive for organizations locally to bargain for benefits that the MOU declares to be pensionable. [This bill] will guarantee those employees a retirement benefit because the MOU treated them as such, in contravention of how state or federal law may treat those benefits. In the most egregious of examples, local parties may agree to MOU terms that (knowingly or not) violate state pension spiking laws. [This bill] would enshrine, rather than correct, those violations in perpetuity."

FISCAL COMMENTS

According to the Assembly Appropriations Committee, this bill would result in the following:

- 1) Ongoing implementation costs to CalPERS, likely in the low hundreds of thousands of dollars annually, with potentially decreasing costs over time, to calculate employer costs in cases when a retirement benefit must be adjusted and to review additional labor memoranda of understandings submitted by employers to ensure they are compliant with laws and regulations. Costs to calculate employer costs would decrease over time.
- 2) Unknown General Fund (GF) or Proposition 98 GF costs to the extent state agencies, public school employers or a CalPERS contracting agency must cover the costs of disallowed payments to their retirees. However, these entities contributed disallowed payments on their employee's behalf and CalPERS provides these disallowed payments back to employers. Employers could use these paybacks to offset costs.

VOTES

SENATE FLOOR: 35-0-5

YES: Allen, Archuleta, Atkins, Becker, Bradford, Caballero, Cortese, Dahle, Dodd, Durazo, Eggman, Glazer, Gonzalez, Hertzberg, Hueso, Hurtado, Jones, Kamlager, Laird, Leyva, Limón, McGuire, Min, Newman, Ochoa Bogh, Pan, Portantino, Roth, Rubio, Skinner, Stern, Umberg, Wieckowski, Wiener, Wilk

ABS, ABST OR NV: Bates, Borgeas, Grove, Melendez, Nielsen

ASM PUBLIC EMPLOYMENT AND RETIREMENT: 7-0-0

YES: Cooper, Voepel, Calderon, Cooley, O'Donnell, Rodriguez, Seyarto

ASM APPROPRIATIONS: 15-0-1

YES: Lorena Gonzalez, Bryan, Calderon, Carrillo, Chau, Megan Dahle, Davies, Fong, Gabriel, Eduardo Garcia, Levine, Quirk, Robert Rivas, Akilah Weber, Kalra

ABS, ABST OR NV: Bigelow

UPDATED

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