

Public Pension Reform (AB 340 and AB 197): A Primer

IV. Frequently Asked Questions

1) Current Members and New Members

Q. Which provisions of AB 340 as amended by AB 197 affect current members?

A. AB 340, as amended by AB 197, not only creates the Public Employee Pension Reform Act (“PEPRA”), but also modifies existing law for current employees.

The provisions affecting current employees include (all citations are Government Code):

- normal cost sharing (Section 20516.5),
- sharing the cost of the employer’s contribution (Section 20516)
- definitions of “new employee” and “new member” that delineates rights for individuals with status in systems prior to Jan. 1, 2013 (Section 7522.04(e) and (f))
- restrictions on retiree employment (Section 7522.56)
- prohibition of advantageous vesting periods for retiree health benefits (Section 7522.40)
- elimination of pension abuses, for example
 - elimination of airtime (Section 7522.46)
 - prohibiting pension holidays (Section 7522.52)
 - no retroactive benefits (Section 7522.44)
 - limitation on elected officials benefits (Section 7522.48)
 - industrial disability for safety (Section 7522.66)
 - loss of pension for certain felonies (Sections 7522.72-7522.74)
 - prohibition against exceeding IRS limits (Section 7522.42), and
 - significant increases in compensation (Section 20791).

Significant Provisions Covering Current Employees

Agencies should focus on the following provisions for current employees that can have substantial long-term impact on pension costs:

1. Cost Sharing: 50 percent Normal Cost, Employer Paid Member Contribution (EPMC), and Employer’s Contribution.

50 Percent Normal Cost Sharing and Elimination of EPMC (Government Code Section 20516.5)

Unlike the mandatory provisions for new members, the cost sharing provisions for current CalPERS members are goals. Even though Government Code Section 20516.5(a) states that it “shall be the standard that employees pay at least 50 percent of normal costs and that employers not pay any of the required employee contribution,” current represented members are specifically allowed to pay less than the standard of 50 percent of the normal cost of pensions until Jan. 1, 2018 (Government Code Section 20516.5(b)). Prior to that date the 50 percent sharing of normal costs cannot be unilaterally imposed by the agency, even after good faith negotiations. In addition, after Jan. 1, 2018, public agency employers can

negotiate, and unilaterally implement if necessary, 50 percent of normal cost, but only up to 8 percent of pay for non-safety members, 12 percent of pay for police and fire members, and 11 percent of pay for other local safety members. (See Government Code Section 20516.5 and Section III, "Duty to Bargain")

For unrepresented current employees, an employer may implement, prior to Jan.1, 2018, 50 percent of normal cost or up to the pay caps of 8, 11, and 12 percent for non-safety members, local safety members and police and fire members, respectively. Because Government Code Section 20516 allows cost sharing to be implemented by bargaining unit, the 50 percent normal cost sharing and elimination of any EPMC may be implemented for unrepresented employees at the discretion of the agency.

Sharing the Costs of Employer's Contribution and Implementing by Bargaining Unit (Government Code Section 20516)

Government Code Section 20516 was amended in two significant ways. First, the amended section allows up to the entire employer's contribution (both normal and Unfunded Actuarial Accrued Liability costs) to be paid by the employees. Prior to the amendment of Government Code Section 20516, employees could share only the actuarially determined costs of an optional benefit or formula. The amended section allows employees to pay the employer's contribution, regardless of a change in benefits. Second, the amended section allows "cost sharing" to be implemented by bargaining unit. Previously, cost sharing could only be implemented by the traditional employee groupings such as miscellaneous, fire, and police. Reaching such agreements with all the bargaining units within a specific grouping was highly improbable. For example, some agencies would have to reach the same cost sharing agreement with more than a half dozen miscellaneous employee bargaining units before the change could apply to the miscellaneous group. As amended, Section 20516 still requires employers to reach an agreement with a represented employee group. Section 20516 does not allow unilateral implementation after impasse with represented employees. By implication, however, there are no restrictions against implementing employee partial or full payment of the employer's contribution by non-represented employees.

Q. How do these reforms impact current members who do not have five years of service?

A. These reforms do not alter the waiting-period for becoming eligible for certain pension rights.

There are two distinct uses of the term "vesting" when it comes to pension benefits. One is the Constitutional vesting of California employees' pension benefits that is derived from a series of California Supreme Court decisions. In short, the courts have determined that each employee's pension benefits vests on the first day of employment as a promise of future wages. That is why changes to core pension benefits cannot be altered, unless replaced by something of comparable value. AB 340, as amended by AB 197, has not changed this form of vesting.

Most of the pension reforms involve the distinction between "new members" (new employees after Jan. 1 2013, or those who do not qualify for reciprocity) and all other employees. The new law does not draw any distinction between current members who are vested after five years and current members without five years. The main distinction is whether the person is a "new

member,” that is, one hired after Jan. 1, 2013 and does not meet any of the reciprocity or break in employment standards.

Q. When does the clock start on the 6-month break in service rule for determining if you are a “new member”? Is it Jan. 1, 2013, when the bill takes effect or could a break in service prior to Jan. 1, 2013 be applied?

A. The clock starts on the 6-month break in service rule upon a public employee’s separation from employment, regardless of whether the separation occurred before or after Jan. 1, 2013. For example, if an employee separates from a CalPERS-contracting agency on Dec. 1, 2012, and is not employed by another CalPERS-contracting agency on or before May 31, 2013, then the employee will be deemed to have had a break in service and will be considered a “new employee” under the new law.

Q. Are defined benefit plans mandated for all new members including part-time, seasonal and temporary employees?

A. No. Government Code Section 20305 continues to exclude part-time, seasonal and temporary employees from participating in CalPERS (unless an agency has amended its CalPERS contract to allow for the participation of part-time employees). Nothing in AB 340 requires agencies to adopt defined plans for part-time, seasonal and temporary employees.

2) Collective Bargaining and Memorandums of Understanding (MOUs)

Q. Must AB 340 and AB 197 changes be collectively bargained?

A. The level of pension benefits for current employees is a mandatory subject of bargaining because it is a form of future wages. To the extent an employer has discretion over the new pension benefits for new members and other requirements for current employees, the employer must negotiate over the area within its discretion. Because AB 340 establishes mandatory formulas and definitions for pensionable compensation, agencies and CalPERS have little or no discretion, and therefore there is no duty to bargain over the legislatively-mandated changes.

On the other hand, where actual agency discretion exists within the confines of a statute, such as the choice of a lower benefit formula for new safety members, then the duty to bargain arises. This is especially true for the provisions that impact current members, such as paying a portion or all of the employer’s contribution, 50 percent normal cost sharing, and the elimination of EPMC. (For a more extensive discussion about these matters, see Section III, “Duty to Bargain”.)

a) Employer and Employee Contributions

Q. How will cost sharing amendments in an existing CalPERS-agency contract apply to new members?

A. AB 340 requires new members to contribute at least 50 percent of the normal cost rate or the contribution rate for similarly situated employees, whichever is greater. However, if a memorandum of understanding (MOU) is in effect on Jan. 1, 2013, those provisions will apply

to current and new members until the memorandum expires. Any MOU continuation does not apply to AB 340's new benefit formulas. Existing cost sharing MOU provisions will apply to new members only if: (1) they are embodied in an MOU in effect on Jan. 1, 2013, and (2) they set a contribution rate different from 50 percent of the normal cost rate.

Q. In bargaining, can employers continue to propose continuing existing employee contributions above 50 percent of normal cost?

A. Yes. Independent of the changes brought by AB 340, employers may propose and negotiate above the standard of at least 50 percent of normal costs. However, until Jan. 1, 2018, employers cannot unilaterally impose changes on represented employees more than the normal costs provided by the statute. (Government Code Section 20516.5). If the employer has already negotiated cost-sharing agreements above 50 percent of the normal cost rate, those negotiated contributions will continue.

In addition, the new law allows employers to propose and negotiate the sharing of the "employer's contribution" subject to reaching an agreement. (See Government Code Sections 20516(a)-(e)). Further, the new law has not changed the employer's previous ability to propose and negotiate Employer Paid Member Contribution (EPMC); and to propose and negotiate an agreement inconsistent with Government Code Section 20516 provided it is incorporated into an MOU and is not part of the contract with CalPERS. (See Government Code Section 20516(f)).

Finally, the new law allows an employer to negotiate and implement cost sharing by individual bargaining unit as compared with the prior limitation that cost sharing could only be implemented within the traditional employee pre-collective bargaining groupings of miscellaneous, fire, and police.

Q. (i) If an agency has already required employees to pay their full member contributions and its MOU expires on Jun. 30, 2013, do new members hired in January pay the full member contribution rate (7-9 percent)?

A. Yes. Government Code Section 7522.30(f) provides that an existing agreement cannot be impaired in relation to cost share and EPMC provisions. Because the 50 percent normal cost sharing would interfere with the terms of the existing agreement to pay the full member contribution. New members would not be required to comply unless and until the MOU expires, is renewed, amended or extended.

(ii) On Jul. 1, 2013, do the new members automatically start paying the higher of the contribution limits set by AB 340 (8, 11, 12 percent) or 50 percent of normal cost?

A. Yes. The new members would be subject to 50 percent normal cost sharing. Note that the 8, 11, or 12 percent caps do not become effective until Jan. 1, 2018 (Government Code Section 20516.5(c).).

a) New Retirement Formulas and Optional Benefits

Q. Will the new safety tiers need to be negotiated?

A. Yes, but only if one of the parties wants to select a new tier other than the default established by law.

Under AB 340 there are three options for safety pension benefits: Basic Safety Plan, Option Plan One, and Option Plan Two. As a default, the new law provides that new employees receive pension benefits under the option that is closest to and provides a lower benefit at age 55 than the formula in effect on Dec. 31, 2012. However, a public employer and the employee representative may negotiate to provide a lower benefit. Any lower benefit must be mutually agreed upon and cannot be unilaterally imposed. Any lower benefit formula must be the same for both represented employees and unrepresented managerial/supervisory employees in the same membership classification (See Government Code Sections 7522.20 (e) and (f)).

Q. Before Jan. 1, 2013, does the new law prohibit negotiating and implementing a second tier that would apply to lateral transfers from other reciprocal agencies?

e.g. If an agency negotiates and implements a new tier for employees hired after Nov. 15, 2012 and after Jan. 1, 2013, the same agency hires an individual with acceptable reciprocity from another agency, does that newly hired person receive the new tier of benefits required by AB 340, or the tier that was negotiated by and in place Nov. 15, 2012?

A. No. AB 340 does not prohibit putting into place a new tier, provided the effective date of the new tier is before Jan. 1, 2013. If the appropriate reciprocity provisions cover a new hire, the new law requires that that the new hire gets the pension benefits for that classification that was in effect as of Dec. 31, 2012. (See Government Code Section 7422.02(c))

It is unclear at this time whether a CalPERS contract amendment to implement the second tier must be approved and implemented before Jan. 1, 2013 in order for any lower tier to become effective. That question may be answered by a future CalPERS regulation.

Q. After Jan. 1, 2013, does AB 340 prohibit an agency from negotiating and implementing a new tier only for lateral hires that are different from the new tiers required by the new law for all new members?

e.g. After Jan. 1, 2013, can an agency negotiate a provision that provides a new tier (3% at 55) for person who do not qualify as a “new employee” or “new member” under AB 340, but are lateral hires under reciprocity rules? Can that new tier of benefits for reciprocal lateral hires provide better benefits than a the new law’s safety formulas but less than the formula for current members (3% at 50)?

A. No clear answer.

The preferred view is that Government Code Section 7522.02(d) clearly states in part that “if the employer adopts a new defined benefit formula on or after Jan. 1, 2013, that formula must

conform to the requirements of this article or must be determined and certified by the retirement system's chief actuary and retirement board to have no greater risk and no greater cost to the employer than the defined benefit formula required by this article and must be approved by the Legislature." Establishing a new tier only for reciprocal lateral hires after Jan. 1, 2013 would have to meet the above test for employers. Adding a new tier (3% @ 55) for lateral hires would meet neither of the above tests (See Government Code Section 7522.02(d)) . Another view is that nothing prior to AB 340 and AB 179 prohibited agencies from negotiating new and lower tier for individuals hired after a specified future date. Also, AB 340 does not clearly prohibit this practice. The new law's prohibitions and mandates apply only to "new members as defined by Section 7522.04" (See Government Code Section 7522.02(b)). Thus the provisions in AB 340 that prohibits any agency from implementing a new tier other than the new law's tiers after Jan.1, 2013, applies to only to "new members." A reciprocal lateral hire is an exception, in effect, to AB 340's definition of "new member."

The League will be trying to work with the Administration, Department of Finance, and CalPERS to ensure that the integrity of the reforms remain intact. Freezing in place the enhanced benefits formulas adopted into law in the early 2000s after Jan. 1, 2013 is clearly counterintuitive to the AB 340 reforms.

Q. What happens to labor contracts? Will they be automatically set the new baseline formulas for new members after Jan. 1, 2013?

A. Labor contracts that have specific pension provisions in conflict with the mandatory provisions of AB 340 will be superseded by the new statutory requirements, with one limited exception. A memorandum of understanding (MOU) containing a specific provision on employee normal cost sharing and/or an Employer Paid Member Contribution (EPMC), will be permitted to continue to the MOU's expiration. All other MOU provisions that contain pension related terms in conflict with Public Employees' Pension Reform Act (PEPRA). For example, benefit formulas for new members – will be superseded. (See Government Code Section 7522.30(f)).

Q. What will agencies need to do with their labor groups? Will side letters to MOUs be needed?

A. Most labor practitioners believe this supersession will require the employer to work with the union on replacement language that is in harmony with AB 340. Some agencies, out of an abundance of caution, may offer the opportunity to negotiate any identifiable impacts of the supersession on mandatory subjects of bargaining. However, any such discussions between employers and unions cannot limit the implementation of the new law's provisions on Jan. 1, 2013.

The manner in which revisions to existing MOUs are memorialized (i.e. side letter, MOU amendment) is generally dependent upon the parties' bargaining practices. There is no legally required format.

Q. Do the new formulas take effect on Jan. 1, 2013, even if the MOU that is in effect contains different formulas for employees hired after that date?

A. Yes. The new benefit formulas are mandated for all new members after Jan. 1, 2013. The only exception is if an MOU provides for a benefit formula that has a normal cost that is less than the cost of the new formulas contained in AB 340.

An MOU continuing past Jan. 1, 2013, with formulas different from the new law's mandates will be superseded. The Legislature has chosen to mandate the new member formulas regardless of current MOU provisions (See Government Code Section 7522.02(b).).

Q. Do optional benefits that are already in place for existing employees under an employer's CalPERS contract apply to new members, and do CalPERS agencies have a duty to bargain optional benefits for new members?

A. Yes. Optional benefits that are already in place under the employer's CalPERS contract and contract amendments will apply to new members, except to the extent those optional benefits are prohibited by AB 340. For example, optional benefit formulas such as 3% at 50 and the 12-month final compensation period are not allowed for new members under AB 340.

Q. Will CalPERS recognize a ratified collective bargaining agreement that agrees to offer a lower tier of benefits prior to Dec. 31, 2012, even if my agency has not been able to complete the formal contract amendment process?

A. No. According to CalPERS, if a city would like to adopt a lower benefit formula prior to Jan. 1, 2013, the agency must complete the contract amendment process in accordance with all applicable requirements (which generally mean that the effective date is the date of final action of governing body) prior to Dec., 30, 2012. CalPERS will work with cities to expedite the contract amendment process to the extent possible, but CalPERS cannot retroactively implement contract amendments that are completed after Jan. 1, 2013.

3) Employer and Employee Contributions

a) Normal Cost Rate

Q. Does "normal cost rate" include mandatory member contribution rates set by statute?

A. Yes. New members must contribute 50 percent of the "normal cost rate," not 50 percent of the "normal cost." AB 340 defines the "normal cost rate" as the "annual actuarially determined normal cost for the defined benefit plan of an employer expressed as a percentage of payroll." In any fiscal year, the employer's contribution plus the employee contribution cannot be less than the "normal cost rate." Thus, the statutory employee contribution is part of the "normal cost rate." AB 340 defines "normal cost" consistently with CalPERS' current practice of excluding the statutorily mandated employee contribution from the annual valuation of normal cost, i.e. the total cost minus the statutory contribution. (See Government Code Sections 7522.30(a)-(e))

As an example, if the employer's "normal cost rate" for miscellaneous is 20percent of payroll, and miscellaneous employees currently pay the full 8 percent employee contribution, under AB 340, members who enter the system on or after Jan. 1, 2013 would pay 50 percent of the normal cost rate, or 10 percent total. In contrast, excluding the statutory member contribution from the "normal cost rate" would mean employees pay 8 percent plus half of the remaining 12 percent, for a total of 14 percent, which is not an appropriate application of 50 percent of normal costs as required by AB 340.

Q. How will my agency know what half of the normal cost will be for members? Will CalPERS publish the normal cost will be for agencies prior to Dec. 31, 2012?

A. According to CalPERS this information will be provided to contracting agencies as part of their Jun. 30, 2011 Annual Valuations that are scheduled to be completed and mailed out in November 2012. If a contracting agency would like to obtain a rough estimate of 50% of the total normal cost for each of its rate plans, the contracting agency may use the employer normal cost and employee contribution rate found in its Jun. 30, 2010 Annual Valuation. Keep in mind that the total normal cost will increase with the Jun. 30, 2011 Annual Valuation due to recent changes in actuarial assumptions.

Q. Will CalPERS calculate normal cost just based on the new formulas (e.g., 2% at 62)? Or will CalPERS calculate normal cost based on all formulas which the agency currently has? Will normal cost for members be calculated separately depending on the “tier that the new member belongs to?”

A. Yes. According to CalPERS, the normal cost will be calculated separately. Cities can expect to see the total normal cost calculation in their valuation reports, which are being sent to cities in November. CalPERS will be sending a letter that will outline which formulas and optional benefits will apply to new members that are hired into your agency after Jan. 1, 2013 and what the normal cost will be for new members. It is not clear when that letter will be sent, but it will be sent before Jan. 1, 2013.

b) Cost Sharing

Q. Does AB 340 allow the employer to impose a contribution of any part of the employer’s share?

A. No. Employer cost sharing of the “employer’s contribution” can only be required for represented employees by agreeing to specific terms of a collective bargaining agreement (See Government Code Sections 20516 (a) – e). For non-represented employees, the requirement to pay a portion of the “employer’s contribution” must be approved by a resolution passed by the agency.

Q. Can the member contributions received through cost sharing be applied to total normal costs, employer normal costs, or employer actual costs?

A. No. Government Code Section 20516(b) requires that member contributions over and above normal contributions be treated as normal contributions for all purposes.

Q. Must the member contributions received through cost sharing be first applied to total normal costs and then, only once it exceeds half of the total normal cost, can it be applied to unfunded liabilities?

A. Yes. Government Code Section 20516 permits collective bargaining agreements to share the cost of the employer contribution, but 20516(b) requires such member contributions to be treated as normal contributions for all purposes.

Q. Should the language “shall be the standard” be interpreted as a mandate or a goal?

A. The phrase “shall be the standard” appears in two different statutory sections: Government Code Section 7522.30(a) applying to new members, and Government Code Section 20516.5 applying to current employees. Both sections include the phrase “shall be the standard” in nearly identical sentences. However, the language following the “shall be the standard” sentence in each instance clearly modifies the meaning.

For new members, the language “shall be the standard” is clearly a mandate because Government Code Section 7522.30(c) requires that beginning Jan. 1, 2013, new members must pay 50 percent of normal costs, and an employer is prohibited from paying any portion of a member’s contribution. (See Government Code Sections 7522.30(a) and (c)).

For current members, by contrast, Government Code Sections 20516.5 (b) and (c) place two limitations on the “shall be the standard.” First, the employee’s share can be no more than a certain percentage of pay (8, 11 or 12 percent) if imposed by the employer after Jan. 1, 2018. Second, prior to Jan. 1, 2018, the 50 percent sharing is subject to reaching an agreement with represented employees. After Jan. 1, 2018 the employer can impose the standard up to the percentage caps (See GC 20516.5).

If the employer does not impose up to the allowable sharing level after Jan. 1, 2018, then the lower shared amount would remain in place. There is no automatic statutory implementation on or after that date. The employer must affirmatively act.

Q. What is a “related non-represented employee” in Government Code Section 20516(a)?

A. Government Code Section 20516, as amended by AB 340 and AB 197, provides that sharing the employer contribution costs shall also apply to “related non-represented employees” through a resolution approved by the contracting agency. Because most of this provision applies to reaching agreement through collective bargaining with represented employees, the new law specifies that this form of cost sharing also applies to “related non-represented employees.” A “related non-represented employee” is an unrepresented employee in the same CalPERS membership classification (e.g., miscellaneous, safety).

If the agency chooses to implement cost-sharing through negotiated agreements on an individual bargaining unit basis, as now allowed by Government Code Section 20516(c), then the “related non-represented employees” cost-sharing would be implemented through an agency resolution at the discretion of the agency. Under these circumstances, the new law does not specify whether the agency’s resolution may come before or follow the collective bargaining, nor does the law specify whether the amount of sharing of the employer’s contribution should be the same for represented and related unrepresented employees.

On the other hand, if the agency chooses to implement this form of cost sharing on the basis of the traditional groupings (miscellaneous, safety), then the employer must implement the cost sharing for all the members of the group, and would be required to adopt a resolution for the “related non-represented employees” that adopts the same cost-sharing for both represented and non-represented employees in the same pension member classification.

c) Contribution Limits

Q. Does AB 340 require that current members pay 50 percent of the normal cost of pensions after Jan. 1, 2013?

A. No. Unlike the provisions for new members, AB 340 does not require current members to pay 50 percent of the normal cost of pensions. However, the law states that “[i]t shall be the standard that employees pay at least 50 percent of normal costs and that employers not pay any of the required employee contributions.” Nothing in the law prohibits an employer, however, from negotiating to this standard provided voluntary agreement is reached with the represented employees.

An employer cannot unilaterally implement the standard until Jan. 1, 2018. At that point, the employer may require represented employees to pay at least 50 percent of normal cost, but no greater than 8 percent of pay for non-safety members, 12 percent of pay for police and fire members, and 11 percent of pay for all other local safety members. Prior to any imposition, the employer must engage in good faith bargaining and the exhaustion of mandatory impasse procedures. Of course, unrepresented employees may be required to pay these amounts without bargaining (See Government Code Section 20516.5).

Q. If, as of Jan. 1, 2018, the employee contribution is 50 percent of normal cost but above the contribution limits in AB 340, will the employee contribution automatically drop to the contributions limits set in the new law?

A. No. The maximum percentages only apply after Jan. 1, 2018 to contribution rates imposed by the employer following exhaustion of the collective bargaining process. The maximum percentages do not apply to contribution rates set by a collective bargaining agreement, so there will be no change to mutually agreed contribution rates on Jan. 1, 2018. However, once that agreement expires, the new law appears to limit the employee contribution to the maximum percentage unless the union and employer agree to a higher contribution.

Q. Does cost sharing of Government Code Section 20516.6 apply equally to all employees after 2018? (e.g., all employees, no matter whether “new member” or not, pay higher of 50 percent of normal cost or the limits of 8, 11, 12 percent)

A. No. After January 2018, new members must continue to pay at least 50 percent of normal costs or the amount of normal cost paid by similarly situated employees, whichever amount is greater. In contrast, current employees must pay (1) the portion of normal cost increase that the employer has been able to negotiate, or (2) the portion of normal cost the employer has imposed, but only up to a maximum of 50 percent of the member contribution limit.

There is no requirement for current employees to pay 50 percent of normal cost prior to 2018; and after that date, the new law does not require the employer to impose that requirement up to the limits, it only allows the agency to take action. (Compare Government Code Section 7522.30 with Government Code Section 20516.5)

d) Employer Paid Member Contributions (EPMC)

Q. With the enactment of AB 340 as amended by AB 197, will employers still negotiate to eliminate EPMC?

A. No, for new members

Yes, for current membersⁱ *(see endnotes for further explanation)*

e) Employer Contribution Rates

Q. Is CalPERS planning on issuing two separate employer rates for each plan (i.e. miscellaneous, fire and police) by both 1) new member rate in the new tier and 2) current employee rate in the current plan design? If yes, could we expect that to occur effective Jan. 1, 2013 or would agencies have to wait for another actuarial cycle, which based on the past lag time, would not see a second rate tier structure until FY 2015?

A. According to CalPERS, if your agency is in a pool CalPERS will issue separate contribution rates for the new retirement formulas. Additionally, like CalPERS' previous practice, if your agency is not in a pool they will issue one contribution rate, which will be expressed as a percentage of payroll. Cities can expect to see their employer rate in their next valuation reports, which are being sent to cities in November. CalPERS will be sending a letter that will outline which formulas and optional benefits will apply to new members that are hired into your agency after Jan. 1, 2013 and what the normal cost will be for new members. It is not clear when that letter will be sent.

4) New Retirement Formulas

a) Current Members and Lateral Hires

Q. Which formula applies to current members if they leave employment with one member agency for employment with another member agency? Or, get rehired by the same agency?

Example 1: On Feb. 1, 2013, a current CalPERS member leaves his current CalPERS employer for a job with another CalPERS employer.

A. In this scenario, the person changing jobs is leaving a CalPERS employer for a new job with another CalPERS employer and does not have a six month break in service. Therefore, the member will go to the retirement formula in place as of Dec. 31, 2012 with the new CalPERS employer.

For example, an employee leaves an Accounting Assistant job at City X for an Accounting Technician job with City Y. Both City X and City Y are CalPERS agencies. The employee has a one week break in service between the two jobs. The employee will go to the retirement formula tied to the City Y Accounting Technician position as of Dec. 31, 2012.

Note – it may be possible for a CalPERS employer to negotiate a retirement formula for future new hires that are current members that is different (lower) than the formula in place on Dec. 31, 2012.ⁱⁱ

Example 2: On Feb. 1, 2013, a current '37 Act agency member leaves their current agency for a job with a CalPERS employer.

A. In this scenario, the person changing jobs is leaving a '37 Act employer for a new job with a CalPERS employer and does not have a six month break in service. If the '37 Act employment was with an agency with reciprocal retirement benefits as required by CalPERS and the current member does not have more than a six month break in service, the employee will be considered a new member and will go to the formula in place for the position held with the new CalPERS employer as of Dec. 31, 2012.

For example, an employee leaves a Deputy Sheriff job at 1937 Act County X for a Police Officer job with CalPERS City Y. The 1937 Act County has reciprocity with CalPERS. The employee has a one week break in service between the two jobs. The employee will go to the retirement formula tied to the CalPERS City Y Police Officer position as of Dec. 31, 2012.

Note – it may be possible for a CalPERS employer to negotiate a retirement formula for future new hires that qualify to be considered a current member (as a result of reciprocity) that is different (lower) than the formula in place on Dec. 31, 2012.ⁱⁱⁱ

For a list of public retirement systems with reciprocity, see End Note III.^{iv}

Example 3: On Feb. 1, 2013, an employee separates from employment with a CalPERS agency. On Nov. 1, 2013, this same employee is rehired by their former CalPERS agency. The employee did not work for any public employer from Feb. 1-Nov. 1, 2013 nor did the employee retiree during this time period. What formula does the CalPERS agency apply to this rehired employee?

A. In this scenario, the employee returns to the formula they had at the time they left employment. Even though the employee had more than a six month break in service, because they are returning to their former CalPERS agency employer, the employee retains the formula they had on the day of separation.

Q. If an agency has a 3% at 50 formula for sworn police then agreed to the 3% at 55 formula and amended their CalPERS contract prior to Dec. 31, 2012, do lateral hires definitively get hired into the 3% at 55 tier, or could they claim a right to the 3% at 50 formula?

A. If the employment at both agencies is reciprocal and a lateral Police Officer is hired after January 1, 2013, they will go to the retirement formula in place with the new agency as of Dec. 31, 2012. If 3% at 55 was the 2nd tier formula in place on or before Dec. 31, 2012 for new hires, then the lateral officer will go to that formula when hired on or after the effective date of the contract amendment provided that the employee did not have more than a six month break in service.

NOTE: Results may be altered in cases in which current employees are returning after leaves of absence or layoffs; consult with legal counsel.

b) Adopting Different Retirement Formulas than New Law

Q. Can my agency adopt a different benefit formula level than what is in AB 340 for new members?

A. Yes, but under very limited circumstances.

If an agency has a benefit formula in effect before Jan. 1, 2013, that has a lower normal cost than what is required under AB 340's new benefit formulas, that plan may remain in force for new members. Otherwise, the basic rule applies: after Jan. 1, 2013, the new law's pension formulas apply to new members.

Also, if an employer adopts a new defined benefit formula on or after Jan. 1, 2013, that formula must be the same formula offered under AB 340 or must be determined and certified by the retirement system's chief actuary and the retirement board to have no greater risk and no greater cost to the employer than the defined benefit formula provided under the new law. The Legislature must also approve any benefit that is different than what is in AB 340. (See Government Code Sections 7522.02(d) and (e) .

5) Pensionable Compensation

a) Compensation Cap

Q. Who is covered by pensionable compensation caps?

A. Pensionable compensation caps apply to defined benefit plans for new members. Generally new members are employees hired after Jan. 1, 2013 who do not have reciprocity with their prior plans.

- For those covered by Social Security, the cap is 100 percent of the SS contribution and benefit base as of Jan. 1, 2013 (\$110,100 for 2012).
- For those not covered by Social Security, the cap is 120 percent of the SS base as of Jan. 1, 2013 (\$132,120 for 2012).
- The cap will be adjusted annually based on changes to the Consumer Price Index for All Urban Consumers and not based on Social Security limits.
- Current members are not subject to the cap.

Q. Are there provisions for changes to the pensionable compensation cap should Social Security implement changes which would dramatically impact the cap?

A. AB 340 does not address this point. Government Code Section 7522.10 (d) (2) allows the Legislature to modify the cap. Should the Federal government make a major change to Social Security, it seems likely that additional legislation would be proposed.

Q. What is the interplay between the limitations in AB 340 and the Internal Revenue Code regarding pensionable compensation used to calculate the defined benefit or defined contribution plan for new members?

A. The Internal Revenue Service (IRS) limit is substantially higher than the new pensionable compensation limit, so for new members as a practical matter it can be ignored for the defined benefit plan (the limit could apply to supplemental defined contribution plans). For current members, the new pensionable compensation limit does not apply but the IRS limit now applies to every retirement system that is tax qualified. In general, the IRS limit is \$250,000 for 2012, though for members who are grandfathered under federal tax law it can be higher.

b) Current Members

Q. How does AB 340 affect existing contracts with top managers where an employer makes contributions to the employee's deferred (457) compensation plan?

A. Generally, AB 340 does not affect existing contracts for current top management employees, although this depends on the exact terms of the contract. However, the contract must comply with current California law (i.e., CalPERS or '37 Act) and IRS requirements.

c) Leave Time

Q. Does AB 340 change the rules for pensionable compensation for payment of leave time?

A. **No.** Existing law already provides that payments for unused sick leave, vacation, annual leave, personal leave, or other compensatory time off, whether paid in a lump sum or otherwise and regardless of when reported or paid may not be considered as "pensionable compensation" for new members nor may it be considered "compensation earnable" for any CalPERS members.

d) Significant Increases in Compensation

Q. How is a significant increase in compensation defined?

A. After Jan. 1, 2013 the CalPERS Board is required to define significant increases in compensation based on a CalPERS agency's actuarial liability due to increased compensation for non-represented employees.

This provision is designed to establish a process to ensure that employers who increase compensation for an employee do not cause a significant increase in actuarial liability for a previous employer who would be forced to pay greater pension benefits under reciprocity rules. If there is a significant increase in liability, that increase will be assessed to the CalPERS agency that created it.

e) Overtime Compensation

Q. Is the "standard overtime" for a group or class of employees still pensionable compensation in the same manner and fashion as it was for CalPERS employees prior to AB 340, or is it now only allowed for peace officers and firefighters who have a "7(k) work schedule" and have "standard overtime" that is part of their normal full-time base?

A. Yes, it appears that overtime may only be “pensionable compensation” for a new member if it is “standard overtime” for the new member’s group or class of employees *and* the new member is a fire fighter or peace officer working under a 7(k) work schedule. Differentiated pay schedules (overtime) seem to be authorized as long as the schedules are for a normal work week, on a pay schedule and cover a group or class of employees. However, this question is subject to interpretation by CalPERS we must wait and see if CalPERS amends this regulation. ^v

6) Supplemental Retirement Benefits

Q. Can an agency provide a supplemental defined benefit plan to new members subject to the pensionable compensation caps?

A. No. Supplemental defined benefit plans existing prior to Jan.1, 2013 can continue; however, the plan cannot be offered to new groups excluded from the plan before Jan. 1, 2013. Also, new employees cannot be added to prior supplemental defined benefit plans.

Further, if an employer adopts a new defined benefit plan or benefit formula after Jan. 1, 2013 the plan or formula must conform to AB 340 or must be determined and certified by the retirement system's chief actuary and the retirement board to have no greater risk or cost to the employer than the plan offered under AB 340 and must be approved by the Legislature.

Q. What are the limits on establishing a new defined contribution plan?

A. There are no limits contained in AB 340 on establishing new defined contribution plans with contributions on compensation up to the cap. There also are no limits contained in AB 340 on establishing new defined contribution plans for current members with contributions on compensation above the cap. However, in each case the plan must comply with current California law (i.e., CalPERS or '37 Act) and IRS requirements.

For employees hired after Jan. 1, 2013 the public employer can provide a defined contribution plan with employee contributions based on compensation in excess of the pensionable compensation cap. The plan must comply with current California law and IRS requirements and:

- The employee may not have a vested right to continuing employer contributions.
- Contributions shall not, when combined with the employer’s contribution to the employee’s retirement benefits below the compensation limit, exceed the employer’s contribution level, as a percentage of pay, required to fund the retirement benefits of employees with incomes below the compensation limits.

Example:

The City Council would like to maximize the contribution to a new top manager’s defined contribution plan. The manager does not have reciprocity and is considered a new member under AB 340. The top manager will earn \$200,000/year. All miscellaneous city employees pay 8 percent toward their defined benefit plan and the City pays 16 percent of the employer’s contribution. There is no Social Security benefit.

$\$200,000 - \$132,120 = \$67,880$
 $\$67,880 \times 16\% = \$10,861$
\$10,861 is the maximum yearly contribution to the top manager's defined contribution plan.

7) Working after Retirement, Retirees

Q. Do the current post-retirement work restrictions and exceptions set forth in the Public Employees Retirement Law (PERL), such as Government Code Section 21221 and 21224, still remain in effect in their entirety after AB 340 goes into effect on Jan. 1, 2013?

A. Yes. Generally speaking, the PERL's specific post-retirement employment limitations and exceptions to those limitations will still apply after AB 340 goes into effect on Jan. 1, 2013.^{vi}

Q. Under AB 340, does the requirement of a 180-day waiting period between retirement and post-retirement employment apply to a member who retires after Jan. 1, 2013, before Jan. 1, 2013 or both?

A. The statute is not clear and CalPERS has not definitively addressed this yet — it may apply to both.

Under the new law (Government Code Section 7522.56), the 180-day waiting period becomes effective on Jan. 1, 2013. The 180-day waiting period is measured from the date of retirement to the date of the compensated service with an employer in the same retirement system from which the retired person receives a pension. It does not matter if the date of retirement occurred prior to Jan. 1, 2013.

For example, if a member retires from CalPERS agency on Aug. 1, 2012 and begins post-retirement employment on Nov. 1, 2012, then as of Jan. 1, 2013, the member must complete a 180-day waiting period, unless one of the exceptions in the new law applies to the retiree. In this example, the retired person would have to stop working for a period of at least 180 days from the date of retirement and would not be eligible to return to post-retirement employment until April 30, 2013.

8) Service Credit and Airtime

Q. Can sick leave still be converted to service credit?

A. Yes, AB 340 did not change the rules regarding sick leave conversion to service credit. For both new (after Jan. 1, 2013) and existing members, sick leave may still be converted to CalPERS service credit if that benefit is part of the employer's contract with CalPERS or if the employer is part of a risk pool.

9) Equal Health Benefit Vesting Schedule

Q. Does the new law apply to health benefits provided to active employees, to health benefits provided only to retirees, or both?

A. AB 340 (Government Code Section 7522.40) states that a public employer shall not provide “to a public employee who is elected or appointed, a trustee, excluded from collective bargaining, exempt from civil service, or a manager of any health benefit vesting schedule that is more advantageous than that provided generally to other public employees, including represented employees, of the same public employer who are in related *retirement* membership classifications.

Although it says “health benefit vesting” rather than “retiree health benefit vesting,” because this statute falls under the Article known as the California Public Employees’ Pension Reform Act, this statute most likely only applies to health benefits provided to employees during retirement, rather than during active employment.

Q. Does the new law limit the level of health benefits that may be provided in retirement or just the length of time an employee must work in order to vest?

A. The latter. The phrase “health benefit vesting schedule” is understood to only refer to the schedule used by the employer to determine whether and to what extent an employee receives retiree health benefits. For example, the length of time an employee must work for the employer in order to be eligible for a specified retiree health benefit would be a vesting schedule.

Assume, for example, the employer requires that general employees work a minimum of 10 years for the employer in order to be eligible to participate in the employer’s retiree health plan with an employer contribution of 50 percent of the premium for employee-only and 20 years for an employer contribution of 100 percent of the premium for retiree-only is a “vesting schedule.” Thus, under the new law (Government Code Section 7522.40), we believe an employer would not be permitted to offer to management employees who are in related retirement membership classifications a preferential vesting schedule.

Q. Under AB 340, does the equal health vesting apply to any retiree health care benefit including CalPERS Medical?

A. Yes. AB 340 (Government Code Section 7522.40) applies to any “public employer” as defined by the new law and any “health benefit vesting schedule” the public employer maintains for retiree health benefits, including the Public Employees’ Medical and Hospital Care Act (“PEMHCA” or “CalPERS Medical”).^{vii}

10) Industrial Disability Retirement for Public Safety

Q. What happens after the end of the “trial” period for the changed to the safety Industrial Disability Retirement (IDR)?

A. At this time, the answer to this question is unknown.