PENSION REFORM UPDATE – AB340

September 4, 2012

City Council Presentation

Background

For nearly 80 years, CalPERS has been administering retirement benefits for public employees and their families in accordance with the California Public Employees' Retirement Law and the California and United States Constitutions.

Currently, CalPERS manages retirement benefits for 1.6 million active and retired State, school and local government employees on behalf of more than 3,000 employers.

Last year, Governor Brown introduced a 12 Point Pension Reform Plan intended to implement comprehensive pension reform related to CALPERS. His plan was based on the need to address escalating costs associated with current benefit levels, which generally can't be supported due to underperforming CalPERS investments related to the current economy.

New California Public Employee's Pension Reform Act of 2013

After many months of public sector pension reform remaining a hot topic, the Conference Committee on Public Employee Pensions passed sweeping reforms of current pension law last week. The changes were subsequently approved on Friday, August 31, 2012 by the Assembly and Senate, and are awaiting the Governor's Signature.

In a press release last week, CalPERS indicated that the proposal includes significant changes that are intended to help protect and ensure the future sustainability of the retirement fund. CalPERS estimates the Pension Reform Act will save between $42 billion and $55 billion over 30 years for CalPERS administered pension plans.

It is important to note that "The Reform Act" – is currently being analyzed and interpreted by various agencies and law firms. We are actively reviewing all literature and will be engaging appropriately to stay abreast of developments and interpretations which provide us with further clarification on the intent of the language.

Original 12 Point Pension Reform Plan versus New Reform Act

The Reform Act will address most of the original 12 Point Pension Reform Plan. The original proposal called for a "hybrid" retirement benefit that combined a much smaller pension with a 401(k) plan and Social Security Benefits. This key aspect has been eliminated. The new Reform Act does NOT address the reduction in retiree health costs for State employees sought by the Governor.

Applicability and Effective Date

The new Pension Reform Act applies to all public employers and pension plans in effect on or after January 1, 2013 with the exception of University of California, charter cities and counties that DO NOT participate in CalPERS.

Most of the provisions in the package apply to NEW employees while some of the provisions apply to current employees.

NEW employees are defined as those hired after January 1, 2013, who have never been members of a public retirement system, or those with more than a six month break in service.

Of key importance to us are the provisions that apply to current employees.

Key Changes in Retirement Benefits

1. **Reduces Benefit Formulas and Increases Retirement Ages for New Members**

The available retirement formulas for new members hired after January 1, 2013, will be redefined and limited. There will be only one plan option for non-safety members, and three plan options for safety members. The retirement age for full retirement benefits will be raised to 67 for non-safety members and to 57 for safety members for maximum benefit.

2. **Prohibits retroactive Enhancements to Benefit Formulas for Current Members**

Public employers will be prohibited from granting any retroactive pension benefit enhancements that apply to service performed prior to January 1, 2013.

3. **Caps Pensionable Compensation for New Members**

The amount used to calculate pension benefits for new members hired after January 1, 2013 will be limited to no more than the Social Security wage index limit - $110,100 for employees who participate in Social Security, and $132,120 for those who do not. The cap will be adjusted each year based on changes to the Consumer Price Index.

4. **Changes Calculation of Benefits based on Regular, Recurring Pay for New Members**

Compensation for the purposes of retirement benefit calculation will be defined as the "normal rate of regular, recurring pay" ……… excluding special bonuses, unplanned overtime, payouts for unused sick leave and other special compensation.

5. **Changes Final Compensation Calculation to 3 Year Average for New Members**

To end the practice of "spiking", final compensation for NEW members will be determined based on the highest average annual compensation during a consecutive 36 month period.

6. **Changes Final Compensation for New Local Elected Members**

The Act would require that the final compensation for NEW local elected members be based on the highest average annual compensation for the period of service as a local elected member. New members would be those elected on or after January 1, 2013.

7. **Prohibits Pension Holidays by Employers**

This provision helps to secure the retirement system for the future by prohibiting employers from suspending the employer and/or employee contributions necessary to fund the annual normal cost rate of the pension.

8. **Implements Equal Sharing of Normal Costs for New and Current Members**

New members hired after January 1, 2013 will be required to pay at least 50% of annual normal costs as determined by the annual CalPERS actuary. This is the amount required to cover the cost of the benefit. Employers will be prohibited from paying this contribution on the employee's behalf. For contracting agencies, the intent of the Pension Reform Act is to increase the employee's contribution to 50% of the total annual normal cost through collective bargaining. If that is not accomplished through negotiations by 2018, the Act authorizes employers to increase employee contributions up to 8% of pay for local miscellaneous members and up to 12% of pay for local police and firefighters, subject to good faith bargaining.

9. **Imposes Federal Contribution and Benefit Limits for New Members**

Employers are prohibited from making contributions on any amounts of compensation that exceed the limit established by the Internal Revenue Code. That limit is $250,000 for NEW members hired on or after January 1, 2013.

10. **Eliminates Purchase of "Air-Time" for New and Current Members**

The Act prohibits the purchase of service credit (known as Air Time) for periods for which there is no performance of service, on and after January 1, 2013.

11. **Requires Forfeiture of Pension Allowance Upon Conviction of a Felony for New and Current Members**

If convicted of a felony while and related to performing official duties, public officials and public employees would forfeit pension and retirement related benefits.

12. **Establishes Limitations on Post-Retirement Public Employment for Newly Retired Persons**

Requires that newly retired persons be required to "sit out" for at least 180 days before returning to work for an employer in the same retirement system, with some defined exceptions.

Rules are included in the Act consistent with previous legislation - AB1028, and limits a retiree to performing a cumulative 960 hours of work in a 12-month period for all employers in the same retirement system.

13. **Reduces Industrial Disability Retirement Benefits for Current Safety Members**

Local safety members who have become disabled as a result of a work related injury or illness are eligible to receive industrial disability. This benefit currently pays the member 50% of the member's compensation as a lifetime benefit. The Act will require that injured employees take a Service Retirement rather than IDR, if they have earned enough years of service to equal a benefit greater than 50% of compensation. This change allows members to receive a benefit that is more closely aligned to their years of service.

Incremental Progress

It is important to note that public employees in many jurisdictions have already made significant concessions over the last few years. As a result of prudent and effective Council direction, the City of Riverside has successfully achieved pension reform with all labor groups during the last round of labor negotiations.

These reforms include provisions in which all New Employees Pay their Own Share of the CalPERS contribution, and Final Compensation Calculation is based on the Average of Highest 3 years. This policy direction will result in a projected 20-year City savings of $386 Million. The City's employee groups are to be commended for their cooperative spirit in this important effort.

We also recognize that Pensions are an important part of employee compensation that enables successful recruitment and retention. The CalPERS benefit plan offers financial security for those public employees who are not covered by Social Security.

Next Steps

We will begin working with our labor groups related to the Pension Reform Act to discuss the impact of the provisions, and to engage in good faith bargaining where appropriate. The key issue we will have before us is the Cost-sharing provision for Current employees, which we have until 2018 to implement.

We will also be receiving further direction from CalPERS related to adopting the newly required resolutions and/or contract amendments to plan changes (new formulas) for NEW employees hired on or after January 1, 2013, and will return to Council as appropriate for further items of information and/or approval.