

CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM

BILL ANALYSIS

Senate Bill 501 **Senate PE&R Committee (Amended 7/5/01)**

Position **Sponsor**

Proponents: **None known**

Opponents: **None known**

SUMMARY

Senate Bill 501 is the annual California State Teachers' Retirement System (CalSTRS) technical housekeeping bill, which makes various grammatical, technical and conforming changes to the Teachers' Retirement Law (TRL) to facilitate efficient administration of the system. The specific changes include:

- Clarifying the definition of full-time equivalent for part-time positions.
- Deleting a reference to a legislative committee that no longer exists.
- Repealing duplicative provisions in the law.
- Making necessary state law changes to implement recent federal tax legislation.
- Explicitly excluding unused educational leave credit in determining eligibility for the career factor and other career-based benefit enhancements, consistent with the treatment of unused sick leave.
- Clarifying the relationship between the ad-hoc benefit increase and the minimum guarantee benefit enacted in 2000.
- Clarifying that the administrative expenses of the Replacement Benefits Program (RBP) include the employer portion of the Medicare payroll tax.
- Clarifying provisions of 2000 legislation enhancing CalSTRS benefits.

HISTORY

Chapter 1032, Statutes of 2000 (SB 1435—Johnston) requires CalSTRS to pay the Medicare Part A premium for retired members who are not eligible for Medicare Part A without payment of a premium.

Chapter 1027, Statutes of 2000 (AB 429—Correa) provides for an increase in benefits paid to members or beneficiaries based on the length of time since retirement, death or disability.

Chapter 1026, Statutes of 2000 (SB 1505—Burton) provides for a minimum guaranteed income for teachers who have a career of at least 20 years and have retired on or before January 1, 2000.

Chapter 874, Statutes of 2000 (AB 2383—Keeley) expands eligibility under Public Employees Medical and Hospital Care Act (PEMHCA) for part-time employees and requires CalSTRS to report on prescription drug and retiree health program.

Chapter 402, Statutes of 2000 (AB 649—Machado) permits state employee members of the Defined Benefit (DB) Program to convert unused educational leave to service credit upon retirement.

Chapter 465, Statutes of 1999 (AB 819—PER&SS) establishes the RBP to pay benefits otherwise payable under the DB Program that exceed limitations imposed by Section 415 of the Internal Revenue Code.

Chapter 678, Statutes of 1998 (AB 1166—House) modifies and clarifies minimum standards for determining full-time for purposes of crediting service for CalSTRS members.

SUMMARY OF AMENDMENTS

The July 5, 2001 version of this bill contains numerous changes of a largely technical nature. The major changes:

- Make the necessary state law changes to enhance the portability of retirement funds from other plans to the DB Program, as enacted in recent federal tax legislation.
- Clarify that period-certain annuities under the Defined Benefit Supplement (DBS) Program and the Cash Balance (CB) Benefit Program have to reflect periods in whole-year increments.
- Add language to prevent provisions of this bill from “chaptering-out” amendments to sections made in other legislation enacted in 2001.

DISCUSSION

1. Clarify full-time equivalent definition

Section 22138.6 defines full-time equivalent with respect to a person employed on a part-time basis. The bill modifies a provision of that section to clarify that the definition applies to a part-time position.

Education Code section affected by amendment: 22138.6

2. Delete reference to committee that no longer exists

Section 22352 refers to the Joint Public Pension Fund Investments Committee, which is no longer in existence. The bill deletes that reference.

Education Code section affected by amendment: 22352

3. Clarify consent to deduct employee contributions

Section 22900 requires a person to make contributions to the DB Program if he or she accepts employment. The bill clarifies that the employment is for service that is being credited to the DB Program.

Education Code section affected by amendment: 22900

4. Modify or delete code section due to duplication

Provisions included in some sections of the law are duplicated in other sections, and are therefore being deleted.

Education Code sections affected by amendment: 22136.5, 24001 and 24101

5. Conform to federal tax law changes

The federal Economic Growth and Tax Relief Reconciliation Act of 2001 enacted a number of federal law changes to improve the portability of funds among different types of retirement plans, including 401(k), 403(b) and 457 plans, IRAs and retirement plans, such as the State Teachers' Retirement Plan. This bill makes the necessary changes in state law to implement the enhanced portability of retirement funds. Specifically, it deletes the existing prohibition in using 403(b) funds to purchase out-of-state service credit that is being credited to the DB Program. It also codifies in state law the existing authority in federal law for the Teachers' Retirement Board to accept direct transfers of retirement funds from trustees of other retirement funds.

Education Code sections affected by amendment: 22811 and 22820

6. Clarify ineligibility of officer of employee organization for Disability Allowance

Elected officials of an employee organization may take a compensated leave of absence from DB Program service. Current law prohibits such officials from receiving a disability benefit while on such a leave of absence. The bill clarifies that the prohibition applies to a disability allowance, reflecting current practice.

Education Code section affected by amendment: 24001.5

7. Exclude unused educational leave credit from various benefit calculations

Chapter 402, Statutes of 2000 (AB 649—Machado) permits state employee members of the DB Program to convert unused educational leave to service credit upon retirement. This is similar to existing authority to convert unused sick leave to service credit upon retirement. Existing law provides a variety of benefit enhancements to members whose years of credited service equal or exceed specified amounts. Credited service is service on which contributions are paid. Because

contributions are not paid on unused sick leave or unused education leave, this service credit, by definition, does not count towards determining eligibility for these benefit enhancements. To make that restriction clear, the TRL also explicitly excludes unused sick leave from being used to determine eligibility for the benefit enhancements. This bill makes it similarly explicit that unused educational leave does not count towards qualifying for such benefit enhancements. In addition, Section 24212 addresses the calculation of a disability allowance when a member does not return to CalSTRS-covered employment, but has unused sick leave at the time of retirement. The bill amends that section to provide for similar treatment of unused educational leave.

Education Code sections affected by amendment: 24203.5, 24203.6, 24209, 24211, 24212, 24410.6 and 24410.7

8. Clarify the relationship between ad-hoc benefit increase and minimum guarantee

Chapter 1027, Statutes of 2000 (AB 429—Correa) provided an increase in benefits to members who died, retired or were disabled prior to 1998. Chapter 1026, Statutes of 2000 (SB 1505—Burton) provided a minimum guaranteed benefit to members whose CalSTRS benefit was below a specified amount, based on years of CalSTRS service. This bill clarifies that the calculation of the benefit paid pursuant to Chapter 1026 does not include the amount paid under Chapter 1027, consistent with current practice and the estimated cost of the previous legislation.

Education Code section affected by amendment: 24410.6 and 24410.7

9. Clarify payment of Medicare payroll taxes on the Replacement Benefits Program benefits

Section 415 of the Internal Revenue Code (IRC) imposes a limit on benefits that can be paid by a state or local government defined benefit plan, such as the DB Program. The RBP was established in CalSTRS, consistent with Section 415, to pay benefits to DB Program members in excess of these limits. Under the IRC, replacement benefit payments are considered wages, even though the retired member is no longer an employee on the payroll of an employer. As a result, the member and the employer must continue to pay Medicare payroll taxes if the member was paying the Medicare tax while employed. (Currently, only one member receiving a benefit under the RBP is required to pay the Medicare tax on that benefit.) In order to simplify the collection and payment of the employer's portion of the payroll tax, this bill includes the employer portion of Medicare payroll tax as an administrative expense for the RBP to pay. The alternative would be to bill the member's former employer and then transfer the payroll tax, on a quarterly basis, to the Internal Revenue Service (IRS). CalSTRS staff determined that it is more efficient and less costly to pay the Medicare payroll tax as an administrative expense rather than to bill the employer for this tax and then transfer the payment to the IRS.

Education Code section affected by amendment: 24260

10. Clarify 2000 benefit legislation

In 2000, 19 bills were enacted that affected benefits provided by CalSTRS, including significant benefit enhancements. This bill clarifies, consistent with the estimated cost of the original legislation, how these changes are applied in specific situations, such as the application of the

longevity bonus when a member divorces, retires for service after receiving a disability allowance or dies prior to retirement but after making a pre-retirement election of an option. The bill also conforms provisions of the TRL to current provisions that base final compensation for specified ex-spouses of members on the highest single year.

Education Code sections affected by amendment: 22664, 24203.6, 24209, 24211, 24307, 26401 and 26911

11. Clarify annuity payments in the Defined Benefit Supplement Program and the Cash Balance Benefit Program

Current law establishes the DBS Program for DB Program members and, for part-time members who elect to participate, the CB Benefit Program. The design of the two programs is nearly identical. Under the programs, members and participants may elect to take their benefit in the form of a lump sum, or, if the member or participant has at least \$3,500 in his or her DBS or CB Benefit account, a monthly annuity. This bill clarifies how annuity payments are made and makes the basis of computing the annuity the same for the two programs, without increasing or decreasing the benefit paid, to simplify program administration and avoid confusion on the part of the member and participant. This bill also clarifies that the period certain annuity which would be payable over a specified number of years would be in whole year increments, as well as clarifies benefits made upon the death of the participant's beneficiary. This bill also clarifies the provisions of the designation of the beneficiary for benefits payable under the DBS program.

Education Code sections affected by amendment: 24402, 25011, 25015, 25018, 25014, 25019, 25021, 26807, 26906, 26911, 27004, 27007 and 27008

12. Clarify the Medicare Benefits (MB) Program and other health benefit provisions

Chapter 1032, Statutes of 2000 (SB 1435—Johnston) established the MB Program to pay the Medicare Part A (hospitalization) premiums for retired DB Program members who are not eligible for premium-free coverage through other employment or through their spouse. For members retiring in the future, eligibility is dependent on the member retiring from a district that has conducted a Medicare division or is in the process of conducting that division. In addition, if the member is under age 58 at the time of the division, the member must agree to be subject to the Medicare payroll tax. This bill specifies, consistent with current practice, when a division is being conducted. It also clarifies that a district does not need to conduct the division if none of the potentially affected employees were under age 58 on January 1, 2001, or if the district was formed after April 1, 1986. In both cases, conducting the division would not result in any reduction in the number of potential participants in the CalSTRS program. In addition, the bill clarifies who is an employer for purposes of the program. Finally, it renames the program the Medicare Premiums Payment Program, which more accurately describes the objectives of the program.

Education Code sections affected by amendment: 25921, 25926, 25940

Chapter 874, Statutes of 2000 (AB 2383—Keeley) extended participation in the PEMHCA Program administered by the California Public Employees' Retirement System to family

members of deceased CalSTRS members and to part-time members of CalSTRS. Certificated employees are not members of CalSTRS; they are members and participants in the State Teachers' Retirement Plan (consisting of the DB Program and the CB Benefit Program), which is administered by CalSTRS. This bill clarifies this terminology.

Government Code sections affected by amendment: 22878.2 and 22878.3

13. Correct grammatical errors in various sections

- The bill removes the text "awarding certifications, in which eligibility for this certification is" from Section 22119.2 because the phrase is unnecessary.

Education Code section affected by amendment: 22119.2

- The bill replaces the word "person" with "member" in Section 22151, because it is a more accurate depiction of school employment and membership status.

Education Code section affected by amendment: 22151

- The bill capitalizes the phrase "Defined Benefit Program" in Section 24255.

Education Code section affected by amendment: 24255

- The bill clarifies that the beneficiary of an option beneficiary is entitled to any allowance that has accrued and is unpaid to the option beneficiary at the time of the option beneficiary's death.

Education Code section affected by amendment: 24300.5

- The bill corrects inadvertent or incorrect references to code sections.

Education Code sections affected by amendment: 24404(b), 25925 and 25930

- The bill deletes references to specific code sections that identify the benefits that beneficiaries of members who died with a pre-retirement election of an option in effect would receive, and replaces them with a reference to the entire service retirement chapter of Part 13, in order to simplify the provision and automatically responsive to changes in service retirement benefits.

Education Code section affected by amendment: 24307

Finally, this bill includes supercession language, which states that if other legislation is passed during the current legislative session that amends sections that also are included in this bill, the other legislation prevails.

FISCAL IMPACT

Benefit Program Costs – The potential costs regarding payment of the employer portion of the Medicare payroll tax as part of the administrative expenses of the RBP are estimated to be less than \$5,000 to \$10,000 per year, which is less than it would cost to collect that tax payment from the affected employers. There are no other costs resulting from this bill.

Administrative Costs – Minor and absorbable.

BOARD POSITION

Sponsor. This bill will make grammatical and technical amendments necessary for continued effective administration of the system. It also deletes superfluous provisions of the law.