Pension cuts coming for some California retirees after court ruling on spiking

County-run pension systems up and down California are preparing to reduce some retirees' income based on a recent state Supreme Court decision that disqualified certain kinds of pay from pension calculations.

The court's July 30 decision upheld a 2012 state law intended to stop public workers from inflating their pensions by manipulating their pay at the end of their careers. The ruling is guiding decisions about what kinds of special pay, such as on-call pay and vacation cashouts, must be excluded from the calculations that set pension amounts.

Local pension boards and their attorneys have identified thousands of pensions that are based partly on the kinds of pay that must be excluded, and they are recalculating monthly payments as a result, according to interviews and public meeting agendas.

The reductions could affect retirees and employees from 20 counties that run pension systems regulated by the County Employees Retirement Law of 1937. The court's decision won't affect state workers or retirees from local governments that contract with CalPERS, which is regulated by a different state law.

The ruling, issued in Alameda County Deputy Sheriff's Association v. Alameda County Employees' Retirement Association, is ushering in rare reductions to pensions that many public employees in California consider sacrosanct.

The court generally upheld the so-called California rule, which protects pensions from any reductions without corresponding new benefits, but it allowed a specific set of changes identified in the Public Employees' Pension Reform Act, often called PEPRA. The law, championed by former Gov. Jerry Brown and approved by the Legislature in 2012, went into effect on Jan. 1, 2013.

Sacramento County retirees are among those facing reductions.

The county's retirement system is preparing to reduce the pensions of former Sheriff's Department officers who received extra pay to take care of police dogs; plant operators and engineers who worked at 24-hour facilities and received standby pay; and employees who sold back two weeks' worth of vacation time in their final year of work, rather than the one week per calendar year the county allows, according to the system's website.

"The decision was made for us by the Supreme Court and we are complying with the court directive to administer the law as the Legislature intended it to be administered," said Eric

Stern, chief executive officer of the Sacramento County Employees' Retirement System. "That doesn't provide any comfort to anyone, but that's the role we play."

The changes vary from county to county, based partly on how each system chose to implement PEPRA when it was passed. In Sacramento and Stanislaus counties, reductions are expected to range from 1 or 2 percentage points to up to about 10%.

Some systems moved immediately in 2013 to make the changes. Among them were the Alameda system at the center of the lawsuit, along with Merced and Contra Costa county systems, which also were sued.

Some systems made partial changes, while others waited until the lawsuits played out, which ended up taking more than seven years. Those systems are now proposing the biggest changes.

The Kern County Employees' Retirement Association waited for the court's decision and is now preparing to exclude 29 types of pay that have been counted toward pensions, according to a list on the system's website. The types of pay that could be excluded range from on-call pay to special stipends for things like bomb detail, SWAT team physical fitness and canine care. Also to be excluded are payments workers could receive if they didn't buy health insurance through their employer.

"The status quo has been maintained for all these years," said Dominic Brown, the system's executive director. "Now the court has said the way things should have been in 2013 and now we have to make corrections."

BILLS OR REFUNDS?

Many questions remain about how each system will apply the court's ruling. Decisions by local pension boards could have big impacts on retirees.

Among the most pressing questions is whether pension systems will force retirees to return the money that was improperly paid to them since 2013. Kern County retirees got notices raising that possibility, but Brown said the system's board was still weighing options Wednesday.

So far, retirement systems are deciding against clawing back overpayments. Along with Sacramento, systems in San Bernardino, Mendocino and Stanislaus counties have decided not to seek repayment, according to interviews and board meeting materials.

Staff at the Sacramento County system have recommended against clawing back the overpayments. The system's board meets Sept. 16.

The systems could reverse course if the Internal Revenue Service orders them to collect the money, according to meeting materials.

Conversely, there are questions over whether pension systems might owe retirees refunds.

Workers contribute a percentage of their pay toward their pensions, and they contribute extra for special pay that is pensionable. Cutting off pension benefits “might entitle employees to a partial refund” to account for the contributions they made toward canceled benefits, the Supreme Court said in a footnote to its decision.

Lower courts, which the Supreme Court left to work out some of the details, also could address clawbacks or refunds.

“That’s a big unknown,” Rick Santos, executive director of the Stanislaus County Employees’ Retirement Association, said of retroactive adjustments.

WHO IS AFFECTED

The timing and the extent of upcoming changes vary by county. Representatives of the systems said they are beginning to notify workers and retirees who will be affected.

The Stanislaus County system has already processed the changes, Santos said.

The system’s board decided in 2012 to exclude from pensions all types of special pay except for on-call pay, he said. After the court’s decision, the system recalculated pensions back to the beginning of 2013 to exclude on-call pay.

The reductions will affect 74 of the $2.2 billion system’s 4,000 retired members, Santos said. He said the reductions average 4% and will take effect Oct. 1.

Most other systems, including those in Sacramento and Kern counties, are finalizing the changes they will make and then have to process them. Both systems anticipate making the changes in the next few months.

Stern, from the Sacramento County system, said he expects the changes to affect “a few hundred to a few thousand” retirees and employees. The $10 billion system has about 12,700 active members and about 12,400 retired members.

He said reductions, which will correct pension payments dating to the beginning of 2013, could amount to as much as 10% for some, with officers who received the canine payments likely to be among the most affected.

Fresno County’s system has determined it won’t have to recalculate benefits, since it has adhered to the 2012 law’s guidelines since the law went into effect, according to a board meeting agenda.

The San Luis Obispo County Pension Trust won’t make changes because it has always excluded all varieties of special pay from pension calculations, said the trust’s executive director, Carl Nelson.

MISAPPLICATIONS

David Mastagni, an attorney representing the sheriff's deputies who sued the Alameda County system, said many local pension boards are misapplying the court's decision.

The 2012 law specifically excludes payments for shifts outside normal working hours, including standby pay and on-call pay.

Mastagni maintains that if workers received the special types of pay as part of their regular duties over many years, rather than just at the end of their careers, the pay should remain pensionable under the Alameda decision.

In addition to its specific exclusions, the 2012 law forbids any payments paid specifically to enhance someone's retirement benefit, as determined by a pension board. That allows some discretion that Mastagni says is being applied too broadly.

He referenced another section of the 2012 law that requires boards to set up a process through which workers can challenge some of of their retirement boards' determinations. He said retirees' due process rights should be honored as the boards make changes.

"I'm hoping that everybody can get on the same page with those things so there's not another round of litigation, because boards are misapplying the statute and misapplying their discretion and/or applying it retroactively," Mastagni said.

Directors of the systems said they are following their attorneys' interpretations of the court's decision.