CalPERS

March 14, 2017

Item Name: Proposed Regulation for Pensionable Compensation under PEPRA

Program: Employer Account Management Division

Item Type: Action

Recommendation
Approve staff's recommendation to pursue the proposed regulation defining pensionable compensation.

Executive Summary
The adoption of the attached regulation would assist with the implementation and administration of the pension reform statutes enacted by Assembly Bill (AB) 340 (Stats. 2012, Ch. 296), which includes the Public Employees' Pension Reform Act (PEPRA) of 2013. It is intended to clarify the California Public Employees' Retirement System (CalPERS') interpretation of what is considered pensionable compensation for "new members" hired on, or after, January 1, 2013, and promote uniform compliance amongst all covered employers.

Strategic Plan
This agenda item supports Goal A, Improve long-term pension and health benefit sustainability by clarifying and communicating CalPERS' interpretation of certain pension reform provisions.

Background
On September 12, 2012, Governor Brown signed AB 340 into law, generally defining pensionable compensation and imposing specific caps and limits on compensation used in the defined benefit calculations for "new members" hired on, or after, January 1, 2013. PEPRA also excludes specified payments from being considered as pensionable compensation. PEPRA did not change reportable compensation or impose any caps or limits on "classic" members hired before January 1, 2013.

On October 4, 2013, Governor Brown signed Senate Bill (SB) 13 (PEPRA clean-up legislation) into law. While SB 13 included technical corrections, it did not make specific changes to the definition of pensionable compensation. However, it did include a provision that would allow a pay item to be excluded from pensionable compensation if agreed upon through collective bargaining with represented state employees or imposed on non-represented state employees.

In April 2014, CalPERS introduced draft regulations for reportable compensation under PEPRA, which the CalPERS Board of Administration (Board) approved and released for public comment. Following the end of the public comment period, the Board held a public hearing to allow stakeholders and other members of the public to provide feedback on the regulations, and in August 2014, the Board approved the draft regulation package to move forward for adoption by the Office of Administrative Law. Governor Brown's administration, however, opposed including temporary upgrade pay in the regulation. As a result, the regulation was never adopted.

Analysis

This proposed regulation is a follow-up to the 2014 effort to implement and administer the pension reform statutes enacted by AB 340, and clarify CalPERS' interpretation of what is considered pensionable compensation for "new members" hired on, or after, January 1, 2013. For "new members," pensionable compensation must meet the following four criteria:

- Pay is part of the normal monthly rate of pay.
- Pay is paid in cash to similarly situated members of the same group or class of employment.
- Pay is for services rendered during normal working hours.
- Pay is paid pursuant to publicly available pay schedules.

PEPRA also expressly states what cannot be included in pensionable compensation for new members. For example, pensionable compensation does not include bonuses, uniform allowance, overtime, reimbursement for housing and vehicles, or one-time or ad-hoc payments. At the completion of the regulation process, approval of this regulation will:

- Ensure compliance with applicable laws governing pensionable compensation
- Describe with precision what is and is not pensionable compensation
- Promote transparency by informing all stakeholders of the types of compensation that can be used to calculate retirement allowances for new members
- Enable the organization to provide an effective platform to clearly communicate the definition of pensionable compensation.

Budget and Fiscal Impacts

<u>Administrative Costs</u>

CalPERS will incur some costs in order to comply with the PEPRA legislation. In general, certain administrative costs will be attributable to the regulation, including education outreach and training, publication costs, and postage. In some instances, CalPERS-covered employers may also incur certain administrative costs for training and costs associated with complying with the regulation; however, staff may be unable to quantify all of the costs incurred by CalPERS-covered employers.

<u>Benefit Costs</u>

CalPERS staff analyzed reporting data for the three fiscal years following PEPRA's enactment (FY 2013-14 through FY 2015-16), and estimates that pensionable compensation reporting in FY 2017-18 may result in an employer normal cost of approximately $16 million for public agencies, schools, and the State. This normal cost is not a new cost, as employers are required to pay contributions on all compensation reported to CalPERS and the pensionable compensation items that are included in the regulation package have historically been reported. In addition, for comparative purposes, the total normal cost for all employers in FY 2016-17 is $5.3 billion.

Benefits and Risks
Without adoption of a regulation, CalPERS members and covered employers may challenge CalPERS' interpretation of pensionable compensation. By adopting the regulation, CalPERS may achieve cost savings as a result of decreased litigation and administrative appeals related to the definition of pensionable compensation as members and covered employers understand what compensation is or is not reportable to CalPERS.

Attachments
Attachment 1 – Proposed Regulation

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