CalPERS

Finance and Administration Committee

Agenda Item 6c

May 15, 2018

Item Name: Assembly Bill 1912 Public Employees' Retirement: Joint Powers Agreements Liability

As Amended April 19, 2018

Sponsor: Service Employees International Union, California

Program: Legislation

Item Type: Action

Recommendation

Adopt a **SUPPORT, IF AMENDED** position on Assembly Bill (AB) 1912 because this bill provides protection to current and future members employed by Joint Powers Agencies (JPAs) who are members of the California Public Employees' Retirement System (CalPERS).

Executive Summary

AB 1912 eliminates the ability of JPAs and community choice aggregators to specify in their joint powers agreements that the debts, liabilities, and obligations of the JPA shall not be those of its member agencies. It makes all current and former JPA member agencies jointly and severally liable for the JPA's debts to a retirement system, and allows for retroactive application of judgments for breach of a party's obligations to the retirement system. In addition, the bill prohibits CalPERS from contracting with a JPA whose member agencies do not accept joint and several liability for the JPA's pension obligation, requires new and existing JPA contracts with CalPERS to require inclusion of such a provision, and extends CalPERS lien authority to the assets of the member agencies of a terminated JPA. It also requires CalPERS, at the request of a terminating agency, to contract to preserve the highest final compensation for the terminating agency's members. AB 1912 further requires CalPERS to file a civil action against member agencies of a terminated JPA to compel payment of the JPA's pension obligations, and removes the authority of the CalPERS Board of Administration (Board) to elect not to reduce member benefits as their employers' liabilities and assets are moved into the Terminated Agency Pool (TAP).

Strategic Plan

This proposal supports the 2017-22 CalPERS Strategic Plan to strengthen the long-term sustainability of the pension fund, and to reduce complexity across the enterprise.

Background

Existing law allows two or more public agencies to jointly exercise common powers to create JPAs to fulfill a service for the member agencies. Pursuant to Government Code (GC) section 6500, member agencies that can exercise joint powers include, but are not limited to, federal agencies, state departments, counties, cities, special districts, school districts, and federally recognized Native American tribes.

Currently, CalPERS provides retirement benefits for 1,511 public agencies and 162 are JPAs. JPAs are established under the Joint Exercise of Powers Act. A JPA is a new, separate organization created by the member agencies, that is legally independent from them. The joint powers agreement describes the size, structure, and membership of the JPA's governing board and documents the JPA's powers and functions. Historically, member agencies of JPAs that contract with CalPERS for retirement benefits have disclaimed liability for the debts and obligations of the JPAs.

CalPERS' 2016 Annual Valuation Reports identified 24,724 CalPERS members that earned service through a contracting JPA, which is approximately 3 percent of the public agency participant total. The combined Unfunded Actuarial Liability for the contacting JPAs is approximately $855 million, which represents a combined funded status of 75 percent.

In the past year, CalPERS has: 1) terminated and placed one JPA that participated in the System into the TAP for failure to pay the required contributions for its current and former employees and retirees; and 2) denied four JPAs that applied to become contracting agencies, but had not required their own member agencies to be jointly and severally liable for their debts and liabilities, including their pension obligations. Three of four JPAs initially appealed CalPERS' decision, but ultimately withdrew their appeals. CalPERS was unsuccessful in its attempts to collect the required contributions from a defunct JPA and its member agencies stated they were not liable for the pension obligations. As a result, its former employees' retirement benefits were reduced by approximately 63 percent. Attaching liability for a JPA's retirement benefits to its member agencies will help ensure that current and future CalPERS members receive their promised retirement benefits.

In accordance with Internal Revenue Service guidance and as set forth in Circular Letter No. 200-022-13, when a prospective public agency requests to contract with CalPERS for retirement benefits, the agency is required to complete a New Applicant Questionnaire to determine whether it is eligible to participate in the System. Currently, JPAs seeking to contract with CalPERS are, among other things, required to have their member agencies accept liability for all debts and liabilities of the JPA, including retirement obligations in its Joint Powers Agreement. This has led some prospective agencies to challenge CalPERS' determinations or abandon the contracting process. Memorializing this policy in statute will help ensure that current and future public employees receive their retirement benefits.

Analysis

1. Specifically, AB 1912:
    - Amends provisions in existing law to remove the ability of JPA member agencies to disclaim liability for the debts, liabilities, and obligations of the JPAs.
    - Makes all current and former JPA member agencies jointly and severally liable for the JPA's debts to a retirement system. It allows for retroactive application of judgments for breach of a party's obligations to a retirement system.
    - Prohibits CalPERS from contracting with a JPA whose member agencies do not accept joint and several liability and reopens existing JPA contracts with CalPERS to require inclusion of such a provision.
    - Allows the Board to elect not to enter into a termination agreement with a JPA under specified conditions and requires the member agencies of the JPA to then assume those retirement obligations.

- Requires CalPERS to file a civil action against the member agencies of a terminated JPA to compel payment of the pension obligations of the terminated JPA, and allows the Board to recover attorney's fees and other costs.
- Extends CalPERS lien authority to the assets of the member agencies of a JPA
- Removes the authority of the Board to elect not to reduce member benefits as their employers' liabilities and assets are moved into the TAP.
- Requires CalPERS, at the request of a terminating agency, to contract to preserve the highest final compensation for the terminating agency's members.
- Requires a JPA or its member agencies to notify CalPERS of its intention to enter into an agreement to preserve the aforementioned highest final compensation, within a specified time prior to the JPA's termination date and permits CalPERS to refuse to enter into an agreement if it determines that it is not in the best interests of the retirement system.

2. Arguments in Support
According to the Orange County of Professional Firefighters Association (OCPFA), "[p]rotecting our members' safety, working conditions, and their hard-earned retirement benefits are top priorities …" Furthermore, OCPFA states that "[w]e cannot allow bad actors in a JPA to forfeit their responsibility to employees who have loyally served their community," and that, "[i]n the case of our Firefighters, they have played by the rules and risk their lives on a daily basis to save property and people throughout Orange County. They have contributed to their retirement plans and it should not be possible for a unilateral action to deny their hard-earned pension benefits."

3. Arguments in Opposition
The California Association of Joint Powers Authorities, California Special Districts Association, California State Association of Counties, County of Riverside, League of California Cities, and Urban Counties of California state that the bill conflicts with the California State Constitution "… constitutional debt limit prohibits an agency from incurring indebtedness beyond the agency's ability to pay the debt back from revenues received in the same fiscal year without the approval of two-thirds of its voters. These safeguards were placed in the state's constitution to avoid a situation in which the holders of an issue of bonds might compel an increase in taxes or foreclose on an agency's assets.

"… applying retroactive joint and several liability to existing contracts, agencies will not incur significant debts that in many cases will exceed an agency's annual revenue without receiving voter approval – thus violating the sighted provision.

" … [a] JPA is an independent governmental body whereby the agency members have no legal, statutory oversight or managing authority – liabilities from cash entities retroactively applied to each member agency would constitute a gift of public funds to an individual(s) and/or public entity."

4. CalPERS Recommended Amendments/Concerns
CalPERS team members identified three concerns with the bill. First, it requires CalPERS to file a civil action against any and all member agencies of a terminated JPA to compel payment of the JPA's pension obligations. To remove CalPERS' discretion to sue impinges on CalPERS' exercise of its fiduciary duty to the system as a whole. Generally, the Board as a trustee takes reasonable, prudent steps to collect outstanding debts. The question becomes what steps are necessary to discharge this duty to collect. That inquiry depends

on the facts of each case but generally requires a weighing of the likelihood of successful collection efforts against their cost. Among the factors to be considered in any particular case are the amount of the delinquency, the employer's solvency, and whether the agency has sufficient assets against which to enforce a judgment. This decision must be left to the discretion of the Board. Team members concluded that the provision needs to be permissive and not mandatory.

Second, JPA member agency liability extends only to pension obligations and not to all debts and liabilities of the JPA. This is not necessarily a fiscal issue for CalPERS, but rather it goes to whether the agency would be eligible under the Internal Revenue Services' guidance regarding the types of entities that may participate in a governmental plan.

Third, the bill adds an unnecessary section to the Government Code-proposed section 20575.1. This provision appears to be modeled after section 20575, which allows a voluntarily terminating agency to ensure that its employees service at the terminating agency will be credited with their ultimate final compensation. Any voluntarily terminating JPA can already avail itself of this provision. Furthermore, subdivision (d) of proposed section 20575.1 requires the apportionment of the terminating JPA's retirement obligations between the member agencies, but such apportioned liability does not comport with, and appears to undermine, the requirement in the bill that all current and former member agencies of a JPA are jointly and severally liable for retirement obligations of the JPA.

Budget and Fiscal Impacts

1. Benefit Costs
   Undetermined.

2. Administrative Costs
   CalPERS team members estimate that the cost to work with the existing 160 JPAs to amend their JPA agreements to include the "joint and several liability provisions" to be approximately $30,000.

   The litigation costs for CalPERS to pursue legal action against member agencies and place a lien on the assets of a terminated JPA are undetermined, but may be significant.

Benefits and Risks

1. Benefits:
   - According to the California State Retirees, this bill "will protect employees and retirees of these JPAs by ensuring that their retirement benefits will be paid in full, as promised, even if a JPA dissolves or terminates their contract with a pension system."
   - Ensures that member agencies forming JPAs will be liable for its pension obligations.
   - Makes explicit CalPERS' authority to prohibit a JPA from participating in CalPERS if the JPA's member agencies are not financially liable for the retirement benefits.
   - Helps ensure payment of current and future JPA employees' retirement benefits.

2. Risks:
   - According to the opponents, this measure "gives exclusive authority to the retirement agency to assign liability" and it "would be virtually impossible for the JPAs governmental body, let alone a retirement agency, to retroactively assign equitable retirement specific liabilities to potentially hundreds of agencies."

Attachments
Attachment 1 – Legislative History
Attachment 2 – Support & Opposition

____
Brad W. Pacheco
Deputy Executive Officer

____
Charles A. Asubonten
Chief Financial Officer