

INITIAL STATEMENT OF REASONS

Problem Statement

The Teachers' Retirement Board ("board") has exclusive authority to administer the California State Teachers' Retirement System ("CalSTRS") under Article XVI, section 17 of the California Constitution. In addition, California Education Code Section 22207 authorizes the board to perform any acts necessary for the administration of CalSTRS and the State Teachers' Retirement Plan in carrying into effect the provisions of the law. Education Code Section 22305 provides that any rules and regulations adopted by the board have the force and effect of law. This regulatory proposal is consistent with the board's fiduciary responsibility to the members, participants and beneficiaries of the system.

CalSTRS administers a hybrid retirement system that includes the Defined Benefit Program (a defined benefit plan), the Defined Benefit Supplement Program (a cash balance plan) and Pension2 (a voluntary defined contribution plan). These regulations deal exclusively with the Defined Benefit Program and the Defined Benefit Supplement Program.

Employers and employees are required by the Teachers' Retirement Law (Education Code Section 22000, et seq.) to contribute a certain percentage of the creditable compensation paid to the employee to CalSTRS. These contributions are credited to either the Defined Benefit Program or the Defined Benefit Supplement Program. Both programs provide a benefit upon retirement, but they are calculated and distributed differently.

The benefit provided by the Defined Benefit Supplement (DBS) Program is comprised of the contributions that were credited to the DBS account and interest on those contributions. Contributions are made to the DBS account either through direct reporting of certain types of compensation by the employer, or by allocation by CalSTRS of eligible contributions that were first remitted to the Defined Benefit (DB) Program. The contributions plus interest are then provided in a lump sum or as an annuity payable over a set number of years, a lifetime or multiple lifetimes.

In contrast, the DB Program provides a lifetime benefit. The service retirement benefit paid by the DB Program is based on a formula:

$$\text{Age Factor} \times \text{Service Credit} \times \text{Final Compensation}$$

The age factor is a statutory number related to the age of the member at retirement. The maximum age factor is 2.4 percent. Service credit is equal to the ratio of the creditable compensation actually paid to a member to the creditable compensation that the member would be paid for working in that position full time. The maximum amount of service credit a member can earn in a school year is 1.000; although there is no limit to the amount of service credit a member can earn over the course of a career, the amount is largely limited by the length of that career. The final compensation calculation is based

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on the highest compensation that is creditable to the DB Program that the member would be paid for working in that position on a full-time basis for a period of time (12 months or three consecutive years, depending on the number of years of service). The compensation earnable by those with a membership date on or after July 1, 1996, is limited by the annual limit prescribed by Section 401(a)(17) of Title 26 of the United States Code. However, for many members the final compensation amount does not have a statutory ceiling. As long as the compensation is creditable to the DB Program, it can be used in determining the final compensation amount. Consequently, the determination of creditable compensation is a very important component of the DB Program benefit.

Under the Education Code, only compensation that is paid in cash by an employer to all persons in the same class of employees for performing creditable service is creditable compensation. These terms are further defined by the Education Code and compensation that does not meet all of these elements is noncreditable compensation. Creditable compensation must be reported to CalSTRS, and contributions must be paid to CalSTRS for all creditable compensation. As explained above, the contributions will be credited to either the DB Program or the DBS Program. The Education Code dictates whether the contributions go to the DB or the DBS.

Consequently, compensation fits into one of three basic categories:

1. Noncreditable. This type of compensation is not reportable to CalSTRS, and no CalSTRS retirement benefits are earned from noncreditable compensation.
2. Creditable to the DB Program. This includes most cash compensation, such as salary, paid to the entire class of employees.
3. Creditable to the DBS Program. This includes non-recurring pay, inconsistent pay increases and contributions for service in excess of one year. The compensation for which contributions are credited to the DBS Program does not affect DB Program service credit or final compensation.

Over the years, employers have requested guidance in applying provisions of the Education Code to specific situations. Due to the variety of ways compensation is structured by employers, it has become difficult to ensure consistent and uniform reporting of creditable compensation without providing more clarity and direction than currently exists in the statute. CalSTRS audits employers for compliance with the reporting requirements, and non-compliant reporting must be corrected by the employer. Last year, through employer audits, CalSTRS took action to correct over \$275,000 in active member contributions and identified \$1.4 million in overpaid benefits to retirees due to errors in reporting.

The regulations proposed in this rulemaking action clarify and make specific the Education Code as it relates to classes of employees, creditable compensation and the appropriate crediting of contributions to either the DB Program or the DBS Program. Existing state regulations contain no overlapping provisions. Thus, the proposed regulations are compatible with existing state regulations.

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Education Code Section 22112.5 defines a class of employees as a number of employees considered as a group because they are employed to perform similar duties, are employed in the same type of program or share other similarities related to the nature of the work being performed. However, the terms used in the statute, “similar duties” and “same type of program,” are not defined. The regulations proposed in this rulemaking action would promote consistent understanding of those terms by clarifying them through definition. The regulations would additionally specify prohibited classes of employees.

Education Code Section 22119.2 defines creditable and noncreditable compensation. It contains terms, including “salary,” “remuneration that is paid in addition to salary,” “fringe benefits,” “expenses paid or reimbursed by an employer” and “not deducted from the member’s salary,” that are not defined in the statute, yet must be understood in order to comply with the statute.

The regulations proposed in this rulemaking action would define and clarify those terms by describing identifying characteristics of each type of compensation to promote consistent understanding and application of each term.

Education Code Section 22905 describes the allocation of contributions to the DB and DBS accounts. The statute contains the phrase “compensation that is paid for a limited number of times as specified by law, a collective bargaining agreement, or an employment agreement.” This phrase is not defined in the statute.

The regulations proposed in this rulemaking action would define and clarify “compensation that is paid for a limited number of times,” providing specific guidance on payments from state Lottery proceeds and parity pay, and describing identifying characteristics of compensation that is paid a limited number of times.

The language referenced in this document and the text of the regulations reflects the Education Code as of January 1, 2014, including changes resulting from Chapter 559, Statutes of 2013. The language of the Education Code in 2013, while still in place at the time the Notice of Proposed Rulemaking is to be published, will no longer be current once these regulations become effective.

Benefits Anticipated

Anticipated benefits of these regulations include:

- Consistent, fair and equitable reporting of the compensation used for retirement purposes of California educators by all employers.
- Clear guidance for reportable compensation, thereby reducing errors and the resulting penalties payable by CalSTRS employers.
- Transparent evaluation of consistency and allocation of accounts by CalSTRS.

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- Reduced incidences and opportunities for manipulation of retirement compensation through late career contract changes and pay increases (“spiking” of salary to increase retirement benefits).
- Improved accuracy of benefit payments to members, with less need for postretirement adjustments.
- Broad and consistent application of the statutory principles that support the integrity of the retirement fund: “consistent treatment of compensation throughout a member’s career, consistent treatment of compensation among an entire class of employees, consistent treatment of compensation for the position, preventing adverse selection, and excluding from compensation earnable remuneration that is paid to enhance a member’s benefits.”

Purpose and Rationale

The proposed regulations do the following:

1. Section 27200. Members affected by this chapter.

This section specifies that the new Chapter 2 applies to members who are not subject to the California Public Employees’ Pension Reform Act of 2013 (PEPRA). Members who are subject to PEPRA are referred to as “CalSTRS 2% at 62” members, and they are not affected by these regulations. Affected members are under the benefit structure referred to as “CalSTRS 2% at 60,” for those members who were first hired before January 1, 2013.

Different rules apply to creditable compensation under the different benefit structures currently administered by CalSTRS. Though parts of the Education Code that are clarified by these regulations apply to both benefit structures, many of the Education Code provisions referenced in the regulations apply exclusively to 2% at 60 members.

Rather than specifying section-by-section which rules relate to both benefit structures, the entire chapter is specific to 2% at 60 members. Any future regulations that relate to members who are subject to PEPRA (“CalSTRS 2% at 62” members) will incorporate the provisions that are shared by both benefit structures as appropriate.

Employers have specifically requested guidance as to reporting compensation for 2% at 60 members. By devoting Chapter 2 exclusively to that benefit structure, employers will enjoy greater ease of use of, and compliance with, the regulations.

2. Section 27201. Effective date.

This section specifies that the provisions of this chapter are effective with service performed on or after July 1, 2014 (or a later date, depending on the earliest effective date allowed following the rulemaking process).

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These regulations clarify the Teachers' Retirement Law and provide specific guidance on implementing certain requirements, such as creating a class of employees whose members have two or more job duties in combination, and reporting special compensation only in situations in which no additional service is performed.

Providing an effective date will aid employers in implementing any changes to their current approach, which may differ from the guidance provided herein.

3. Section 27300. Basis of establishment of a class of employees.

This section provides definitions for terms used in the Education Code to define "class of employees" to ensure that employers and CalSTRS share a consistent understanding of what constitutes a class for reporting purposes. The manner in which compensation is paid to a class of employees is one of the bases for determining creditability of compensation. The regulation defines and clarifies the terms that describe the criteria that are used to establish a class.

"Job duties" refers to a complete listing of ten specific categories of creditable service activities in the Education Code. A finite and comprehensive list of specific creditable activities is described in Education Code Section 22119.5. Every creditable service activity that is reportable for CalSTRS purposes is covered under subdivisions (a) and (b) of that section. This regulation clarifies that "similar duties" are considered those duties grouped under each of the paragraphs under subdivision (a), as well as subdivision (b).

Similarly, "program" is defined as any educational program established pursuant to state or federal law. This comprises every program that is funded in public education and recognizes that programs established pursuant to state or federal education policy may have distinct duties, responsibilities and requirements.

The Education Code allows for a class of one to be established, which has the potential to lead to special treatment of compensation on an individual or selective basis. The Education Code provides that a class of one must be in "common use"; these regulations make that provision specific by requiring that common use of job duties in a class by at least two other employers must be demonstrated by the employer. This provides employers with specific criteria to assess "common use."

Classes of employees are established at the employer level, and are not generally reviewed by CalSTRS unless the compensation comes to staff attention for review. The onus is then on the employer to correct the established class and any attendant compensation that was reported in error as a result.

Specific guidance as to how to determine whether job duties are "similar" or whether a program is of the "same type" provides employers with the tools to create valid classes of employees. The criteria are finite, limiting the potential for employers to establish an invalid class of employees subject to disapproval by CalSTRS.

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4. Section 27301. Prohibited classes of employees.

This section specifies prohibited classes of employees. The Education Code provides that “the board shall have the right to override the determination by an employer as to whether or not a group or an individual constitutes a ‘class of employees.’” This section lists distinguishing qualities in the establishment of a class of employees that are prohibited by the board because they create opportunities to manipulate the creditability of compensation for that group. Explicitly prohibiting establishment of a class of employees based on these distinguishing qualities provides employers information they need to ensure they do not establish a class that is subject to being overridden by CalSTRS.

A class of employees distinguished by a retirement program or benefit formula or that is age or service biased is prohibited regardless of whether the class meets the criteria in section 23700. A class of employees distinguished by the characterization of compensation of its members is acceptable only if the class members are employed in similar job duties or a separate program. A class of employees distinguished by an option or requirement to work a longer day, or more days per year, is acceptable only if the class members are employed in a separate program.

As an example of a prohibited class based on the length of the work day, CalSTRS has discovered more than one instance in which an employer established a separate class of employees for teachers who taught an additional period each day, beyond the regular work day. The only difference in the job duties performed by this group and the other teachers employed by that same employer was the additional period added to the work day. By establishing a separate class of employees, those teachers had a greater full-time requirement and compensation earnable, and were able to have higher salaries reported to the DB Program. Under the TRL, the extra period should have been reported as an additional assignment and the contributions on earnings above the compensation earnable should have been credited to the DBS account.

5. Section 27400. Salary.

Subdivision (a)

This subdivision describes requirements of salary, listing the qualities that salary must possess.

Written bargaining unit contracts are negotiated at the employer level, and administrator-level employment agreements are individually negotiated. There is, therefore, a broad range of ways in which salary is defined and described by over 1,600 CalSTRS employers. For example, an agreement used by one employer might include payments for years of experience, educational attainment or other achievements as part of the salary schedule. Another employer may pay a flat stipend to employees for the same purpose. The manner in which compensation is structured, described and paid, and not just its purpose, is important in assessing its creditability for CalSTRS reporting purposes.

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Each of the criteria listed differentiate salary from other types of payments as follows:

- *Paid in cash by an employer to an employee for the performance of creditable service:* This differentiates salary from compensation that is not paid in cash, such as an employer-provided vehicle. The vehicle is taxable income for IRS purposes. This requirement provides an identifying feature employers use to distinguish “salary” from “taxable income.”
- *Explicitly characterized as salary on a contract, salary schedule or employment agreement:* This requirement specifies that any pay that meets the other requirements listed is not salary unless it is explicitly described as such.
- *Used as a basis for future pay increases:* This criteria is included to differentiate salary from other types of pay, such as off-schedule payments that are not the basis of future pay increases.
- *Paid without a requirement by the employer for proof of expenditure:* This criterion is included to differentiate between salary and a reimbursement.

By defining salary in terms of qualities it possesses, employers and CalSTRS can easily recognize payments that are and are not salary.

Subdivisions (b) and (c)

Subdivisions (b) and (c) specify that an employer must establish a full-time requirement and compensation earnable for all assignments in which an employee will earn salary and describe how to apply this requirement when the employer provides release time, also called “reassigned time.”

CalSTRS retirement benefits are based, in part, on service credit earned. However, employers may also report “special compensation,” which is not associated with earning service credit.

Currently, many employers report special compensation when a member is released from his or her regular job to perform creditable service in another assignment. In these instances, the member is performing an activity that meets the definition of creditable service but is not receiving service credit for the activity. Instead, the employer is reporting the service credit that was not actually performed for the primary assignment. This is essentially an administrative workaround for employers that functions on a premise that the service performed while on assignment during release time is equivalent to the assignment from which the employee is released. The practice is not specified or supported in law.

The regulations instead provide that employers have the option of creating a separate class of employees for positions that include additional assignments, or they could keep the classes of employees separate and report the compensation for the activities as two separate assignments, each with its own compensation earnable. In both options, the member would accrue service credit.

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CalSTRS heard from employers that establishing a separate full-time requirement and compensation earnable would be challenging for certain assignments, such as coaching, when time spent at the assignment is not specifically monitored or predictable and pay is a flat rate for the completion of the assignment. Nonetheless, employers are familiar with establishing these bases for CalPERS reporting requirements and for part-time assignments under the federal Patient Protection and Affordable Care Act. CalSTRS considered providing specific guidance to employers who expressed interest in a formula to create such a base. However, in order to avoid potential conflicts with guidance issued by CalPERS and the federal government, and in line with current autonomy employers possess in establishing these bases, CalSTRS opted not to prescribe a mechanism for determining a time base to employers outside of what is already provided in the Education Code.

Employers who do not offer release time currently have to provide a full-time requirement for part-time positions; therefore, they already comply with this provision. For employers who do not, establishing a separate class is a straightforward alternative and is specifically allowed in the regulations language. The option of creating a separate class of employees was highlighted specifically in the regulations in order to ensure that option is clear to employers who informed CalSTRS that it would be difficult to establish a separate full-time requirement and compensation earnable for a specific assignment.

In response to concerns expressed by some employers that establishing separate time bases for each assignment would necessitate the creation of hundreds of separate salary schedules, CalSTRS did further research and consulted experts in bargaining unit negotiations. Staff found that creating a separate class would be an alternative that would not necessarily require an entirely separate salary schedule. For example, the difference in pay between members of the class of “teacher” and members of a class of “teacher plus [additional duty]” could be included on the regular “teacher” salary schedule as a footnote indicating that the salary for the separate class will earn an additional percentage or flat amount.

This specific approach is necessary because one of the consequences of allowing employers to report creditable service with flat dollar amounts as special compensation is that the compensation paid increases members’ compensation earnable and could inflate final compensation. In addition, allowing for creditable service to be reported without accruing service credit is not supported in the Teachers’ Retirement Law.

By requiring that employers establish a full-time requirement and compensation earnable for assignments that earn salary, CalSTRS ensures that employers will consistently and appropriately report salary concurrent with its associated service.

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Subdivision (d)

This subdivision specifies that compensation that is permanently restructured as salary is salary, effective on the date of the restructure. It additionally describes the circumstances under which CalSTRS will presume a restructure is not permanent.

A restructure of compensation can occur when a bargaining unit contract or employment agreement is renegotiated to change the nature of compensation. For example, an employer reduces support for health benefits and provides an across-the-board salary increase acknowledging the reduction in benefits. When this occurs, the resulting compensation generally is creditable in whatever manner its new nature dictates.

Prior to the mid-1990's, restructured compensation was not creditable to CalSTRS. If compensation was restructured as described in the example above, CalSTRS would view the salary increase as retaining its original nature as noncreditable employer-sponsored health benefits. However, following study by staff and as documented in a letter to CalSTRS dated March 25, 1996, the consulting actuary advised that a permanent restructure of compensation would not have an adverse impact to the fund. The consulting actuary further advised that employers may react to changing tax laws or attempt to contain costs by implementing permanent restructures and that CalSTRS should acknowledge that employers do not necessarily want pensions reduced as a result, and the board supported the new approach.

However, when restructuring takes place on a temporary basis for a select individual or group during the years just prior to retirement, it can result in an inflated final compensation that is not in line with the contributions remitted to CalSTRS. When compensation is not treated consistently throughout a member's career, under law, CalSTRS must determine how much of the compensation is inconsistent, and that amount is diverted to the member's DBS account (detailed in Article 5).

These regulations specify conditions that will result in a finding that a restructure is not permanent, ensuring consistent understanding between CalSTRS, employers and other stakeholders concerning the creditability of compensation that results from a negotiation restructuring compensation.

Subdivision (e)

This subdivision clarifies Education Code Section 22119.2, which states (emphasis added):

“Creditable compensation shall include: [...] Amounts that are deducted from a member's *remuneration*, including, but not limited to, deductions for participation in a deferred compensation plan; deductions to purchase an annuity contract, tax-deferred retirement plan, or insurance program; and contributions to a plan that meets the requirements of Section 125, 401(a), 401(k), 403(b), 457(b), or 457(f) of Title 26 of the United States Code.”

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“Creditable compensation does not mean and shall not include: [The deductions listed above] when the cost is covered by an employer and is not deducted from a member’s *salary*.”

The Education Code clearly states that amounts deducted from salary for the items listed above are creditable as salary. This section defines and clarifies “deducted from a member’s remuneration” to mean deductions made at a member’s discretion. This section is also added explicitly to the regulations in order to differentiate amounts deducted from a member’s *salary* from amounts that may be deducted from a member’s *compensation paid in addition to salary*, or deducted from anything other than salary, which are noncreditable as described in law and further clarified under Section 27500 of the regulations.

Explicitly describing the circumstance under which these deductions are creditable will promote consistent understanding, reduce related audit findings and improve the rate of correct reporting of these payments.

Subdivision (f)

This subdivision clarifies creditability of compensation in the event that the employment agreement identifies something as both salary and a fringe benefit or expense. This subdivision makes it clear that if an item of compensation meets both the definition of salary and the definition of fringe benefit or expense, it is salary. CalSTRS has reviewed employment agreements that contain this ambiguity. Because of the variety of ways contracts and agreements are drawn, it is necessary to establish this rule in regards to compensation that could meet the criteria of both salary and a fringe benefit or expense.

6. Section 27401. Remuneration that is paid in addition to salary.

Subdivision (a)

This subdivision clarifies the phrase, “remuneration that is paid in addition to salary,” one of the components of creditable compensation as defined in Education Code Section 22119.2. This subdivision describes the qualities and requirements this type of remuneration must possess in order to be creditable compensation, reportable to CalSTRS.

Remuneration in addition to salary may be creditable to the DB Program or the DBS account, depending on the way in which it is paid. Subdivision (a) first describes that compensation in addition to salary must be paid in cash in accordance with a publicly available written contractual agreement. Reported compensation must be verifiable by CalSTRS during an investigation or audit. Subdivision (a) then restates a requirement of the Education Code, that remuneration in addition to salary must be paid to all persons in a class of employees in the same dollar amount, the same percentage of salary or the same percentage of the amount being distributed. Staff deemed this restatement of the law necessary in the context of this subdivision, which clearly lays

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out the other qualities needed for creditability of this type of compensation, for ease of use of the regulations.

Paragraph (1) of subdivision (a) describes six categories of qualifications or requirements that an individual could meet to be paid remuneration in addition to salary that is not associated with the performance of additional service. Paragraph (2) identifies compensation that is contingent upon the availability of funds as an additional category of remuneration in addition to salary. Each of these categories was distilled from the following sources:

1. California Department of Education. The Department of Education conducts a voluntary survey of K-12 employers each year and the results are posted on their website. From the 2011-12 dataset, staff pulled every narrative description of “bonus” payments offered by employers and categorized those that are creditable to CalSTRS by broad purpose. Staff determined that each pay type was due to one of the following:
 - Possession or attainment of a certificate, license, special credential or advanced degree.
 - Career or service longevity.
 - Hiring, transfer or retirement.
 - Employment in a position that is hazardous or difficult to staff.
 - Achievement of a performance benchmark.
2. California Community Colleges Chancellor's Office. The Chancellor's website provides information regarding programs offered by community colleges. Most are associated with the performance of additional service and, therefore, are classified as salary. Those that were not necessarily associated with additional service were validated to ensure all of them fit under the categories already identified through the California Department of Education research.

The only remuneration in addition to salary that would be paid for an attainment unique to community college employers identified by CalSTRS was compensation to achieve compensation parity between part-time and full-time faculty of California community colleges for similar work, as funded pursuant to the Budget Act. This type of payment falls under paragraph (2), “Compensation that is paid contingent upon availability of funds.”

3. Feedback from employers. In early listening sessions with employers, CalSTRS solicited employers for common types of special compensation that they pay. One broad category identified was compensation paid contingent upon availability of funds, such as Lottery pay, parity pay and off-schedule salary payments. These payments have historically been reported as creditable compensation to CalSTRS, and this category is included in paragraph (2).

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4. Feedback from member advocates. Member advocates noted that additional pay associated with having more students in the classroom was not covered under the current creditable categories already identified. This type of pay is creditable, and so an additional category was added to subdivision (a):
 - Employment in an assignment in which the number of students enrolled exceeds the contractual amount.

Some stakeholders requested that CalSTRS provide an exhaustive list of specific types of compensation identified by CalSTRS as creditable. CalSTRS investigated this and determined that the pay types available to CalSTRS membership were too extensive to provide an exhaustive list (more than 400 bonuses with unique titles are named on the CDE's J-90 response file). In addition, as mentioned previously, the purpose of a payment is only one component of establishing creditability. The manner in which pay is distributed to an entire class and the nature of the pay, whether ongoing or paid a limited number of times, is as essential in determining creditability. Therefore, CalSTRS determined that "remuneration that is paid in addition to salary" would be best clarified, similar to "salary" in Section 27400, in terms of qualities that employers and CalSTRS can readily and consistently recognize. CalSTRS anticipates that this clarification will promote consistent understanding and improved reporting with reduced errors by employers.

Subdivision (b)

This subdivision specifies that compensation that is permanently restructured as remuneration that is paid in addition to salary is remuneration that is paid in addition to salary, effective on the date of the restructure. It additionally describes the circumstances under which CalSTRS will presume a restructure is not permanent.

A restructure of compensation can occur when a bargaining unit contract or employment agreement is renegotiated to change the nature of compensation. For example, an employer changes a doctoral degree increase that was previously included as a step on the salary schedule into a separate non-salary flat amount paid to employees who meet the qualification. When this occurs, the resulting compensation generally is creditable in whatever manner its new nature dictates.

Staff could not identify a theoretical circumstance in which a payment that is not creditable as provided in these regulations could be restructured as remuneration in addition to salary and, therefore, be creditable. However, one type of creditable compensation (salary) could be restructured into another type of creditable compensation (remuneration that is paid in addition to salary). Although such a change would not appear to have any adverse impact for funding purposes, cognizant of the fact that that unanticipated types of restructuring by employers could occur in the future, CalSTRS has determined it would be prudent to clarify that the same rules apply to any type of restructure involving creditable compensation.

A discussion of the purpose, rationale and anticipated benefits of the language in this subdivision—which is substantially similar language to the restructure language

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related to “salary”—is detailed under the discussion of subdivision (d) of Section 27400.

Subdivision (c)

This subdivision describes certain types of compensation that are specifically not included in the definition of remuneration that is paid in addition to salary. A summary description of each of these compensation types and the rationale for specifically excluding them follows:

- *Cash paid by an employer to an employee who receives cash in lieu of a fringe benefit or expense.* For example, an employer might provide that a member who elects not to receive employer-paid health benefits instead receives a monthly amount in cash from the employer. Cash in lieu is paid to replace a fringe benefit or expense paid by an employer and is, therefore, not creditable. However, since it is paid in cash in equal measure to members of a class of employees who qualify to receive it, similar to the criteria for assessing creditability described in subdivision (a), CalSTRS determined that specific guidance to employers, enabling them to distinguish this type of non-salary pay as noncreditable compensation, is likely to promote accurate reporting.
- *Cash paid by an employer on behalf of an employee for a fringe benefit, expense or reimbursement.* This type of payment is not received by the employee as cash. However, some types of fringe benefits or expenses are taxable income for IRS purposes. This requirement clarifies for employers that although such payments may be reportable for tax purposes, they are not reportable to CalSTRS.
- *Cash paid by an employer to an employee that is the remainder from money allocated for fringe benefits or expenses.* Similar to cash in lieu, as described in the first bullet, this provision is specifically included for the same reason and with the same anticipated benefit.

7. Section 27500. Amounts not deducted from a member’s salary.

This section clarifies Education Code Section 22119.2, which states (emphasis added):

“Creditable compensation shall include:[...] Amounts that are deducted from a member’s *remuneration*, including, but not limited to, deductions for participation in a deferred compensation plan; deductions to purchase an annuity contract, tax-deferred retirement plan, or insurance program; and contributions to a plan that meets the requirements of Section 125, 401(a), 401(k), 403(b), 457(b), or 457(f) of Title 26 of the United States Code.”

“Creditable compensation does not mean and shall not include: [The deductions listed above] when the cost is covered by an employer and is not deducted from a member’s *salary*.”

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The Education Code clearly states that deductions for the items listed above are not creditable if they are not deducted from salary. In Section 27400, these regulations clarify that amounts deducted from salary at the member's discretion are salary and, therefore, creditable. This section further clarifies that compensation paid in addition to salary that is contingent upon the purchase of any of these items is not creditable. CalSTRS determined it was necessary to add this section explicitly to prevent a pass-through or workaround in which the member is required to use certain amounts to purchase the items, even if the items are paid through a deduction from the member's remuneration.

Explicitly describing the circumstance under which these deductions are noncreditable will promote consistent understanding, reduce related audit findings and improve the rate of correct reporting of these payments.

8. Section 27501. Fringe benefit.

This section provides a definition interpreting the term "fringe benefit" as used in Education Code Section 22119.2. The term is not defined specifically in the Education Code. In the past, CalSTRS has directed employers to use criteria similar to that used by the Internal Revenue Service for an accountable plan (a taxable cash payment plan) to determine whether something was a fringe benefit or not. However, this is not appropriate because the IRS defines a fringe benefit as "a form of pay . . . in addition to stated pay" whereas CalSTRS differentiates between "remuneration in addition to salary", which is creditable, and "fringe benefits", which are noncreditable (IRS' 2013 *Federal, State, and Local Governments Fringe Benefit Guide*). Therefore, just because something is or is not a fringe benefit to the IRS has no bearing on whether something is a fringe benefit for purposes of the accurate reporting of compensation to CalSTRS.

The regulations clarify "fringe benefit" to assist in consistent reporting to CalSTRS. Following is an explanation of the three types of compensation described in the regulations as constituting a fringe benefit, and a discussion of the rationale for each follows:

- *A good or service for which the cost is paid to a third party or otherwise covered by the employer.* A good or service paid for by the employer does not meet the definition of compensation because it is not paid in cash to the employee. However, this clarification is needed because of the possible misconception that the "value" of the good or service is equivalent to a cash payment. This clarifies that if what the employee receives is a good or service, it is a fringe benefit.
- *Compensation allocated to an employee to cover a personal or business expense that could otherwise be provided in the form of a good or service.* In this instance, the employee receives cash that is earmarked for a purpose that could otherwise be provided by the employer as described above; for example, a car allowance is provided instead of an employer-provided vehicle. Such an allowance serves the same purpose as the fringe benefit it replaces.

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- *Cash in lieu of, or cash remaining from, a good or service.* An example of this is when an employer provides support for health benefits up to a certain dollar amount, and the employee declines coverage, or else selects a plan that costs less. If the employer provides cash compensation to the employee as a result, it retains its essential nature as payment for a good or service.

9. Section 27502. Expenses paid or reimbursed by an employer.

Subdivision (a)

This subdivision clarifies expenses paid by an employer by describing specific types of compensation that employers and CalSTRS can use to readily and consistently identify expenses paid by an employer. A summary of those types of compensation and a discussion of the rationale behind each follows.

- *Compensation allocated to an employee to cover a cost the employee is expected to incur in the course of performing duties for that employer, which could otherwise be covered by the employer or provided in the form of a reimbursement of the cost.* Similar to the example above under “fringe benefit”, one example of this is a car allowance. The car allowance could have otherwise been provided as a reimbursement of the individual’s actual transportation expenses. Such an allowance serves the same purpose as the expense paid by an employer that it replaces.
- *Cash paid directly to a third party or a cost that is otherwise covered by the employer.* In this instance, the compensation is not paid in cash, such as an employer-provided vehicle. Compensation that is not paid in cash is not creditable to CalSTRS under the definition of “salary” and “remuneration that is paid in addition to salary.” This paragraph clarifies that the noncreditable compensation, when paid to a third party to cover a cost, is an expense paid by the employer.
- *Cash in lieu of, or cash remaining from, compensation allocated to cover a cost.* An example of this is when an employer will reimburse an employee for up to a certain amount of substantiated expenses and then provides the employee the entire amount even if the receipts are for less than the entire amount. Another example is if the employer provides a car and the employee declines it. If the employer provides cash compensation to the employee as a result, it retains its nature as an expense paid by the employer.

Subdivision (b)

This subdivision clarifies expenses reimbursed by an employer. The description is based upon the Internal Revenue Service’s three criteria for an accountable reimbursement plan. Such payments are not taxable and are not reportable to the IRS or to CalSTRS. CalSTRS determined that using existing criteria developed by the Internal Revenue Service would aid employers in recognizing these types of payments. However, CalSTRS opted not to directly reference the applicable Internal Revenue Code. The rationale behind that decision was that cross-referencing would

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put the system at risk to monitor and interpret federal rules outside its control. Instead, CalSTRS is establishing these criteria based on the spirit of current guidance from the IRS and will retain the flexibility to retain these criteria even if the IRS should change its rules.

10. Section 27600. Consistent treatment of compensation.

This section clarifies and makes specific subdivisions (b) and (f) of Education Code Section 22119.2.

Subdivision (a)

CalSTRS has discretion to determine the appropriate crediting of contributions between the DB Program and the DBS account according to the principles specified in Section 22119.2 of the Education Code. These regulations define what considerations CalSTRS uses to assess whether compensation is consistent with those principles that support the integrity of the retirement fund:

- Consistent treatment of compensation throughout a member's career,
- Consistent treatment of compensation among an entire class of employees,
- Consistent treatment of compensation for the position,
- Preventing adverse selection, and
- Excluding from compensation earnable remuneration that is paid to enhance a member's benefits.

CalSTRS reviews increases in creditable compensation that exceed certain system-defined thresholds to determine whether the increase is in line with the principles above. These regulations describe evidence that employers can present to CalSTRS to demonstrate that a compensation increase is consistent. Acceptable evidence would demonstrate that the pay increase was due to any of the following reasons, summarized below, including a discussion of the rationale for each:

- *A restructure of compensation that meets the criteria described in subdivision (d) of Section 27400 or subdivision (b) of Section 27401.* This clarifies that a permanent restructure of compensation is a valid rationale for a salary increase. While a compensation restructure late in a member's career is generally unfavorable from a funding perspective, a permanent change to an employer's business practice that coincides with the end of a member's career but results in a permanent increase in creditable compensation for that position going forward is acceptable from an actuarial perspective, as described in the March 25, 1996, letter from CalSTRS consulting actuary.
- *A salary deferral due to a reduction in school funds.* It is a reality of education funding that fluctuations in budget can lead to temporary salary stagnation for educators and administrators. Clear documentation that an increase is the result of prior years' salary that was deferred in response to external budgetary forces would adequately demonstrate that pay was consistent.
- *A commensurate percentage increase in compensation earnable for other employees performing similar job duties for the same employer.* If a pay

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increase is consistent with that offered to other employees performing similar job duties for that employer, then that demonstrates that the increase was not offered to enhance the member's benefits but was instead an action taken on a broader scale by the employer.

- *A change in duties required of the employee that is incorporated in the first contract for the immediate successor to the position.* If a pay increase is the result of additional duties required of a position, the pay increase is consistent so long as the expectation continues for the successor to the position. Requiring the change of duties to remain for the successor demonstrates a change in the employer's business practice, rather than a temporary assignment that is given to enhance that member's benefits.
- *An increase in responsibility of the employee that is incorporated in the first contract for the immediate successor to the position.* Similar to the previous bullet, if a pay increase is the result of increased responsibility required of a position, the pay increase is consistent so long as expectation continues for the successor to the position. Requiring the added responsibilities to remain for the successor demonstrates a change in the employer's business practice, rather than a temporary assignment that is given to enhance that member's benefits.
- *Attainment of an educational or performance benchmark.* If a pay increase is the result of an educational or performance benchmark that would be paid regardless of proximity to retirement, then that demonstrates that the pay increase is not paid to enhance that member's benefits.
- *An increase that establishes pay parity (list of situations follows in regulation text).* The listing includes commensurate compensation earnable and compensation increases that would demonstrate that the increase was not offered to enhance the member's benefits but was instead an action taken on a broader scale by the employer.
- *A commensurate compensation earnable for the immediate successor.* A commensurate compensation earnable for the immediate successor demonstrates that the increase in compensation was a permanent change in the employer's business practice, rather than a temporary measure to enhance the member's benefits.
- *A commensurate compensation earnable for the immediate predecessor.* A commensurate compensation earnable for the immediate predecessor demonstrates that the increase in compensation was not offered to enhance the member's benefits but was instead an action taken on a broader scale by the employer.
- *More education or experience than the immediate predecessor.* If compensation is higher overall than the previous holder of a position and that compensation is the result of additional education or experience that would be rewarded with an increase in pay regardless of proximity to retirement, then that demonstrates that the compensation differential is not paid to enhance that member's benefits.

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CalSTRS received input from some stakeholders who requested that CalSTRS define specific thresholds for reviews of consistent compensation, such as providing a defined time frame that CalSTRS would look at prior to retirement (and any increases prior to that time would not be subject to review), or defining in numerical terms the thresholds above which compensation would be subject to review. CalSTRS considered this input and determined that, while promulgating these specific thresholds would increase transparency, it would also subject the system to risk by giving an improper advantage to anyone who might wish to circumvent those thresholds. Supporting this determination and in line with its fiduciary responsibility, CalSTRS is exercising its express exemption from establishing audit and investigative thresholds pursuant to subdivision (e) of Government Code Section 11340.9.

Making these criteria, which employers can utilize to show that a compensation increase is not inconsistent, specific through regulation provides CalSTRS and employers the tools to implement a consistent and transparent assessment of whether compensation is creditable to the DB Program or subject to allocation to the DBS account.

Subdivision (b)

This subdivision clarifies a presumption by CalSTRS that if a successor's pay is less than a member's and the reduction is attributable to less education or experience, compensation is presumed to be consistent. This clarification is needed in addition to the criteria listed in subdivision (a) because successor pay is used to assess consistent treatment of compensation for a position, not consistent treatment throughout a member's career. If, in the course of the assessment, successor pay is less due to this factor and would be paid regardless of proximity to retirement, then that demonstrates that the compensation differential is not paid to enhance that member's benefits.

Subdivision (c)

This subdivision clarifies a presumption by CalSTRS that in assessing consistency of an increase affecting that member's final compensation calculation that is not due to any of the circumstances in subdivision (a), the increase is presumed to be inconsistent. This is a reverse statement of subdivision (a) and is necessary to clarify what CalSTRS will do if an employer does not demonstrate that a compensation increase is due to any of the factors listed. CalSTRS presumption of inconsistency is the first step in the process of appropriate crediting of contributions.

Subdivision (d)

This subdivision clarifies CalSTRS presumption of inconsistent treatment if a specific pattern of duties or responsibilities is being assigned by an employer to employees during the final compensation period.

This provision is included in recognition that the other consistency factors described in this section, which focus on consistent treatment of a member's compensation and consistent treatment of a position, do not otherwise address this specific scenario.

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This scenario, in which an employer could establish a high-paying title or duty and then assign it selectively during the final compensation period, would be an example of adverse selection, and compensation resulting from this type of assignment is against the principles described in the Education Code.

This subdivision gives employers tools to identify and prevent this scenario from occurring. It increases transparency by making clear that compensation resulting from an assignment that follows a pattern of being used as a vehicle to enhance a member's benefits will be subject to a presumption of inconsistency.

11. Section 27601. Appropriate crediting of contributions.

This section clarifies subdivision (f) of Education Code Section 22119.2.

Subdivision (a)

Paragraphs (1) through (3)

The first three paragraphs of subdivision (a) provide the specific formula CalSTRS will utilize when compensation is found to be inconsistent with the principles outlined in the Education Code, after a presumption is made pursuant to Section 27600 of these regulations when the inconsistency affects the member's final compensation.

Each formula applies to a specific situation and dictates the amount by which the member's compensation earnable is reduced, with the contributions on the earnings in excess of that amount allocated to the Defined Benefit Supplement account. Each formula is summarized below, along with a discussion of the rationale for each:

- *If the inconsistent treatment of compensation is the result of a restructure of compensation that is not permanent, the amount that was restructured shall be credited to the member's Defined Benefit Supplement account beginning with the effective date of the restructure.* As discussed under Sections 27400 and 27401, a nonpermanent restructure of compensation does not represent consistent treatment of compensation throughout a member's career. Any pay increase that is the result of a nonpermanent restructure is creditable to the DBS account in its entirety.
- *If any part of creditable compensation is restructured into a fringe benefit or an expense paid or reimbursed by the employer, or otherwise becomes noncreditable, that amount is not creditable compensation beginning with the effective date of the restructure.* This paragraph clarifies the noncredibility of compensation that is restructured as noncreditable. The permanency of such a restructure is irrelevant because the compensation is not creditable in either case. These regulations provide clear guidance as to restructured compensation that becomes creditable, but otherwise are silent as to restructured compensation that is not creditable. CalSTRS determined this clarification would assist employers in identifying the proper approach to

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reporting restructured compensation by providing comprehensive direction on all possible restructures.

- *If the inconsistent treatment of compensation is not attributable to a restructure, the portion of compensation affecting the member's final compensation determined to be in excess of the following thresholds is not creditable to the Defined Benefit Program.* CalSTRS identified several scenarios under which this might happen during an individual's career and determined that there was no way to apply the same formula to each scenario. A concise categorizing of three situations—an increase concurrent with a change in position, an increase that occurs in a position held between two and five years, and an inconsistent increase that occurs in a position held more than five years—required unique thresholds that would be applied during the final compensation period. A discussion of each threshold listed in the regulations follows:
 - *For inconsistent compensation increases concurrent with a change in position, the threshold is the immediate predecessor's salary increased by the average percentage increase of the compensation earnable of a representative sample of employees during the year the inconsistent compensation increase occurred.* When an individual changes position, CalSTRS determined that his or her prior salary becomes an irrelevant baseline for future increases. An inconsistent increase concurrent with a change in position would only be identified, pursuant to Section 27600, if the predecessor and successor salaries were not demonstrated to be consistent. For example, an individual earns significantly more than his or her successor or predecessor in the absence of demonstrated education and experience, or the additional pay was attributable to duties temporarily assigned to that individual but not to his or her successor. CalSTRS determined that the most appropriate baseline in this scenario is the predecessor's pay, delivering a number based on consistent treatment of a position, increased by an amount that reflects the pay increases by other employees of that employer in that year (see the following discussion of paragraph [4]).
 - *For inconsistent compensation increases for a position held between two and five years, the threshold is the member's compensation earnable for the year prior to the year in which the inconsistent increase occurred increased by the average percentage increase of the compensation earnable for a representative sample of employees during the year the inconsistent compensation increase occurred.* When an individual holds a position and an inconsistent increase is awarded during his or her tenure, CalSTRS determined that the individual's prior year salary makes the most appropriate baseline (as opposed to another individual's pay) because it already incorporates that individual's education, experience and other qualifications. A

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year-over-year inconsistent increase while in a position would only be identified, pursuant to Section 27600, if no other factors listed in that section explain the change in pay. In the absence of any other factors describing the increase, CalSTRS determined that the most appropriate baseline for an individual with a relatively short tenure in the position (less than five years) is the individual's prior year pay, delivering a number based on consistent treatment during that individual's career, increased by an amount that reflects the pay increases by other employees of that employer during that year (see the following discussion of paragraph [4]).

- *For inconsistent compensation increases for a position held five or more years, the threshold is the member's compensation earnable for the year prior to the year in which the inconsistent increase occurred, increased by the average of the compensation increases earned during the member's final five years of employment.* When an individual holds a position and an inconsistent increase is awarded during his or her tenure, CalSTRS determined that the individual's prior year salary makes the most appropriate baseline (as opposed to another individual's pay) because it already incorporates that individual's education, experience and other qualifications. A year-over-year inconsistent increase while in a position would only be identified, pursuant to Section 27600, if no other factors listed in that section explain the change in pay. This formula differs from the other two listed because it does not rely on a representative sample of other employees of that employer, and it does not restrict its averaging to the year in which the increase occurred. Instead, CalSTRS would use the average of the compensation increases earned during the final five years of employment. CalSTRS determined that the most appropriate baseline for an individual with more than five years' tenure in a position would be based on the rest of that member's career, delivering a number based on consistent treatment during that individual's career. One-fifth of the member's inconsistent increase is retained, averaged together with four adjacent years of compensation increases. CalSTRS determined five years would be an appropriate average because it smoothes the outlier year sufficiently and considers increases earned prior to the final compensation period, without being unduly long such that it would cause administrative challenges.

Paragraph (4)

To define a representative sample, CalSTRS determined that others performing similar job duties would be most appropriate to compare, since they were more likely to have been part of the same agreement or an agreement negotiated in a similar manner. Contracts between different groups (for example, classroom teachers and administrators) are negotiated separately.

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CalSTRS identified that a comparator pool of three employees, consisting of the member and two others, would be administratively feasible. Including the member as part of the comparator pool means that at least one-third of the inconsistent increase is retained by the member. CalSTRS determined that averaging the actual increase with two others would adequately smooth the outlier compensation increase to constitute consistent treatment of compensation.

CalSTRS considered using pay increases awarded to all CalSTRS-covered employees generally by the employer but discarded this approach following research into employer compensation, as some employers—particularly very small employers—year-over-year were found to show a net negative amount due primarily to staffing changes rather than actual pay increases awarded. This approach was found to be overly subject to staffing and demographic shifts that were not relevant to the intent of the allocation formula.

In cases where an individual is in a class comprised of two duties and there are no others with similar duties at that employer (an example would be a teacher/librarian who performs a half day in each component duty), CalSTRS determined that a larger comparator pool would be necessary. That comparator pool would consist of: two others performing the first duty (in the example, teachers) and two others performing the second duty (in the example, librarians). The member's increase would be averaged with each set of individual component duties.

In cases where there is nobody else at that employer performing the same duties (for example, a county superintendent), CalSTRS determined that the next closest similar duties would be used, as demonstrated by the nearest match in salary range or the nearest match in full-time requirement. These two factors are used because:

- The closest match in salary range is likely to be an individual whose duties and responsibilities are at a similar level to the member in question.
- The nearest match in full-time requirement is likely to be an individual whose duties more closely correspond to the member in question.

CalSTRS explored using pay increases earned by others with that same job title in other counties that shared similar features. With input from stakeholders, CalSTRS attempted to refine criteria to find an equitable method to use this approach but found that an equitable comparison between employers could not satisfactorily be engineered. This became more difficult as more tailored funding between employers arose as a result of the new Local Control Funding Formula included in the Governor's 2012-13 budget.

As a result of these challenges and in response to stakeholder feedback, CalSTRS determined the best approach would be to benchmark such representative samples on an individual basis and restricted to a single employer as described above.

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CalSTRS evaluated whether or not it was necessary and appropriate to include a prescriptive standard in the regulations and impose a limiting formula on the system's current flexibility in judgment provided by the Education Code. Currently, in cases of a finding of inconsistency, contributions are allocated to member's DBS accounts on a case-by-case basis. It is CalSTRS desire to provide a consistent and transparent formula to allocate contributions to members' DBS accounts in instances of inconsistency. This ensures equitable treatment of members by reducing the element of staff judgment that is unavoidable under the current process.

12. Section 27602. Compensation that is paid a limited number of times.

This section clarifies Education Code Section 22905.

Subdivision (a)

This subdivision clarifies that Lottery and parity payments are creditable to the DB Program. This specification is necessary because they are paid a limited number of times and would otherwise be creditable to the DBS account. However, as distinguished from other limited-time payments, Lottery and parity pay are funded continuously by statute and paid pursuant to the availability of funds at the state level, and are therefore ongoing and creditable to the DB Program.

CalSTRS determined that, unlike other compensation types described in these regulations, the two pay types listed warranted specific instructions. Naming them specifically provides employers information they need to report them to CalSTRS correctly.

Subdivision (b)

This subdivision describes remuneration in addition to salary that is creditable directly to the DBS account. Two criteria are listed. A summary and the rationale of each follows:

- *The compensation is not ongoing.* This is clarified so that members and employers are aware of criteria that demonstrate whether pay is not ongoing.
- *The compensation is paid to an individual contingent upon either of the following:* A discussion of each of the two qualifiers listed in the regulations follows:
 - *Availability of funds.* It is fairly common in California education to provide a bonus off the salary schedule that is based on availability of funds on a year-by-year basis. Such ad-hoc payments are not the basis of future pay increases and are not creditable to the DB Program on the basis that they are not ongoing. This specification ties into the provision above because pay that is granted solely based on availability of funds, regardless of purpose or source, is not creditable to the DB Program; whereas the items in subparagraph (B) of

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paragraph (2) of subdivision (b) (described in the bullet below) generally are, unless they are not ongoing.

- *Meeting any of the following qualifications or requirements (list follows)*. The list that follows is comprised of the same items described under Section 27401 and is included here for the same reason.

This section provides clear criteria for identifying payments that are creditable to the DBS account. CalSTRS anticipates that providing this guidance will improve the accuracy and consistency of reporting compensation that is paid a limited number of times.

STUDIES, REPORTS OR OTHER DOCUMENTS RELIED UPON

Creditable Compensation – Policy Issues; California State Teachers’ Retirement System Benefits and Services Committee meeting, Item 5a, April 11, 1996.

STANDARDIZED REGULATORY IMPACT ANALYSIS

CalSTRS has considered the proposal's impact on business, with consideration of industries affected and information supplied by interested parties, including the ability of California businesses to compete with businesses in other states.

CalSTRS has determined that the regulations proposed do not constitute a major regulation as they are not expected to have any economic impact beyond improved reporting by employers, which is expected to result in savings to those employers. The regulations will have impact on an individual basis to CalSTRS members insofar as their take-home pay and credited compensation for retirement purposes are affected by the appropriate reporting and crediting of contributions as specified herein. Neither of these impacts is anticipated to have any notable effect on California businesses. Specifically:

- The action will not affect the creation or elimination of jobs within the state.
- The action will not affect the creation of new businesses or the elimination of existing businesses within the state.
- The action will not affect the expansion of businesses currently doing business within the state.
- The action will have no effect on the health and welfare of California residents, worker safety, and the state's environment.

CONFERRING WITH INTERESTED PERSONS

Pursuant to Government Code Section 11346.45, staff at CalSTRS held a series of meetings via telephone and in person with more than fifty employers, including county offices of education, K-12 school districts and community college employers, and member advocate groups, including representatives of the California Teachers

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Association, the Association of California School Administrators, the Small School Districts' Association and the California Federation of Teachers, to discuss issues and concerns surrounding these proposed regulations. Early drafts of the proposed concepts have been provided to interested persons, and revisions have been made based upon the dialogue and feedback received.

ALTERNATIVES CONSIDERED

CalSTRS weighed the option of continuing to determine whether or not a class of employees was valid on a case-by-case basis. CalSTRS determined that there was inconsistent understanding as to the requirements in the law, and it would benefit employers to provide additional guidance through regulation.

CalSTRS considered the option of continuing to determine creditability of compensation on a case-by-case basis. CalSTRS concluded that the only effective way to ensure reporting requirements are consistently understood is by clarifying them through regulation.

CalSTRS reviewed the option of continuing to determine the appropriate crediting of contributions to the DBS account on a case-by-case basis. CalSTRS concluded that clarifying its standards for determining inconsistent treatment of compensation and establishing a consistent formula to be used in cases of inconsistent treatment through regulation would be the most effective method to implement this authority with transparency and equity.

The board has not identified any alternative that would lessen any adverse impact on small businesses.

ECONOMIC IMPACT ON BUSINESS

These regulations do not place any economic burden on business as they do not place any additional licensing, record keeping or compliance requirements on businesses. The primary economic impact of these regulations is to individual educators and their employers, and any indirect effect on businesses would be solely the result of that impact.