STAFF REPORT

AGENDA NO: 8c

MEETING DATE: September 3, 2019

To: Honorable Mayor and City Council

Date: September 3, 2019

From: Sonya M. Morrison, Human Resources Director – (650) 558-7209

Subject: Adoption of a Resolution Authorizing the Mayor to Send a Letter of Opposition Regarding SB 266, Public Employees' Retirement System: Disallowed Compensation: Benefit Adjustments

RECOMMENDATION

Staff recommends that the City Council adopt the attached resolution authorizing the Mayor to send a letter of opposition regarding SB 266, Public Employees' Retirement System: Disallowed Compensation: Benefit Adjustments.

BACKGROUND

The Public Employees Retirement Law (PERL) and the Public Employees' Pension Reform Act of 2013 (PEPRA) govern what an individual is entitled to receive as pension benefits in retirement. What an employee receives as a pension benefit is a factor of how long they have worked in a CalPERS agency, the pension formula, and their final compensation. The PERL and PEPRA govern what is included in final compensation, which is compensation earnable, pay rate, and special compensation. These terms are further defined in detail in the California Code of Regulations (CCR) sections 570 and 571, and these sections clearly define exactly what is eligible to be included in the final compensation calculation. Anything not included in the CCR sections 570 and 571 is considered 'disallowed compensation' by CalPERS and is excluded from the pension benefit calculation. CalPERS, as the administrator of the pension plan, interprets the PERL, PEPRA, and CCR when calculating the pension benefit for an individual, and their determination is final; appeals by an individual are heard and decided by the CalPERS Board of Directors.

The City and employee bargaining units negotiate components of compensation, including special compensation, which is memorialized in the Memoranda of Understanding the City holds with each bargaining unit. The City is careful to advise the bargaining units throughout this process that CalPERS is the authority and the final determination of what is considered 'pensionable compensation' and what is not (meaning what is allowed compensation and what is disallowed compensation for the purposes of determining the retirement benefit). The City follows the CCR regulations and works closely with CalPERS to try to ensure the components of compensation are accurately reported to CalPERS, but the ultimate determination is made by CalPERS when an individual retires and CalPERS calculates their pension benefit. The City has an incentive to accurately calculate and report compensation as corrections create an administrative burden and a budget impact.

Senate Bill 266, introduced by State Senator Connie Leyva, would significantly alter current legislation concerning responsibility for retirement liability created by disallowed compensation. The bill would abdicate all responsibility previously held by CalPERS to ensure that retirement benefits are calculated and administered correctly and require public agencies to directly pay retirees and/or their beneficiaries disallowed retirement benefits using General Fund dollars. The League of California Cities has taken an oppose position on this bill and requested that cities do so as well.

DISCUSSION

The provisions in SB 266 create policy, operational cost, and legal concerns for every local government agency and are retroactive.

Specifically SB 266:

- **Creates a Double Payment for the City:**
  Under current law, once a benefit is determined to be disallowed, both the employer and the employee cease making future payments on that benefit. Past contributions from the employee are returned to the employee, while past contributions from the employer are applied towards future payment. The employer has already made its contributions and should not be double paying for the benefit.

- **Means CalPERS has no Incentive to Properly Calculate Benefit Payments:**
  Recent amendments to the measure remove all responsibility by CalPERS to ensure benefits are reviewed, calculated, and administered correctly. Instead, SB 266 places sole responsibility on the employer—even if the employer exercises its right to have CalPERS review its compensation proposal. While staff understands that CalPERS has asserted that they face IRS plan qualification concerns for paying out an unlawful benefit, the fact that there is zero accountability or assurances afforded to the state or local agency when CalPERS reviews a compensation agreement is irrational.

- **Creates Compliance and Implementation Issues:**
  Under SB 266, the City would be issuing direct General Fund payments to retirees, which would trigger GASB 68 reporting requirements. Given the unique circumstances surrounding these overpayments, staff would have to track and report these liabilities. Such additional responsibilities will require the City to hire costly outside actuarial and legal experts to ensure that the City is following federal reporting laws. SB 266 is a de facto and retroactive benefit enhancement bill that would further strain cities' budgets at a time when retirement obligations are making it financially difficult to provide critical services for the public. The City has already seen dramatic increases in pension costs, with actuarial valuations estimating that Burlingame's pension costs will double over the next 8 to 10 years, to a high of over 82% of payroll for Safety employees and 42% pf payroll for Miscellaneous employees. These increases in pension cost obligations make it difficult for the City to fund infrastructure improvements and provide services.

  This measure also fails to consider the common practice of employees moving from jurisdiction to jurisdiction throughout their careers. Under normal circumstances, CalPERS pays out the benefit if an employee works for multiple agencies who enjoy reciprocity. However, under SB 266, it is unclear. Such confusion will lead to compliance, legal, and implementation challenges.

This measure would also require the City to track and maintain current records of all retirees and their beneficiaries in order to deliver the direct payment. SB 266 would present agencies with a costly logistical challenge.

- **Is a Gift of Public Funds and is a Violation of the California Constitution:** Under SB 266, the City of Burlingame would be issuing monthly, unlawful, payments to former employees and/ or their beneficiaries in perpetuity. Continued payment of a disallowed benefit to a retiree would constitute a gift of public funds, in violation of Section 6, Article 16 of the California Constitution. Such violation would leave a public agency left to defend itself from costly litigation lawsuits filed by members of the public.

Attempts by the League of California Cities to suggest a series of amendments to try and make the measure lawful and workable were rejected. These suggested amendments included, but weren't limited to:

- Eliminating the retroactivity provisions in the bill.

- Establishing a pre-retirement audit system through CalPERS that would enable the retiree to begin receiving base-salary pensionable compensation immediately allowing CalPERS to review special pay compensation and adjust the benefit upwards if required after the special compensation review. This would alleviate the concern regarding retirees' detrimentally relying on erroneous benefit calculations and would avoid a situation where CalPERS needs to reduce benefits paid in error.

- Allowing CalPERS to review and certify that proposed pensionable compensation meets standards set forth by CalPERS. Such certification would indemnify the agencies for liability resulting from a future CalPERS error.

For these reasons, staff recommends that the City Council oppose the bill and authorize the Mayor to share the City's opposition with the appropriate Legislators and the League of California Cities.

FISCAL IMPACT

The fiscal impact of this bill is difficult to determine, but is likely to be significant and include the cost of the administrative burden. The impact will increase the City's pension obligation, increasing the unfunded liability, increasing the required annual payments, and creating an ongoing financial burden on the City.

Exhibits:
- Resolution
- Draft letter of opposition letter
- Bill text