

**CALIFORNIA STATE TEACHERS'
RETIREMENT SYSTEM**

BILL ANALYSIS

CONFIDENTIAL-Government Code §6254(I)		
Department: California State Teachers' Retirement System	Author: Soto	Bill Number: AB 1432
Internal Routing:	Sponsor: CalSTRS	Version: Amended 5/21/2007
Subject: Federal Pension Law Conformity		Related Bills:

SUMMARY

This proposal conforms to the federal Pension Protection Act of 2006 to:

- Allow members of the Defined Benefit (DB) Program to purchase service credit for service performed in an educational institution that receives public funding located outside of the United States; and
- Authorize beneficiaries other than spouses to roll over a benefit distribution.

PURPOSE OF PROPOSAL

Provide consistency between federal pension law and the law governing pensions for California's public teachers.

BOARD POSITION

Sponsor.

SUMMARY OF AMENDMENTS

The May 21, 2007 amendments remove the urgency clause. If passed, the bill would become effective January 1, 2008.

Departments That May Be Affected		
CalSTRS		
<input type="checkbox"/> New / Increased Fee	<input type="checkbox"/> Governor's Appointment	<input type="checkbox"/> Legislative Appointment
<input type="checkbox"/> State Mandate	<input type="checkbox"/> Urgency Clause	<input type="checkbox"/> Regulations Required
		<input type="checkbox"/> Legislative Report
Board Position	Agency Secretary Position	Governor Office Use Only
<input checked="" type="checkbox"/> S <input type="checkbox"/> O <input type="checkbox"/> Defer to:	<input type="checkbox"/> S <input type="checkbox"/> O <input type="checkbox"/> Defer to:	_____ Position Approved
<input type="checkbox"/> SA <input type="checkbox"/> OUA	<input type="checkbox"/> SA <input type="checkbox"/> OUA	_____ Position Disapproved
<input type="checkbox"/> N <input type="checkbox"/> NP	<input type="checkbox"/> N <input type="checkbox"/> NP	_____ Position Noted
<input type="checkbox"/> NA	<input type="checkbox"/> NA	_____ No Position
Director _____ Date _____	Agency Secretary _____ Date _____	By _____ Date _____

SUMMARY

This proposal conforms to the federal Pension Protection Act of 2006 to:

- Allow members of the Defined Benefit (DB) Program to purchase service credit for service performed in an educational institution that receives public funding located outside of the United States; and
- Authorize beneficiaries other than spouses to roll over a benefit distribution.

PURPOSE OF PROPOSAL

Provide consistency between federal pension law and the law governing pensions for California's public teachers.

BOARD POSITION

Sponsor.

SUMMARY OF AMENDMENTS

The May 21, 2007 amendments remove the urgency clause. If passed, the bill would become effective January 1, 2008.

LEGISLATIVE HISTORY

Chapter 654, Statutes of 2006 (SB 1465—Soto), among other things, allows members to purchase up to two years of service credit for time spent teaching for the Peace Corps as permissive service credit.

Chapter 30, Statutes of 2002 (AB 131—Corbett), conforms California law to the rollover and service credit purchase provisions of the federal Economic Growth and Tax Relief Reconciliation Act of 2001 by allowing members to purchase service credit with newly authorized rollover funds.

Chapter 1074, Statutes of 1998 (SB 1021—PE&R), conforms California law to the federal Pension Simplification Act of 1996 and the Taxpayer Relief Act of 1997 by clarifying concurrent membership between CalSTRS, the California Public Employees' Retirement System and the 1937 Act County retirement systems.

PROGRAM BACKGROUND**Permissive Service Credit**

Permissive service credit can be purchased for performance of prior public educational services in other states and counts towards qualifying for the various benefit enhancements paid to DB members with 25 or 30 or more years of service credit, such as highest single year final compensation, the career factor and the longevity bonus. Service performed in a private school, whether in California or another state, is not considered permissive service. Purchases of non-qualified service credit are unrelated to any actual prior permissive service and do not count towards qualifying for such enhancements. Consistent with federal law, a member with at least

five years of service in the DB Program may purchase up to five years of nonqualified service credit by paying its entire actuarial cost.

Although teaching in another state is specified by Section 415(n) of the Internal Revenue Code (IRC) as permissive service that can be credited to a defined benefit retirement plan, such as the CalSTRS DB Program, teaching service in a foreign country, other than as a federal employee, was not previously identified as prior service eligible for purchase as permissive service. In addition, whereas California Education Code Section 22820 restricts the purchase of service credit to “service performed in a position while employed by a public educational institution located in another state or territory of the United States, or for educational service performed as an employee of the United States,” CalSTRS’ interpretation of previous federal law does not define public employees to include employees of foreign schools who receive some funds from the U.S. State Department and have been, therefore, ineligible to purchase credit for service performed therein.

The process for members who apply to purchase out-of-state service credit requires members to obtain the necessary information from their former employer and/or the retirement system to which the former employment was credited. The benefit owed to the member by the former retirement system must be forfeited in order for the member to purchase the service credit and have it credited to CalSTRS. The member is responsible for ensuring the former employer and/or retirement system provides information related to the type of employer and the type and basis of employment. Once the member receives the information, he or she forwards it to CalSTRS. Upon receiving the information, CalSTRS verifies the information provided and converts the employment information into service credit.

Rollover Distributions

CalSTRS allows DB members and participants of the Cash Balance Benefit Program to designate any person as a beneficiary; the relationship of the person to the member or participant is of no concern to CalSTRS. However, the means by which these funds are distributed varies depending on the type of beneficiary because until January 1, 2007, federal law prohibited beneficiaries other than spouses from rolling over a benefit distribution. Under state laws, registered domestic partners generally are accorded the same rights as spouses. Because their rights did not extend to federal tax matters, currently the Teachers’ Retirement Law specifically excludes domestic partners from the rollover provisions applicable to the DB Program. Being able to rollover a distribution enables the deferment of taxes to continue.

ANALYSIS

Permissive Service Credit

The Federal Pension Protection Act of 2006 permits pension systems to extend permissive service credit coverage to service performed in U.S. State Department schools and foreign elementary and secondary schools. AB 1432 allows members of the DB Program, other than retired members, to purchase credit for service performed in an educational institution located in a foreign country, consistent with the Pension Protection Act. The foreign school must receive at least a portion of its funding from public sources to be eligible for purchase. In addition, a foreign school participating in an arrangement with a Department of State school must receive its

funding from the Department of State under Title 22 of United States Code Section 2701 to be eligible for purchase.

The responsibility for gathering all required information from the foreign employer will remain with the member who will submit it to CalSTRS. CalSTRS will create a process for administering the purchase of foreign service credit, including providing forms in multiple languages and other reasonable steps to overcome language barriers.

Because CalSTRS cannot know what types of data are maintained by foreign employers, especially in less-developed countries, it must establish criteria for verifying foreign employment. Therefore, if the member cannot obtain verifiable records of foreign employment, the service will not be eligible for purchase.

Rollover Distributions

This proposal removes the language that currently expressly prohibits domestic partners from rolling over a benefit distribution. Because the Federal Pension Protection Act of 2006 now allows for all beneficiaries to rollover a benefit distribution whether or not they are spouses, CalSTRS must amend its law to remain consistent.

FISCAL IMPACT

Program Costs/Savings: Any costs associated with increased purchases of permissive out-of-state service will at best be the contributions paid by purchasing members.

Administrative Costs/Savings: Unknown but probably not substantial.

ARGUMENTS

Pro:

- Allows DB members to receive a retirement benefit for all of their “public” teaching service;
- Equalizes treatment of registered domestic partners with any other person, whether married or not, for the purposes of benefit distributions;
- Allows pertinent parts of the Federal Pension Protection Act of 2006 to be enacted.

Con:

- Increases the potential liabilities of the State Teachers’ Retirement Plan if investment returns fall below assumed rates over long periods.

LEGISLATIVE STAFF CONTACT

Will Turner

Legislative Analyst

(916)229-4702

wturner@calstrs.com

Jennifer Baker

Director of Governmental Affairs and Program Analysis

(916)229-3866

jbaker@calstrs.com