March 31, 2021

The Honorable Thomas J. Umberg
Chair, Senate Judiciary Committee
Legislative Office Building, Room 2187
Sacramento, CA 95814

RE: Senate Bill 278 (Leyva) - Public Employees' Retirement System. Disallowed Compensation. Benefit Adjustments.
Notice of Opposition [As Amended 03/23/2021]

Dear Senator Umberg:

On behalf of the organizations below representing cities, counties, special districts, joint powers authorities, county offices of education, and school districts, we write to respectfully oppose Senate Bill (SB) 278, which would require public agencies and schools to directly pay retirees and/or their beneficiaries disallowed retirement benefits using general fund and Proposition 98 dollars. SB 278 places 100 percent of the total liability for such overpayments on public agencies—abdicating all responsibility previously held by CalPERS to ensure that retirement benefits are calculated and administered correctly. As such, SB 278 is a de facto and retroactive benefit enhancement measure that would further strain local agency and school budgets at a time where the impacts of COVID-19 and retirement obligations are making it exceedingly difficult to effectively provide critical services for the public. Our objections to this measure are rooted in policy, operational, cost, and legal concerns that would inevitably face virtually every state and local government agency should this measure be signed into law.

CalPERS has No Incentive to Properly Calculate Benefit Payments
In 2012, the California State Legislature passed significant public pension reform legislation known as the Public Employees' Pension Reform Act (PEPRA,) which took effect January 1, 2013. While the reforms were significant, they led to confusion as to what may lawfully be offered as employee pension benefits. As a result, some public agencies and their represented employee organizations came to agreements on benefit packages that did not meet the new legal standards to be considered a pensionable benefit. Those future retirement benefits, which were being paid for by employers and employees into pension systems such as the California Public Employees Retirement System (CalPERS), were at some point determined to violate the law and were terminated. Terminated benefits that violate PEPRA are considered "disallowed benefits."

Under current law, once a benefit is determined to be disallowed, both the employer and the employee cease making future payments on that benefit and past contributions from the employee are returned to the employee, while past contributions from the employer are applied towards future payment. Unfortunately, in the case of a ***retiree*** that received the disallowed benefit, the pension system must recoup the overpaid benefit from the retiree and reduce the retiree's pension benefit prospectively. They must do so because it is unlawful to pay out a benefit that is not legally allowable or earned.

This measure removes all responsibility by CalPERS to ensure benefits are reviewed, calculated and administered correctly. SB 278 places sole responsibility on the employer—even if the employer exercises their right to have CalPERS review their compensation proposal as proposed in section 5 of the measure. Additionally, this measure would further remove accountability from CalPERS to provide the proper guidance needed by local agencies on compensation proposals. Specifically, in subdivision (1) of section (5), CalPERS is simply charged "upon request" to review the "consistency" of an agency compensation proposal, rather than ensuring that an agencies proposal is in compliance with the California Public Employees' Pension Reform Act of 2013 (PEPRA). Given there are nearly 3,000 local government employers in the CalPERS system—many with multiple bargaining units with varying degrees of sophistication and understanding of the compensation rules, this revised provision would not provide any safe guards for retirees, active employees or public employers. The lack of accountability by the administrator of public retirement benefits would lead to more confusion and compliance challenges for public agencies.

SB 278 Requirements Would Create Compliance and Implementation Issues
Under SB 278, the state, local agencies, and public schools would now be issuing payments to retirees by diverting resources from their general funds. Even though direct payments to retirees would be made outside of the retirement system, such liabilities still trigger GASB 68 reporting requirements. Given the unique circumstances surrounding these overpayments, agencies would now have to track and report these liabilities. Such additional responsibilities would require agencies to hire costly outside actuarial and legal experts to ensure that they follow federal reporting laws.

Moreover, the bill fails to consider the common practice of employees moving from jurisdiction to jurisdiction throughout their careers. What happens when a retiree worked for multiple public employers in different retirement systems? Under normal circumstances, CalPERS pays out the benefit if employee works for multiple agencies who enjoy reciprocity. However, under SB 278 it is unclear. Are multiple agencies now responsible for directly paying a retiree or beneficiary? What happens in the case where an employee's bargaining unit at one employer agreed to a disallowed benefit but worked for the majority of their career for another agency? Is the agency where the retiree worked longest on the hook for an agreement that they were not a party to? Such confusion would lead to compliance, legal and implementation challenges.

Gift of Public Funds is a Violation of the California Constitution
Senate Bill 278 would require agencies to issue unlawful, payments to former employees and/or their beneficiaries in perpetuity. Public agencies cannot continue to make payments to retirees as proposed

by SB 278 for the same legal basis that requires pension systems to recoup their disallowed retirement benefit payments to retirees. 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.

Again, it is unfortunate that after an agency and their bargaining unit came to an agreement on benefits and those benefits had been paid for any amount of time for the benefit to be taken from the retiree. Although public agencies may feel morally or ethically compelled to do so, public agencies simply cannot continue to make payments directly to a retiree for an unlawful benefit.

Findings and Declarations of the Measure Cause Concerns
Our organizations take exception to subdivision (f) of the findings and declarations of the measure. While public employers stipulate that submitting MOU's and reporting said compensation to CalPERS is required by law, the findings fail to acknowledge that such agreements are done so with mutual agreement and understanding of the laws that guide pensionable compensation. Sophisticated and highly trained legal counsel for **both employers and employees mutually agree** to terms of employment and compensation through the collective bargaining process. Moreover, it is the responsibility of all parties, including CalPERS, the administrative body who promulgates regulations that guide agencies to ensure that compensation as mutually agreed by both labor and management legal teams is in fact a lawful benefit. The findings fail to recognize this reality and insinuate that the employer is solely at fault for a process that includes labor, management, and CalPERS.

The moral hazard of assigning the financial liability of errors solely to the employer creates an incentive for organizations locally to bargain for benefits that the MOU declares to be pensionable. SB 278 will guarantee those employees a retirement benefit because the MOU treated them as such, in contravention of how state or federal law may treat those benefits. In the most egregious of examples, local parties may agree to MOU terms that (knowingly or not) violate state pension spiking laws. SB 278 would enshrine, rather than correct, those violations in perpetuity.

In subdivision (j) of the findings and declarations sets a dangerous legal precedent suggesting the Legislature's intent to perpetuate the continued misappropriation of public dollars for an "alleged misapplication or calculation of compensation occurs". To be clear, when CalPERS determines that a benefit is unlawful such a determination is not "alleged" but rather definite. It should be noted that if an active employee or a retiree has a dispute with the manner in which CalPERS calculates their full compensation, there are current and effective avenues to appeal such determination through the administrative law judge (ALJ) process. Once an error is identified and corrected, the spirt of the law is upheld. Lawmakers should exercise caution in supporting language that undermines the California Constitution and the public's trust.

For these reasons, public agency and educational organizations below must oppose SB 278. For any questions, please feel free to contact Bijan Mehryar, Legislative Representatives at the League of California Cities, at 916-882-9886 or bmehryar@cacities.org.

Sincerely,

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