

## **LEGISLATIVE PROPOSAL: Service Retirement Benefit Backdating**

### **SUMMARY**

This proposal, effective upon authorization by the Teachers' Retirement Board, would reduce the timeframe members may backdate their service retirement or service retirement during evaluation of a disability application from as early as January 1, 2012, or January 1, 2014, respectively, to up to 180 calendar days prior to when CalSTRS receives their retirement or disability application.

### **RECOMMENDATION**

**Sponsor.** The board's policy is to support or sponsor legislation that reduces inequities or deficiencies in plan design.

### **REASON FOR THE PROPOSAL**

This proposal would minimize unintended consequences affecting tax liability and other income-based non-CalSTRS benefits for members who request significantly backdated service retirement benefits, avoid reputational risk associated with large pension payouts, and prevent potentially paying out more based on Defined Benefit Supplement (DBS) additional earnings credits (AECs) than the pension administration system otherwise would have.

### **ANALYSIS**

#### **Existing Law:**

Existing law allows members applying for service retirement under the Defined Benefit Program to choose a retirement date no earlier than January 1, 2012. Members applying for service retirement during the evaluation of a disability application can select a service retirement date as early as January 1, 2014.

#### **This Proposal:**

This proposal, effective upon authorization by the board, would reduce the window in which members may backdate their service retirement or service retirement during the evaluation of a disability application to up to 180 calendar days prior to when CalSTRS receives their retirement or disability application.

### **PROGRAM BACKGROUND**

Chapter 703, Statutes of 2011 (SB 349–McLeod), amended Education Code section 24204 to provide members greater flexibility in electing service retirement benefit effective dates, allowing members to backdate as early as January 1, 2012, the effective date of this legislation. Chapter 558, Statutes of 2013 (AB 1379–PE,R&SS), amended Education Code section 24201.5 to provide that flexibility to as early as January 1, 2014, for service retirement during evaluation of a disability application.

Between January 1, 2017, and January 1, 2022, 89% of members who backdated their service retirement requested a benefit effective date within six months of when their application was

received. Only 2% of backdating members during the same timeframe selected a benefit effective date more than two years from when their application was received, with the longest being about 5.45 years.

Some members taking advantage of the flexibility to backdate their service retirement several months or years have found that the resulting large lump-sum payments have created significant issues with tax liability, retroactive Social Security offsets and qualification for other income-based non-CalSTRS benefits, including Medicare. In addition, significant backdating creates some unintended consequences for the payout of the DBS account. The pension administration system is programmed to include AECs up until the date the retroactive payments are made. AECs are otherwise not granted to members who are retired. This results in a greater benefit than for those members who begin payments immediately following their selected benefit effective date.

By virtue of when the amendments to Education Code section 24204 took effect, it is possible that a member could backdate their service retirement to sometime between January 1, 2012, and June 30, 2012. If all other eligibility requirements were to be met, that member could potentially participate in the Medicare Premium Payment Program, which is currently only available to members who retired before July 1, 2012. This scenario, which remains highly unlikely as no benefit effective dates have been backdated to that extent, would be eliminated by this proposal.

## **FISCAL IMPACT**

Program Cost – May result in minor savings to the Teachers’ Retirement Fund by preventing paying out large lump sums and more DBS AECs than the pension administration system otherwise would have.

Administrative Costs/Savings – Costs are estimated to be approximately \$150,000 for changes to the new pension administration system. Updating the existing pension administration system and online member interface would be an effort of two to five months for internal staff. Reductions in administrative workload and costs associated with unanticipated payments and large cash outflows are expected.

## **ARGUMENTS**

Pro: Minimizes unintended tax and other income-based non-CalSTRS benefit consequences.

Creates potential minor savings to the fund.

Con: May draw criticism for restricting members’ existing flexibility and could invite disputes from members whose retirement planning included a significant backdate.

Creates workload and cost pressure related to updating pension administration systems.