



Agency Watch



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**A PERIODIC PUBLICATION FOLLOWING
DEVELOPMENTS IN PUBLIC EMPLOYEE
RETIREMENT ISSUES.**

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QUESTIONS ON LEGISLATIVE MATTERS,
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WINTER 2010

END OF YEAR SUMMARY AND LOOKING AHEAD AT 2010

A BUDGET PREOCCUPATION

2010 began just like 2009 with major questions about how to resolve California's multi-billion dollar budget deficit. After tax increases, spending cuts, and a mixed bag of money-shifting gimmickry in 2009, a deficit still persists today. Meanwhile, public employee retirement-related bills and almost any other types of non-budgetary legislation became a second thought. A small number of retirement bills were introduced this session and an even smaller number have been enacted into statute. On the retirement front, 2010 begins with some serious questions about the sustainability of pension benefits on the media and public policy front.

PENSION SUSTAINABILITY

At the CalPERS Educational Forum in October, Ron Seeling, the CalPERS chief actuary, suggested that the state's pension system could be facing decades of unsustainable pension costs of on average 15% to 20% of pay for a miscellaneous plan and 35% of pay for a safety plan. CalPERS has announced plans to convene stakeholders – employers, labor and legislators – and start discussing sustainability of pension benefits. Retiree healthcare benefits are also being discussed, including approaches that limit benefit levels by instituting two-tier plans and cutting benefits for new hires.

GOVERNOR'S PENSION PROPOSAL

In his own attempt to head off the pension sustainability issue, the Governor proposed state employee pension and retiree healthcare reforms as part of his budget negotiations in 2009, just a few years after

his last pension reform proposal ended in a difficult fight with labor unions. This time the Governor proposed creating a two-tiered system under which new hires would be provided lower benefits than current employees receive. The proposal would essentially return employee pension formulas for new hires back to 1999 levels. The Governor's new budget proposal is quiet on this issue.

LATEST BALLOT MEASURE

Not to be outdone, the California Foundation for Fiscal Responsibility has decided to give pension reform another go through the ballot process in 2010 with a pair of initiatives. This time, instead of scrapping defined benefit plans for defined contribution plans (as Governor Schwarzenegger proposed during the Governor's first term), the group wants to keep defined benefit pension plans but reduce the benefits for newly-hired employees. The new plan would also raise the normal retirement ages for public safety and miscellaneous employees. Final compensation would be based on the highest five years of salary instead of the highest one year and retiree health benefits would only be available to new employees who work ten years for a public agency and have at least five consecutive years immediately prior to retirement. In addition, public agencies would be required to make their actuarially required contribution to their pension and retiree healthcare funds each year, regardless of their funded status.

2010

2010 will likely see increased focus on public employee benefits, particularly if retirement reduction propositions qualify for the state ballot, employer contribution increases become imminent and CalPERS stays in the news.



WAYS TO RECEIVE LEGISLATIVE DEVELOPMENTS FROM PARS

Periodic Legislative “PARS Agency Watch”

-- Please see the next edition of PARS Agency Watch for an update on California and federal developments. Feel free to call us to add other staff members to the Agency Watch mailing list.

Monthly PARS Legislative Email Alert

-- A monthly email communication for those interested in more timely information about California legislative developments in public employee retirement/benefits (sent out February through October). To receive this free service, just email your request to mtoal@pars.org or call 800.540.6369 x 135.

PARS Web Site -- Past editions of PARS Legislative Alerts and Agency Watch newsletters are also available on our web site at www.pars.org. We also include links to legislative web sites.

The contents of this publication reflect PARS' understanding of the facts. Before taking any action based on this information, consult professional advisors regarding your agency's specific objectives and circumstances. For further information, contact PARS.

CALPERS UPDATE

CALPERS INVESTMENT PERFORMANCE

While the market decline deserves most of the blame for the new surge in the unfunded CalPERS liability, according to Wilshire Associates (CalPERS' financial consultant) the nation's largest pension fund has now performed worse than the average large public pension fund over the past one, five and ten year periods. By the end of the June 30, 2009 reporting period, CalPERS' portfolio sank 23.5% in the 2008-09 fiscal year, while the average large pension fund dropped 18.8%. In real estate investments, CalPERS also fared worse than its peers losing an average of 8.6% per year over the last three years, while the average public pension fund's real estate investments lost 4 percent over that same period.

“SMOOTHING” POLICY CHANGES

In 2009, the PERS Board officially approved modifications to their “smoothing” method for schools and local agencies. The new plan temporarily buffers public agencies against the recent investment losses sustained by the retirement system. PERS took this action to keep from adding more stress to already strained government budgets. The losses from this year will be applied to the June 30, 2009 actuarial valuation, which is used to establish contribution rates for the 2011-12 fiscal year. This is when agencies would see larger contribution rate increases, particularly since PERS ended this plan year (as of June 30) with a 23.5% investment loss.

The smoothing changes would have the effect of phasing in the impact of the 2008-2009 investment losses over 3 fiscal years. The changes prevent employer rates from increasing dramatically in subsequent fiscal years if the financial markets rebound in 2009-2010 or 2010-2011. The Governor opposed the move questioning PERS' optimistic view of its investments and willingness to defer pension contributions to future generations.

CALSTRS UPDATE

CREDIT DOWNGRADED

CalSTRS credit rating was lowered by Fitch Ratings on August 21, 2009. Fitch cited investment losses (also at around 25%) and the fund's inability to raise employer contribution rates without the Legislature's approval. In the last fiscal year, the fund suffered nearly a \$42 billion loss. The downgrade by Wall Street will have little effect on CalSTRS itself but will likely mean higher interest costs for local governments that use the pension fund's credit rating when they borrow. CalSTRS has been lobbying for higher contribution rates and control over rate setting for years with little success. The state's budget problems and current economic forces make it unlikely that contribution rates will be increased as much as actuarially necessary for the foreseeable future likely forcing larger increases in the future.

LAST YEAR FOR MID-YEAR RETIREMENT INCENTIVES IN SCHOOLS

On October 11, 2009 the Governor signed Assembly Bill 506 (Chapter 306/2009) making this the last fiscal year in which K-12 districts will be able to do mid-year retirement incentives, at least in the current format. Districts using early retirement incentives to achieve fiscal savings will no longer be able to let employees retire mid-school year and then come back as long-term substitutes or emeritus teachers for the remainder of the school year.

As of July 1, 2010, STRS retirees who are under the “normal retirement age” of 60 will be prohibited from working in any STRS-related service for six months after they retire. A retiree who violates this will have their retirement allowance reduced up to the total annual retirement allowance that year.

BILLS SIGNED INTO LAW IN 2009

The following summarizes the key retirement related bills signed into law by the Governor during the first year of the

2009-10 session. As the fiscal problems of the State continue there is a fair chance that there will continue to be a relatively low number of retirement related bills put forward and/or acted upon in the second year of the session.

● **AB 86 (Nava) Airport Police Officers:**

This bill would authorize agencies to include certain airport law enforcement officers in the local safety member classification. This bill passed both houses last session but was vetoed by the Governor with the blanket “budget crisis” explanation. Similar bills have been resisted by public agencies and public safety unions in the past for cost reasons and to restrict which groups receive safety benefits. However, the case was made that in the wake of 9/11, Airport Patrol Officers, who are armed and emergency first respondents in airports, now have greater responsibility and face significant injury risk in performance of their duties to deter potential terrorists. (Chapter 79)

● **AB 232 (Hill) STRS Benefit Payment Information:**

This bill would eliminate a requirement that STRS send a copy of the benefit payment information to any retired member, disabled member or beneficiary who has payments transmitted by direct deposit or by mail to a financial institution. (Chapter 90)

● **AB 399 (Brownly) PERS – Accumulated Contributions:**

This bill requires PERS to provide members who have separated from all service, and who have attained age 70, with an election form to take a refund of their retirement account contributions or apply for retirement if vested. (Chapter 240)

● **AB 506 (Furutani) STRS Post-Retirement Earnings Limits:** AB 506 makes the following specific changes to the STRS post-retirement earnings limitations:

- After July 1, 2010, employees who retire and are then rehired by a district within six months after retirement, and who would be less than age 60 at the time they

returned to work, will see a dollar for dollar reduction in their STRS benefit.

- Extends current exemptions from the STRS post-retirement earnings limit for two years, until June 30, 2012.
- Makes exemptions, after June 30, 2010, available to support staff who retired prior to January 1, 2009.
- Requires documentation of eligibility for any exemption to be received by STRS no later than June 30 of the school year for which the exemption is to apply. (Chapter 306)

● **AB 654 (Mendoza) STRS – Penalties and Fees:**

This bill would allow STRS to: 1) charge interest on installment payments to purchase “air-time”, 2) charge interest on delinquent contributions, and 3) assess penalties or fees on late or improper reports from schools and agencies. (Chapter 249)

● **AB 966 (Committee on Public Employees, Retirement and Social Security) PERS Housekeeping Bill:**

Among other provisions, this bill excluded from PERS membership any employee whose appointment or employment contract does not fix a term of full-time, continuous employment over 6 months, unless exceptions apply such as if it requires service of an average of 20 hours per week for one year or longer or if the person completes 125 days or 1,000 hours. (Chapter 130)

● **AB 1584 (Committee on Public Employees, Retirement and Social Security) Placement Agents Disclosures:**

This bill requires public retirement system boards to develop and implement a policy requiring the disclosure of payments to placement agents. The bill also expands post-employment restrictions on high level officers and investment staff of local pensions funds ('37 Act funds), so that they are consistent with restrictions that currently apply to officers and staff members of CalPERS and CalSTRS. (Chapter 301)

PARS BENEFIT PROGRAMS

PARS EARLY RETIREMENT INCENTIVES

During these difficult budgetary times, PARS is analyzing, designing, and implementing retirement and separation incentives programs to assist public agencies in achieving fiscal savings and staff reorganization. Since 1983, PARS has implemented more than 500 retirement incentives, primarily for educational agencies in California. **Contact PARS for a free analysis.**

PARS GASB 45 TRUST PROGRAM FOR MUNICIPALITIES AND SPECIAL DISTRICTS

PARS, in conjunction with Union Bank, has created a “one-stop” program of services and an irrevocable trust to fund post-employment benefits for cities, counties, and special districts. The California Special Districts Association joined as an endorsing program sponsor in 2008.

CSBA GASB 45 SOLUTIONS PROGRAM FOR EDUCATIONAL AGENCIES

In partnership with the California School Boards Association, PARS administers the GASB 45 Solutions Program to provide educational agencies, including school districts, community college districts, and county offices of education, with a comprehensive trust solution and other services to assist them with retiree healthcare and liability. The California County Superintendents Educational Services Association (CCSESA) joined as an endorsing program sponsor in 2005.

PARS RETIREMENT ENHANCEMENT PLANS

With CalPERS’ admission that future projected contribution rates are unsustainable, employers should be aware of other options to provide supplemental retirement benefits. PARS Retirement Enhancement Plans (REP) can be utilized to attract and retain highly qualified managers and staff by adding an additional layer of retirement benefits to an agency's existing plan. Protections through plan design can contain costs for employers and employees.

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- **SB 519 (Ashburn) PERS Death Benefits:** This bill deletes the provisions for PERS pre-retirement death benefit eligibility that would change the law on January 1, 2010, to spouses attaining age 62 instead of 60, and instead maintains the current benefits indefinitely. (Chapter 188)
- **SB 634 (Committee on Public Employees and Retirement) STRS Housekeeping Bill:** Among others, there is a provision to make membership election irrevocable for substitute teachers and other part-time employees who optionally select to participate in the STRS Defined Benefit Program (participation in STRS is not mandatory for part-time employees) which would remain in effect until the member terminates employment. The bill also covers changes in eligibility for reduction-in-service, domestic partner

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rights, documentation for post-retirement earnings, beneficiary law, and other matters. (Chapter 304)

- **SB 752 (Correa) Voluntary 2nd Tier in Orange County Retirement System:** This bill establishes a voluntary 2nd tier in the pension system in Orange County. New hires must elect to join one of the two tiers when they are hired. The new tier has a reduced pension formula combined with a defined contribution account. (Chapter 362)

EYE ON WASHINGTON

IRS ANNOUNCES PENSION PLAN LIMITATIONS FOR 2010

The Internal Revenue Service has announced that cost-of-living adjustments applicable to dollar limitations for retirement plans will remain unchanged for 2010. Some analysts had expressed concern

that the IRS would be required to reduce the maximum that workers can contribute to plans. But the Treasury Department concluded that the relevant law doesn't require a reduction in limits for 2010, even though there was negative inflation.

While the maximum amount workers can contribute to their plans will remain the same next year, retirees who receive Social Security benefits won't get a cost-of-living increase for the first time in more than three decades. These announcements came in October after the Labor Department reported that the consumer price index fell in the third quarter from the year-ago quarter. Social Security benefits, retirement-plan limits and many other government programs are tied to the inflation rate during that period.

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