New Law Affects Public Employee Pension Benefits

On September 12, 2012, Governor Jerry Brown signed into law Assembly Bill (AB) 340, a bill which enacts the much anticipated California Public Employees' Pension Reform Act of 2013 (PEPRA). The intent of the bill is to save the State tens of billions of dollars over the next 30 years by capping retirement benefits, increasing retirement age, and implementing other measures meant to stop retirement benefit abuse.

PEPRA is of special interest to educational entities, because it makes statutory changes that will have an effect on new members of the California State Teachers' Retirement System (CalSTRS) and the California Public Employees Retirement System (CalPERS) hired on or after January 1, 2013. PEPRA will also have effects on current members of both CalSTRS and CalPERS systems.

It should be noted that PEPRA includes charter schools in the definition of "public employer." As such, charter schools that participate in a public retirement system are subject to PEPRA.

PEPRA has effects on other public agencies, as well. Therefore, non-educational agencies should consult with legal counsel regarding the effects the new laws have on them.

The key provisions of PEPRA related to retirement benefits for school employees include, but are not limited to, the following:

Provision	Summary
New Retirement Formulas (Government Code sections 7522.02(b), 7522.04(f), 7522.20, 7522.25) (Education Code sections 24202.6(a), 24202.7)	PEPRA establishes new retirement formulas for public employees who are "new members" of a public retirement system. "New member" is defined as an individual who becomes a member of any public retirement system for the first time on or after January 1, 2013, and who was not a member of any other public retirement system prior to that date. Additionally, "new member" is defined to include an individual who becomes a member of a public retirement system for the first time on or after January 1, 2013, and who was a member of another public retirement system prior to that date, but who was not subject to "reciprocity" as defined in the law. The value of these new formulas cannot be exceeded by an employer offering a defined benefit pension plan. With regard to new CalSTRS members, PEPRA sets a defined benefit formula of 2% at age 62, with an early retirement age of 55, and a maximum benefit factor of 2.4% at age 65. With regard to new, non-safety CalPERS members, PEPRA sets a defined benefit formula of 2% at age 62, with an early retirement age of 52, and a

	maximum benefit factor of 2.5% at age 67. PEPRA specifies three different formulas that will apply to safety employees hired on or after January 1, 2013. Which formula applies will depend upon the formula currently in place for the same class of employees.
Hard Cap on Compensation Used When Calculating Retirement Benefit (Government Code sections 7522.10(c)-(d), 7522.32(a))	PEPRA caps the annual salary that counts toward final compensation for all new members of any public retirement system at $110,100 (the 2012 Social Security Contribution and Benefit Base) or 120% of that limit ($132,120) for employees who do not participate in Social Security. This amount will be adjusted annually. For new members of a public retirement system, "final compensation" means the employee's highest average annual "pensionable compensation" earned during a period of at least 36 consecutive months, or at least three school years, as specified.
Definition of "Pensionable Compensation" (Government Code section 7522.34(a), (c))	"Pensionable compensation" for new members of any public retirement system means "the normal monthly rate of pay or base pay of the member paid in cash to similarly situated members of the same group or class of employment for services rendered on a full-time basis during normal working hours, pursuant to publicly available pay schedules." "Pensionable compensation" does not include, for example, any compensation paid to increase an employee's retirement benefit, compensation that has already been received in kind by the employee as a cash benefit, any one time or ad hoc payments made to an employee, any severance or separation payments, or payments for unused vacation, annual leave, personal leave, sick leave, or compensatory time off. However, accumulated and unused leave for absence for illness or injury for which full salary is allowed may still be counted toward service credit at retirement pursuant to Education Code section 22717.
Equal Contributions (Government Code section 7522.30)	New members of any public retirement system are required to contribute at least 50% of the annual actuarially determined normal costs. Districts may negotiate with current classified employees for agreements that require current classified employees to pay 50% of normal costs. However, districts cannot impose 50% cost sharing on current classified employees until after January 1, 2018. Notwithstanding the above, PEPRA authorizes classified employee contributions to be more than 50% of the normal costs if agreed to through collective bargaining. Thus, an employer and collective bargaining unit may negotiate for employees to share the cost of the employer's contribution and to pay for more than 50%. The collective bargaining agreement must specify the exact percentage of employee compensation that shall be contributed to the employer's contribution costs. However, PEPRA prohibits employers from using impasse

	procedures to increase an employee rate to greater than 50%. Moreover, PEPRA prohibits employers from contributing at a greater rate to the plan for non-represented, managerial, or supervisory employees than employers contribute for other public employees who are in related retirement classifications.
Prohibition of Supplemental Benefits (Government Code section 7522.18)	PEPRA prohibits an employer from offering a supplemental defined benefit plan unless it was offered on or before January 1, 2013. Supplemental plans that were offered before January 1, 2013, cannot be offered to any new groups or classes of employees. Among other effects, this restriction will limit the options available to districts when considering an early retirement incentive because supplemental defined benefit plans will no longer be available for this purpose.
Eliminates "Air Time" (Government Code section 7522.46)	PEPRA prohibits a public employee from, on or after January 1, 2013, purchasing nonqualified service credit, or "air time." Previously, CalPERS and CalSTRS allowed members to purchase up to five years of service credit. Applications to purchase airtime that are received before January 1, 2013, can still be approved.
Prohibits Retroactive Retirement Formula or Benefit Enhancements (Government Code sections 7522.44(a)-(b))	PEPRA prohibits public employers from granting current employees and employees hired on or after January 1, 2013, retirement formula or benefit enhancements retroactively. If a change to an employees' classification or employment results in an increase in the retirement formula or employee benefit formula, the increase would apply only to service performed on or after the operative date of the change.
Breaks in Service/Post Retirement Earnings (Government Code section 7522.56)	PEPRA specifies that an individual who was an active member in a public retirement system and who, after a break in service of more than six months, returned to active membership in that system with a new employer is considered a "new member" of the public retirement system for purposes of PEPRA. However, a change in employment between state entities or from one school employer to another shall not be considered as service with a new employer. PEPRA limits all non-safety employees who retire from public service to working no more than 960 hours per year for a public employer. Additionally, a 180-day waiting period is required before an employee's return to work. However, PEPRA provides an exception to the 180-day waiting period for employees who retire at normal retirement age and did not receive an early retirement incentive, if the governing body of a local agency takes action by way of adopting a resolution at a public meeting to certify that the retiree is needed to fill a critical position and the employee's departure did not create the need for employment.
Felons Forfeit Benefits (Government Code	PEPRA requires pension and related benefit forfeiture of any public employee (both current and new) including those employees elected or appointed to a public office, who is convicted of a felony in carrying out official duties, in seeking an elected office or appointment, or in

section 7522.72)	connection with obtaining salary or pension benefits. PEPRA also specifically requires pension and related benefit forfeiture of any public employee who has contact with children as part of the employee's official duties who has been convicted of a felony that was committed against a child who the employee has contact with as part of his or her official duties.

As outlined above, the enactment of PEPRA brings a great deal of change to California pension laws, especially to new employees, hired on or after January 1, 2013, who have never been a member of a California public pension system. If you have any questions regarding the above or how this new law affects current employees, future employees, or the collective bargaining process, please feel free to contact one of our eight offices located statewide. You can also visit our website or follow Lozano Smith on Facebook.

Written by:

Karen Rezendes
Shareholder
Walnut Creek Office
krezendes@lozanosmith.com

Marisa R. Lincoln
Senior Counsel
Walnut Creek Office
mlincoln@lozanosmith.com