CalPERS

Board of Administration Offsite

July 16, 2018

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

As Amended July 3, 2018

Sponsor: Service Employees International Union, California

Program: Legislation

Item Type: Action

Recommendation

Adopt a **SUPPORT, IF AMENDED** position on Assembly Bill (AB) 1912 (Rodriguez) to the extent this bill provides additional protection to current and future members employed by Joint Powers Authorities (JPAs) that contract with the California Public Employees' Retirement System (CalPERS), and the provisions are amended as follows:

- For voluntary terminations under Sections 20570 and 20571 of the Public Employees' Retirement Law (PERL), require the member agencies of a terminating JPA to submit their mutual agreement for apportionment of liability with the notice of intent to terminate;
- For involuntary contract terminations under Section 20572 of the PERL, require a JPA's member agencies to submit their mutual agreement for apportionment within 60 calendar days of the CalPERS Board of Administration's (Board) demand. If the member agencies fail to provide their mutual agreement, the member agencies shall be bound by the Board's determination to apportion liability; and
- Clarify that the decision to sue and initiate other collection efforts should be consistent with the Board's fiduciary duties.

Executive Summary

Among other things, AB 1912 would require the member agencies of a JPA that participates in a public retirement system to reach mutual agreement on the apportionment of JPA retirement obligations to the retirement system prior to the termination of its retirement contract, as specified. It also requires a retirement board to apportion those liabilities among the member agencies when they fail to reach agreement, and authorizes the member agencies to challenge that apportionment through arbitration, as specified. AB 1912 extends CalPERS lien authority to member agencies of a JPA that terminates its contract. It also requires CalPERS to consider and exhaust all options and necessary actions prior to reducing retirement benefits paid to former employees of JPAs from 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 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 contracting 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, or its member agencies that had limited their liability for the debts and obligations of the JPA. 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.

Analysis
1. Key provisions of AB 1912:
   - Limits the ability of JPA member agencies to disclaim retirement liability of the JPA to a public retirement system.
   - Requires the member agencies of a JPA to mutually agree as to the apportionment of the JPA's retirement obligations among themselves prior to a termination pursuant to the sections of the PERL that outline the process by which a CalPERS member agency can voluntarily terminate its contract or the CalPERS Board can terminate an agency's contract involuntarily for nonpayment, or a decision by the governing body of the JPA to dissolve or to cease the operations of the agency.
   - Requires a retirement board to apportion the retirement liability of the JPA to each member agency based on the share of service received from the agency, or population of each member agency, when the member agencies are unable to reach mutual agreement.
   - Allows member agencies specified in the retirement board's apportionment to challenge its determinations, which shall be referred to an arbitrator, who is granted sole discretion in the final disposition of apportionment, and requires the arbitrator to submit a copy of that determination to the retirement board within seven days.

- Requires apportionment under all three determination methods to equal 100 percent of the retirement liability of the JPA and allows apportionment to former member agencies.
- Prohibits the effective date for the dissolution of a JPA or the termination of its retirement contract to occur until a final decision regarding apportionment of its retirement liabilities is reached.
- Applies the preceding liability apportionment provisions retroactively to a member agency, or current and former member agency of a JPA that has an agreement in existence with a retirement board on or before January 1, 2019, unless the JPA dissolved prior to that date.
- Establishes in the PERL, provisions for the Board to exercise a lien on the assets of a terminating JPA, to include the assets of all parties to a JPA that terminates its CalPERS contract, and subject only to a prior lien for wages.
  - Establishes in the PERL, alternative provisions that allow, but do not require, the Board to enter into an agreement with the governing body of a terminating JPA or member agency to preserve the ability of its employees to have their highest final compensation used in the calculation of benefits earned under the JPA, and ensure that benefit is adequately funded prior to termination.
- Removes the authority of the Board to elect not to reduce member benefits as their employers' liabilities and assets are moved into the Terminated Agency Pool.
  - Requires the Board, prior to reducing the retirement benefit of a member formerly employed by a terminating JPA, to consider and exhaust all options and necessary actions, including evaluating whether to bring a civil action against any and all of the member agencies that are parties to a terminated JPA, to compel payment of a terminated JPA's retirement obligations, to include reasonable attorney's fees and other costs.

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
A coalition consisting of, among other, the California Association of Joint Powers Authorities, California Fire Chiefs Association, California Special Districts Association, California State Association of Counties, Fire Districts Association of California, League of California Cities, and Urban Counties of California have contended in a letter opposing a prior amended version of the bill that the "… 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."

   CalPERS Concerns
   CalPERS team members' primary concerns are the bill applies the same three step process to apportion liability to both voluntary and involuntary terminations, and does not include any timelines or deadlines for the member agencies to follow. Because a default in payment

obligations is a basis for an involuntary termination under the PERL, team members recommend following a more streamlined process that requires member agencies to submit a mutual agreement to apportion liability within 60 calendar days of the Board's demand pursuant to Section 20572 of the PERL, and if no agreement is provided, allow the Board to apportion liability among the member agencies, which determination shall be binding on the member agencies.

In the case of a voluntary termination pursuant to Sections 20570 and 20571 of the PERL, even though the bill precludes termination until a final determination of apportionment, team members recommend including the following timelines: 1) Require the member agencies to submit their mutual agreement with the notice of intent to terminate; 2) if the member agencies fail to agree, the Board shall determine apportionment within 60 calendar days after it receives all necessary information to determine share of service or population of the member agencies; and 3) any appeal of the Board's determination to binding arbitration must be initiated within 60 calendar days.

<u>Provisions Requiring Clarification</u>
Team members believe the bill adds an unnecessary provision to the PERL, proposed to become GC Section 20575.1. It 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. However, any voluntarily terminating JPA can already avail itself of this provision. Furthermore, AB 1912 requires the member agencies of a JPA that do not enter into an agreement under this provision to assume those obligations on their own retirement systems. It is unclear what CalPERS' role, if any, would be here.

Additionally, it requires CalPERS, prior to reducing the retirement benefits of the members of a terminating JPA as provided for in existing law, to consider and exhaust all options and necessary actions, including evaluating whether to bring a civil action against any and all of the member agencies that are parties to a terminated JPA. Team members recommend amendments to clarify that the decision to sue and initiate other collection efforts should be consistent with the Board's fiduciary duties.

Budget and Fiscal Impacts

1. <u>Benefit Costs</u>
   Undetermined.

2. <u>Administrative Costs</u>
   CalPERS team members are unable to estimate at this time, the cost to work with the existing contracting JPAs in the event their member agencies are unable to reach mutual agreement, for the System itself to apportion liabilities based on the JPA services each member agency receives, or by population.

   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. <u>Benefits:</u>
   - 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."

- Helps ensure that member agencies forming JPAs will be liable for its pension obligations.
- Helps ensure payment of current and future JPA employees' retirement benefits.

2. Risks:
   - The potentially extended length of time it may take to reach a final apportionment of liability among a JPA's member agencies, and for CalPERS to collect those funds has the potential to increase liabilities for member agencies.

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

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