



Agenda Item 6c

February 20, 2013

ITEM NAME: State Legislative Proposal: Conformity with the Public Employees' Pension Reform Act of 2013 (PEPRA)

PROGRAM: Legislation

ITEM TYPE: Action

RECOMMENDATION

Sponsor legislation to add and amend certain sections of the Government Code administered by the Board of Administration (Board) of the California Public Employees' Retirement System (CalPERS) to clarify ambiguities and to better conform these provisions to the newly enacted pension reform statutes.

EXECUTIVE SUMMARY

This proposed legislation would make several changes to the Public Employees' Retirement Law (PERL), Public Employees' Medical and Hospital Care Act (PEMHCA), Legislators Retirement Law (LRL) and the Judges' Retirement Law (JRL I & JRL II) in order to facilitate the implementation of newly-enacted pension reform legislation. The proposed changes are technical in nature and will better align CalPERS processes and statutes to the new pension reform laws, and to the pension reform clean-up legislation presently being considered by the Legislature. The proposed changes are not intended to alter the intent or the provisions of the PEPRA and related pension reform statutes. Without these changes, CalPERS pension reform implementation efforts may become delayed or subject to unnecessary challenge.

STRATEGIC PLAN

This proposal is consistent with Strategic Goal A to improve long-term pension and health benefit sustainability.

BACKGROUND

On September 12, 2012, Governor Brown signed into law Assembly Bill (AB) 340 and AB 197, which included the PEPRA and related pension reform changes to the PERL, the JRL I and II, and the LRL to make many changes to the retirement benefits available to existing and future public employees. These statutory provisions became effective on January 1, 2013.

For public employees newly hired on or after January 1, 2013, and for certain employees returning to public service on or after that date, the pension reforms generally provide reduced defined benefit pension formulas with increased normal retirement ages, establish a new definition of pensionable compensation (the types

of pay that can be used to calculate retirement benefits), impose a three-year final compensation period, establish a cap on the pensionable compensation that can be used to calculate pension benefits, and require equal sharing of the normal cost of pension benefits. For existing and future employees, the pension reforms prohibit retroactive benefit increases, impose benefit forfeiture for employees convicted of job-related felonies, prohibit Additional Retirement Service Credit purchases, and require strict adherence to federal contribution and benefit limits established by the Internal Revenue Code for public pensions. In addition, AB 340 closes the Legislators' Retirement System to new members, requires equal retiree health benefit vesting periods for non-represented and represented employees, prohibits employer pension contribution holidays, and imposes limitations on public employment after retirement. AB 340 also exempts charter cities and charter counties that operate their own public retirement systems and the University of California from pension reform.

With most complex legislation, follow-up legislation is necessary to correct drafting oversights and facilitate the orderly implementation of the new statutory provisions. The PEPRA and related pension reform laws are no different, and CalPERS staff has identified several areas in existing sections of the PERL, PEMHCA, LRL, and JRL I & II that would benefit from clarification and greater conformity with the new laws. The proposed legislation contemplated here is intended to address some of those issues. The Legislature is already considering Senate Bill (SB)13 (Negrete McLeod), which makes several changes to the PEPRA and the PERL provisions to correct drafting errors and clarify key provisions. SB 13 is an urgency bill and is intended to address the most critical clean-up issues.

In addition to these statutory changes, CalPERS staff is also developing regulations to clarify areas of the new laws, and to identify new processes necessary to implement the pension reform changes.

ANALYSIS

As noted above, the PEPRA reduces and caps pension benefits for most new public employees, requiring the establishment of new procedures for administering the enrollment and benefits of new members. The PEPRA and related pension reform changes also affect member enrollment, benefit calculations, actuarial valuations, employee and employer contribution rate calculations, validation of member information, and participating agency contract management procedures.

Since the public release and enactment of the PEPRA and related pension reform legislation, CalPERS staff has been reviewing, and continues to review, the new laws in order to identify the tasks that will need to be undertaken to implement pension reform. This review process is ongoing, and may reveal the need for additional changes. CalPERS staff has already identified the need for several statutory changes that would aid in pension reform implementation. These changes do not alter the underlying intent of the PEPRA and related pension reform laws, and

are intended to assist CalPERS in fully implementing the new retirement benefit framework required as a result of pension reform.

The proposed changes to sections of the Government Code administered by the Board would likely address several issues, including, but not limited to the following issues:

- Clarify that the Board will administer each System in conformance with the applicable provisions of the PEPRA as if they were contained within the PERL, PEMHCA, JRL I & II, and the LRL. To the extent the Board identifies a conflict between the PEPRA and one of the other existing statutory schemes administered by the Board, the PEPRA would control.
- Amend applicable PERL provisions to recognize the new State Second Tier benefit formula applicable to new members pursuant to the PEPRA.
- Amend applicable PERL provisions to recognize the new PEPRA requirements regarding the prohibition against employer paid member contributions for new members.
- Incorporate the new health benefit vesting equity requirement mandated by the PEPRA into the PEMCHA.
- Clarify in a PERL provision how CalPERS will administer retirement benefits for members with service credit accrued under both PEPRA and non-PEPRA retirement formulas.
- Amend the applicable PERL provisions to conform to the new post-retirement employment restrictions as required by the PEPRA.
- Amend the applicable PERL provisions to incorporate the prohibition against retroactive benefit enhancements as required by the PEPRA.
- Make technical, non-substantive changes throughout the PERL to recognize the new pension reform requirements and to eliminate potential conflicts between the existing PERL provisions and the PEPRA provisions.
- Clarify definitions in the PERL, LRL, and the JRL I & II to reflect the changes necessitated by the new pension reform provisions.

These proposed changes are necessary to ensure that implementation of the PEPRA and related pension reform changes continue without unnecessary delays and costs. These clarifying changes should also help avoid confusion for members, employers, other stakeholders, and CalPERS staff, and aid in the consistent application of the new pension reform provisions.

BENEFITS/RISKS

Benefits

- Assists CalPERS continuing implementation of the PEPRA and related pension reform statutes.

- Clarifies provisions in the PERL, PEMHCA, LRL, and JRL I & II that might otherwise require the Board to develop and adopt additional regulations and procedures necessary for CalPERS to implement pension reform.
- Provide clear direction for members, employers, other stakeholders, and CalPERS staff to ensure the consistent application and the efficient implementation of the pension reform changes.
- Minimize the costs associated with possible legal challenges brought to clarify conflicts between the pension reform statutes and existing retirement law.

Risks

- Failure to clarify provisions of the PEPRRA affecting CalPERS and its members and employers may subject implementation to unnecessary delay.
- Failure to improve conformity between the PEPRRA and the PERL, LRL, and the JRL I & II may limit CalPERS ability to fully implement the new laws, and subject the System to unnecessary legal challenges and to the costs associated with defending such challenges.

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