



California Public Employees' Retirement System
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Announcements

Circular Letter

December 29, 2021

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Distribution: IV, V, VI, X, XII, XVI

To: All CalPERS Employers
Subject: Disallowed Compensation Benefit Adjustments: Senate Bill 278, Chapter 331, Statutes of 2021

Purpose

The purpose of this Circular Letter is to provide information regarding the addition of Government (Gov.) Code section 20164.5 (Chapter 331, Statutes of 2021) effective January 1, 2022, to the Public Employees' Retirement Law (PERL).

This provision defines disallowed compensation, stipulates what would occur if California Public Employees' Retirement System (CalPERS) determines disallowed compensation has been reported, and identifies the impacts on the pension benefits of a retired member, survivor, or beneficiary.

Disallowed Compensation

Under Gov. Code section 20164.5, disallowed compensation is compensation reported for a member by the state, a school employer, or a contracting agency that CalPERS subsequently determines is not in compliance with the California Public Employees' Pension Reform Act of 2013 (PEPRA) (Article 4 [commencing with section 7522] of Chapter 21 of Division 7 of Title 1), Gov. Code section 20636 or 20636.1 of the PERL, or the administrative regulations of the system under California Code of Regulations (CCR), title 2, section 571 and 571.1.

Overpayment and Penalty Obligations for Disallowed Compensation

If a misapplication or miscalculation of retirement benefits occurs due to disallowed compensation and the conditions under subdivision (b)(3)(A) of Gov. Code section 20164.5 are met, the employer will be liable to pay CalPERS the full cost of any overpayment and pay the impacted retiree a portion of the actuarial equivalent¹ of any reduced retirement benefit as a penalty.

The penalty is equal to 20% of the lump-sum of the actuarial equivalent present value of the difference between the monthly allowance based on the disallowed compensation and the adjusted monthly allowance for the duration that allowance is projected to be paid by the system. The employer will be required to pay:

- 90% of this penalty directly to the affected retired member, survivor, or beneficiary
- 10% of the penalty to CalPERS

Our Actuarial Office will provide the actuarial calculations to the employer for the amount due to both CalPERS and the member.

Overpayment and penalty obligations apply if all the following conditions under Gov. Code section 20164.5 subdivision (b)(3)(A) are met:

1. The compensation was reported, and contributions were made on that compensation while the member was actively employed.
2. The compensation was agreed to in a memorandum of understanding (MOU) or collective bargaining agreement between the employer and the recognized employee organization as compensation for pension purposes and the employer and the recognized employee organization did not knowingly agree to compensation that was disallowed.
3. The determination by the system that compensation was disallowed was made after the date of retirement.
4. The member was not aware that the compensation was disallowed at the time it was reported.

Not Covered under Disallowed Compensation

Payroll reporting errors and reporting special compensation items and pay rates above the maximum amount listed in a labor policy and/or agreements are not considered disallowed compensation; these types of errors are considered payroll reporting errors.

The following reporting errors are not within the scope of disallowed compensation under Gov. Code section 20164.5:

¹ Actuarial equivalent means a benefit of equal value when computed upon the basis of the mortality tables adopted and the actuarial interest rate fixed by the board under Gov. Code section 20013.

- Lump-sum reporting of reportable compensation
- Reporting compensation above the limit defined in the labor policies and/or agreements
- Misreporting of payroll such as, but not limited to:
 - Misreported pay rates such as \$10.00 versus \$100.00
 - Misreported pay rate types such as monthly as an hourly pay rate
 - Misidentified special compensation category and type

Compensation Review by CalPERS

Employers may submit an MOU, collective bargaining agreement, or other labor policies and/or agreements to CalPERS for review. We will determine if the compensation language item can be reported for retirement purposes.

It is important to report accurate member information in compliance with the PERL, PEPR, and title 2 of the CCR. Retirement benefits are calculated based on a member's years of service credit, age at retirement, and final compensation.² Inaccurate reporting of employee compensation leads to incorrect calculation of retirement benefits further resulting in underpayment or overpayment of contributions and benefits. If compensation items, such as labor agreement language and/or pay schedules, are submitted for review, the CalPERS MOU Review team will verify compliance of your proposed items and determine if the items are reportable for pension purposes. The MOU review can be completed within 90 days of receipt of all the required information. Email items for consideration to the [MOU Review Team](#).

Defining Compensation for Classic Members and PEPR Members

Compensation Earnable for Classic Members

Pursuant to Gov. Code sections 20636 and 20636.1, compensation earnable is defined as the pay rate and special compensation of the member, as further clarified by those statutes. It must also be 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 and paid pursuant to a publicly available pay schedule.

Gov. Code sections 20636(c) and 20636.1(c) further specify that special compensation includes any payment received for special skills, knowledge, abilities, work assignment, workdays or hours, or other work conditions. Pursuant to CCR, title 2, section 571, a list of special compensation items is identified along with the requirements under subsection (b).

² Final compensation is the highest annual compensation which was earnable during any consecutive 12- or 36-month period of employment preceding the effective date of retirement or last separation from service which ever is earlier.

Pensionable Compensation for PEPRA Members

Gov. Code section 7522.34 and CCR, title 2, section 571.1 state that pensionable compensation of a PEPRA member of any public retirement system is defined as the normal monthly rate of pay or base pay for normally required duties that must be historically consistent for the job classification and reported periodically as earned. It must also be 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 and paid pursuant to a publicly available pay schedule.

CCR, title 2, section 571.1(b) further identifies, clarifies, and defines the types of pay that meet the criteria of pensionable compensation according to each subsequent criterion set forth in subdivision (a) which must also be met.

Requirements of Publicly Available Pay Schedules

Subdivision (a) of CCR, title 2, section 570.5 lists the requirements for a publicly available pay schedule used to determine pay rates. Pay rates shall be limited to the amount listed on a pay schedule and does not include any additive pay or special compensation items into base pay. Any special compensation items, if requirements are met, must be reported separately from pay rate.

Retroactive Application of Procedures

Gov. Code section 20164.5 will apply to any determinations made on or after January 1, 2017, if an appeal has been filed and the member, retired member, survivor, or beneficiary has not exhausted their administrative or legal remedies.

Additional Resources

In reference to [Circular Letter 200-041-21 \(PDF\)](#), the [Compliance in Compensation Reporting](#) webpage provides tools and resources to educate employers about compensation reporting requirements to comply with the PERL. In addition, the [Special Compensation Reportability Table](#) provides reportability details for each member category within the identified special compensation category and type.

Questions

If you have any questions, call our CalPERS Customer Contact Center at **888 CalPERS** (or **888-225-7377**).

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