Revised on 6/8/21

KCERA *Alameda* Decision FAQs

Frequently asked questions submitted to KCERA Staff have been compiled and corresponding responses are provided below under the following categories:

ALAMEDA BACKGROUND & DEFINITIONS

1. **Question:** What is the *Alameda* Decision and why is it impacting KCERA members?

- **Answer:** The pension reform laws of 2013, commonly referred to as "PEPRA legislation," limited the types of compensation that could be included in members' pension calculations. In 2013, many peer retirement systems switched their pay codes from pensionable to non-pensionable to conform to the new laws and were sued by various labor groups. Because KCERA had a legal Settlement Agreement from 2002 regarding these pay codes, it decided to wait for the courts to give authoritative guidance. The various lawsuits made their way through the courts and all the way up to the California Supreme Court, which decided the *Alameda* Case on July 30, 2020. Specifically, the Court ruled that the PEPRA legislation was valid law and it superseded previous settlement agreements. KCERA must now timely implement the Court's decision.

2. **Question:** Why must KCERA make these changes?

- **Answer:** Members have raised concerns that the exclusion of certain pay codes from member pension calculations is contrary to KCERA's commitment to pay the "promised benefit." While KCERA has a fiduciary duty to administer the promised benefit to our members, its duty to pay such benefits is conditioned on the member being legally eligible for the benefit. KCERA cannot pay a benefit that is contrary to the law even if the employer promised or agreed to offer it. The Internal Revenue Service mandates that KCERA follow the laws governing its plan benefits and adjust overpaid or underpaid benefits to avoid the risk losing its tax qualified status.

  KCERA's tax qualified status exempts KCERA from having to pay taxes on its investment earnings and is what enables all KCERA Plan Sponsors and KCERA members to make retirement contributions on a pre-tax basis. Without KCERA's tax exempt status, there would be less funds available to pay monthly pensions because taxes would have to be deducted from investment earnings and employer and employee contribution payments.

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The California Supreme Court ruled that the PEPRA legislation was valid law and it superseded previous settlement agreements. KCERA must now timely implement the Court's decision to comply with the law and to maintain the tax qualified status of the plan.

3. **Question:** What are *Alameda* Exclusions?

- **Answer:** When KCERA Staff refers to "*Alameda* Exclusions," it is referring the types of pay used to fund "in-kind" benefits. The California Supreme Court decided in the *Alameda* case that county retirement plans must exclude these in-kind benefits from the pension calculation because an in-kind benefit that cannot be received by a member directly in cash, is not considered "compensation," as that term is defined by statute and case law and never should have been included in the pension calculation.

  Prior to the *Alameda* case, plans were permitted to, but case law did not appear to require it to, exclude these in-kind benefits. The San Joaquin Valley Air Pollution Control District is the only employer with "*Alameda* Exclusions," because it is the only employer that required some of its KCERA members to use a portion of its District Cafeteria pay for in-kind benefits and included the payment to the in-kind benefit provider in their pension calculation.

4. **Question:** What are "in-kind benefits"?

- **Answer:** Any non-cash benefit that is provided by the employer, which the employee has no ability to elect to receive directly and keep in cash. Rather, the employee must receive the benefit "in-kind," such as by receiving lodging, a uniform, an insurance plan and employer payments to deferred compensation plans.

5. **Question:** What's the difference between an "in-kind" benefit and the Flex$Pay offered by the County of Kern?

- **Answer:** For purposes of determining whether the pay is pensionable or not, the significant difference is the ability to elect to receive the amount as cash.

6. **Question:** When did KCERA begin collecting employee contributions on Flex$Pay or District Cafeteria (DC pay) payments?

- **Answer:** After October 23, 2001.

  On January 15, 1991, the Kern County Board of Supervisors adopted the provisions of California Government code section 31460.1 (excluding flexible benefits from the pension calculation for all KCERA members) through Resolution 91-056. SJVAPCD was formed in 1992 and its DC pay began in September of 1993.

  Following the California Supreme Court's decision in the *Ventura* case, KCERA's Board of Retirement approved Resolution 99-03 on July 28, 1999. This Resolution designated employer payments into a flexible benefit program (including DC pay) as excluded from compensation in accordance with Cal. Gov. Code section 31460.1 and the Kern County Board of Supervisors Resolution 91-056, among other things. Resolution 99-03 was later adopted by the parties to the *Ventura* Settlement Agreement in 2001 ("Settlement Agreement"), except that the Settlement Agreement added employer paid flexible benefit payments **(to the extent received in cash)** into

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the pension calculation. As part of the Settlement Agreement, the County's Board of Supervisors agreed to repeal Resolution 91-056 on October 23, 2001. Until the PEPRA legislation (as interpreted by California Supreme Court's *Alameda* decision), KCERA's *Ventura* Settlement Agreement applied to all past, present, and future KCERA members.

7. **Question:** What are PEPRA Exclusions?

➢ **Answer:** PEPRA Exclusions refer to the types of pay listed in California Government Code section 31461(b) and 7522.34(c). These exclusions include, among other things, availability pays, on-call pays, stand-by pays, and any pay, regardless of its name, that is paid for services an employee provides outside normal working hours. More items of pay are excluded for PEPRA members under section 7522.34(c) than are excluded for Legacy members under section 31461(b). As a result, some pay codes are designated as pensionable for Legacy members and not pensionable for PEPRA members.

BASIC KCERA PLAN INFORMATION

8. **Question:** Can you clarify the different "Tiers"? Who are "Legacy" members and who are "PEPRA" members?

➢ **Answer:** KCERA administers benefits for five different benefit tiers:

- General Tier I: "3% at age 60"
- General Tier II: "1.62% at age 65"
- General Tier III*: "2.5% at age 67" (**Westside Recreation and Park District only)*
- Safety Tier I: "3% at age 50"
- Safety Tier II: "2% at age 50"

In general, Legacy members are those who became members of KCERA on or before December 31, 2012. Legacy members may be General Tier I, General Tier II, Safety Tier I or Safety Tier II. PEPRA members are those who became members of KCERA on or after January 1, 2013. PEPRA members may be General Tier II, Safety Tier II or General Tier III. Your membership date is not the same as your hire date. "Membership" in KCERA begins when you start paying retirement contributions, which can be anywhere from one day to two weeks after your hire date with a KCERA plan sponsor. There are a variety of factors that could impact Tier placement including: reciprocity, multiple periods of service, refunds, redeposits, etc.

RETIREMENT CONTRIBUTION CALCULATIONS

9. **Question:** How are employee retirement contributions calculated?

➢ **Answer:** For the vast majority of KCERA members, contributions are calculated as a percentage of pensionable earnings with a small adjustment for integration with social security. For full-time employees, pensionable earnings are the sum of scheduled biweekly base pay plus actual pensionable special pays. For part-time employees, pensionable earnings are the sum of actual base pay plus actual pensionable special pays.

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However, the MOU Agreements for some KCERA member groups require contributions to be calculated differently.*

** Some member groups do not pay contributions, some KCSC members pay a flat percentage of biweekly base pay (ERC), and KCFFU member contributions are capped at a percentage of base pay.*

RETIREE PENSIONS

10. **Question:** Which retirees are affected by the *Alameda* Court's decision?

- **Answer:** Members who retired before January 1, 2013 will not be affected by KCERA's expected implementation of the *Alameda* Exclusions or PEPRA Exclusions.

  Members who retired before July 30, 2020 will not be affected by the change in law referred to as the *Alameda* Exclusions. Staff recommended and the Board of Retirement confirmed that no adjustments will be made to these members' pensions for any *Alameda* Exclusions.

  However, a member who retired on or after January 1, 2013, may have their pension reduced for any applicable PEPRA Exclusions.

11. **Question:** Will retirement pensions be reduced?

- **Answer:** Unfortunately, for some members who retired on or after January 1, 2013, the answer is, "yes." KCERA Staff is reviewing approximately 200 pay codes to see which are impacted by the *Alameda* Decision. Once Staff determines which codes are to be included in or excluded from the pension benefit calculation by PEPRA and the *Alameda* Decision, Staff will bring its recommendations to the Board of Retirement for designation of the affected codes. After the Board designates those pay codes, Staff will begin to calculate the corrections to monthly benefits. KCERA intends to contact individual members as soon as possible to notify them whether their pension benefit may be adjusted.

12. **Question:** When will my monthly pension check be reduced?

    Answer: KCERA Staff is making every effort to complete all adjustments as soon as administratively feasible. However, the process of implementing benefit and contribution changes for approximately 300 retired members involves complex calculations and consideration of unique member issues such as Domestic Relations Orders, Disability Retirement, Temporary Annuity Options (TAO), and the like. The complexity and volume of member accounts may increase the time it takes KCERA Staff to make the corrections.

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13. **Question:** When will these changes start for retirees?

- **Answer:** The effective dates are July 30, 2020 and August 30, 2020, but most changes to retiree pensions will not be implemented until at least October 2020. On August 24, 2020, the Board of Retirement approved a Resolution which set the following effective dates for retirees: July 30, 2020 for members with *Alameda* Exclusions who retired on or after that date (SJVAPCD only) and August 30, 2020 for retired members who have PEPRA Exclusions. Because KCERA will need time to determine which member accounts may need adjustments, the full implementation of the *Alameda* decision will occur over time, in phases. First, KCERA will adjust the monthly pension benefit prospectively for affected retirees. Then, KCERA will recoup amounts retirees were overpaid from August 30, 2020 (for PEPRA Exclusions) and July 30, 2020 (for *Alameda* Exclusions) through the date that the pension payment was adjusted.

14. **Question:** I am a retiree, if I have to pay back an overpayment due to pays that should not have been included in my pension calculation, am I going to be required to pay it in a lump sum or will KCERA make payment arrangements?

- **Answer:** KCERA will provide lump sum and monthly repayment options for members, as needed and as allowed by the laws governing KCERA.

15. **Question:** After affected pay codes are excluded from my pension calculation, how will my monthly pension be recalculated? Will you use my next highest paid year of compensation or will you just subtract the newly excluded pay codes from my current benefit?

- **Answer:** The pension administration system will automatically search for and select your highest twelve consecutive months of salary for Legacy members and the highest 36 consecutive months for PEPRA members. This means that your adjusted pension amount could, but may not, be based on the same year used to calculate your pension at retirement. KCERA Staff will review each recalculation for accuracy before finalizing the new benefit.

16. **Question:** Will this decision affect my TAO option (Temporary Annuity Option) that I chose when I retired?

- **Answer:** The temporary annuity amount KCERA used to calculate your pension benefit was based on information obtained from Social Security at the time you retired. Therefore, your pension may be reduced due to any affected special pays but the temporary annuity amount used for the calculation of your benefit will not be changed.

17. **Question:** For retirees whose pension benefit will be adjusted, is this adjustment going to be retroactive from the time of retirement?

- **Answer:** KCERA Staff has developed a workbook to help members identify their unique situation. See the document called "**Scenario Analysis – Impacted Members**" on the KCERA *Alameda* Resources Page.

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ACTIVE MEMBERS

18. **Question:** How are my employee retirement contributions calculated?

- **Answer:** For the vast majority of KCERA members, employee contributions are calculated as a percentage of pensionable earnings with a small adjustment for integration with social security. For full-time employees, pensionable earnings are the sum of scheduled biweekly base pay, plus actual pensionable special pay codes. For part-time employees, pensionable earnings are the sum of actual base pay plus actual pensionable special pay codes.

  However, the MOU Agreements for some KCERA member groups require employee contributions to be calculated differently.*

  ** Some member groups do not pay contributions, some KCSC members pay a flat percentage of biweekly base pay (ERC), and KCFFU member contributions are capped at a percentage of base pay.*

19. **Question:** If I am currently working will I still pay contributions on these Special Pay Codes?

- **Answer:** KCERA has asked plan sponsors to cease collecting contributions on pay codes that are determined to not be pensionable.

20. **Question:** When will the changes to employee retirement contributions start for active members?

- **Answer:** Plan sponsors are implementing the changes as soon as administratively feasible. Contributions that are collected in error will be refunded. (See also Corrective Distribution section below).

21. **Question:** How will these changes affect my biweekly paycheck?

- **Answer:** Because most of the affected pay codes are being excluded from the pension calculation, you will no longer pay retirement contributions on the amounts you receive for those pay codes. This means that your take home pay should increase.

22. **Question:** I'm an active member and some of my special pays are on the list. So, does that mean that I am not going to get paid for or receive that special pay any longer?

- **Answer:** No. You are still going to be paid for any special pay code(s) on your paycheck, (as allowed by your employer). The changes to the designation of your pay codes means that you will no longer pay retirement contributions on the amount related to that pay code because it will no longer be included in your retirement calculation when you retire.

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23. **Question:** If I became a member of KCERA prior to PEPRA (January 1, 2013), will my future pension benefit be affected?

- **Answer:** It depends. The PEPRA legislation changed the definition of compensation earnable, which applies to all Legacy members. Therefore, certain pay codes affected by the *Alameda* decision will no longer be included in your pension calculation at retirement. If your highest consecutive 12-months of compensation was based on pay codes that have recently been excluded, your future pension benefit will likely be less than what you previously expected. However, if your highest consecutive 12-months are ahead of you (meaning, you are likely to promote to a higher paying classification before you retire), then your future retirement benefit will not be affected.

SPECIAL PAY CODE DESIGNATIONS

24. **Question:** Will we receive notification if we are/are not affected by the *Alameda* decision?

- **Answer:** KCERA has sent our numerous email communications to impacted members via the member portal and via U.S. mail.

25. **Question:** Which Special Pay Codes are affected?

- **Answer:** KCERA Staff has published a **Pay Code Tracker** on the KCERA *Alameda* Resources Page, which has been updated to reflect those special pay code designations approved by the Board of Retirement. There you can see which codes are to be included in or excluded from the pension benefit calculation.

26. **Question:** How do I know which special pay codes I am receiving? Where can I locate the pay code? How can I find out what the pay code means/stands for?

- **Answer:** KCERA Staff has made changes to its Member Portal system so that members can view their individual pay types through the Portal. If you do not already have a Portal account, instructions can be found on the login page. Special pay codes may also be reflected on the biweekly paystub received from your employer.

27. **Question:** Since my schedule is mandatory and I receive one of the affected pay types, shouldn't it be included in my retirement calculation? I have no choice in my schedule.

- **Answer:** The PEPRA legislation, upheld by the California Supreme Court, excludes several pay types, including payments for "additional services rendered outside normal working hours" without regard for whether the additional services were mandatory or voluntary.

28. **Question:** Will this affect my Longevity pay I will receive when I retire?

- **Answer:** See the **Pay Code Tracker** on the KCERA *Alameda* Resources Page for the pay codes that have changed. Longevity pay has not changed.

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29. **Question:** Why is Flex$Pay for Legacy members of the County, Hospital Authority and Court included in the pension calculation, but excluded from the calculation for PEPRA members?

- **Answer:** The additional salary paid to these members as Flex$Pay is considered a separate cash "allowance" to help offset the cost of purchasing voluntary benefits like dependent care, miscellaneous health care items (not insurance premiums), life insurance, disability insurance, etc. The PEPRA legislation (California Government Code section 7522.34(c)(7)) prohibits KCERA from including "allowances" in a PEPRA member's pension calculation. Section 7522.34(c)(7) does not apply to Legacy members. Legacy members are subject to Government Code section 31461, which does not specifically exclude "allowances" from the pension calculation like section 7522.34(c)(7).

CORRECTIVE DISTRIBUTIONS

30. **Question:** What is a Corrective Distribution?

- **Answer**: In short, it is a payment by KCERA to the member for excess employee contributions the member paid. Under IRS' guidance (Revenue Procedure 2019-19), when employee contributions are over or under collected, it is considered an "Operational Failure" because the KCERA failed to follow its governing terms. When this occurs, the IRS requires the retirement plan to correct the failure. For overpaid contributions, the matter is corrected via a Corrective Distribution. And, for underpaid contributions, KCERA is required to collect and return the underpaid contributions to the retirement fund.

31. **Question:** Who will receive a Corrective Distribution?

- **Answer**: At this point, KCERA's Board has approved the return of overpaid contributions to Active and Deferred members. It is important to note that not all KCERA members will receive a Corrective Distribution, as not all members earn special pays and not all members had special pay codes that were affected by the *Alameda* decision. In general, this means that only those members whose account history demonstrates 1) that they paid employee contributions on pay codes that were recently re-designated as non-pensionable; 2) that the compensation from the affected pay code(s) was earned and received after January 1, 2013; and 3) that the overpayment of contributions was not off-set by an underpayment of contributions for another recently designated pay code.

  As noted in Retirement Contribution Calculations, MOU Agreements may structure member contributions differently (i.e. flat rate versus percentage of pay); so, not all KCERA members who receive pay codes affected by the *Alameda* decision pay contributions on those pay codes.

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32. **Question:** How was the corrective distribution amount estimated?

➢ **Answer:** After the KCERA Board re-designated the special pay code impacted by the *Alameda* decision, KCERA Staff notified plan sponsors of the changes to pensionable pay codes to ensure that the pay codes properly reflected the new designations for the "impacted payroll periods" (See Active Members).

To calculate your Corrective Distribution, KCERA reviewed pensionable earnings and the contributions paid for the impacted payroll periods. KCERA calculated the contributions owed on the revised pensionable earnings and subtracted this from the contributions paid. KCERA Staff then applied interest to this difference for each biweekly payroll period. The result is the amount of your Corrective Distribution.

33. **Question:** What are the "impacted payroll periods"? In other words, what effective dates did you use in calculating the Corrective Distribution?

➢ **Answer:** PEPRA Exclusions are effective as of January 1, 2013 whereas *Alameda* Exclusions are effective as of October 23, 2001* or your KCERA membership date (whichever is earlier).

*For SJVAPCD members: When KCERA staff previously introduced the issue of *Alameda* exclusions, KCERA Staff explained that such exclusions would be effective on the KCERA membership date. KCERA Staff's explanation was based on the assumption that all SJVAPCD members paid contributions on District Cafeteria pay ("DC" pay) from their KCERA membership date forward.

Further historical analysis revealed that SJVAPCD employee contributions on DC pay did not begin until October 23, 2001.** This means that SJVAPCD members with KCERA membership dates prior to October 23, 2001 did not pay employee contributions on DC pay until that date. Thus, any overpaid contributions on DC pay will be calculated as of October 23, 2001, not as of the KCERA membership date

**On January 15, 1991, the Kern County Board of Supervisors adopted the provisions of California Government code section 31460.1 (excluding flexible benefits from the pension calculation for all KCERA members) through Resolution 91-056. SJVAPCD was formed in 1992 and its DC pay began in September of 1993. Following the California Supreme Court's decision in the *Ventura* case, KCERA's Board of Retirement approved Resolution 99-03 on July 28, 1999. This Resolution designated employer payments into a flexible benefit program (including DC pay) as excluded from compensation in accordance with Cal. Gov. Code section 31460.1 and the Kern County Board of Supervisors Resolution 91-056, among other things. Resolution 99-03 was later adopted by the parties to the *Ventura* Settlement Agreement in 2001 ("Settlement Agreement"), except that the Settlement Agreement added employer paid flexible benefit payments (to the extent received in cash) into the pension calculation. As part of the Settlement Agreement, the County's Board of Supervisors agreed to repeal Resolution 91-056 on October 23, 2001

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34. **Question:** When will I receive my corrective distribution?

- **Answer:** Please refer to the individual letter you received from KCERA for specific information related to the unique review of your special pay code history. Staff is working through each member file individually and prioritizing those with higher distribution amounts first. Distributions for active employees will also be prioritized. Our hope is to complete and process all distributions by December 31, 2021.

35. **Question:** Can the Corrective Distribution amount be rolled over to a Deferred Compensation Plan or a 401K to avoid the tax withholding?

- **Answer:** No. See, Tax Implications.

36. **Question:** Why is my coworker receiving a larger Corrective Distribution than me?

- **Answer:** Employee pensions are specific to the individual employee. As noted in Basic KCERA Plan Information above, KCERA has several Tiers relating to different member benefits and over 200+ available pay codes. Even within each Tier, members employed by the same plan sponsor, within the same department, performing the same job, do not pay the same amount in employee contributions. Each member's retirement contribution amounts depend on several factors, such as age at entry into the KCERA retirement plan, prior public employment, MOU terms, etc. Because each member's retirement contribution payments vary, even within job classifications, it follows that no two individuals will receive the same Corrective Distribution.

37. **Question:** If I receive a Corrective Distribution, will that change my retirement contribution balance shown on my prior retirement statements?

- **Answer:** Yes. The Corrective Distribution is a return of excess contributions, plus the interest earned on those contributions. This means your retirement contribution balance will be reduced accordingly.

38. **Question:** Will this affect my years of service once Corrective Distributions have been dispersed?

- **Answer:** No.

39. **Question:** Will this affect my ability to purchase service credit?

- **Answer:** No. Members may continue to purchase service credit, but will not be charged for and will not be able to purchase special pay codes that have been recently re-designated as non-pensionable.

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ABILITY TO OBJECT/ADMINSTRATIVE APPEAL

40. **Question:** If I do not agree with KCERA's designation of a special pay code or other change to my current or future benefits, can I appeal?

- **Answer:** Yes. KCERA offers an administrative appeal process. Once the Board of Retirement takes action, KCERA Staff will send a letter notifying affected members of the change and the individual financial impact. The letter will include information about how to proceed with an administrative appeal.

TAX IMPLICATIONS

41. **Question:** Will this affect my retirement tax status? My disability tax status?

- **Answer:** Any effect on your current tax rate will depend on how much your monthly pension is reduced. Please consult a tax professional once KCERA notifies you of the specific financial change to your monthly pension.

42. **Question:** What is Rev. Proc. 2018-52 and how does it pertain to KCERA's overpayment/underpayment corrections of benefits and contribution policies?

- **Answer:** Revenue Procedure 2018-52 (Rev. Proc. 2018-52) is an updated and modified Employee Plans Compliance Resolution System (EPCRS) submission procedure for the Voluntary Correction Program (VCP). [https://www.irs.gov/]. The IRS established EPCRS to help qualified retirement plans correct errors that could affect the plan's tax qualified status. KCERA's corrections policies were drafted in accordance with the Internal Revenue Code, including its revenue procedures.

43. **Question:** Can the Corrective Distribution amount be rolled over to a Deferred Compensation Plan or a 401K to avoid the tax withholding?

- **Answer:** No. Under the IRS' guidance (Revenue Procedure 2019-19) excess employee contributions are considered an "Operational Failure" based upon a failure to follow the Plan's terms. Such failures must be corrected through one of the correction procedures authorized by the IRS. "Corrective Distributions" are the mechanism used to return excess employee contributions. The IRS does not allow "Corrective Distributions" to be rolled over on a pre-tax basis.

  Additionally, members who previously paid employee contributions on the recently re-designated PEPRA Exclusions and *Alameda* Exclusions did so on a pre-tax basis. From a tax perspective, this means, that the member's contributions were not taxed and improperly reduced the member's taxable income (to the extent of the payment on the recently excluded pay code). KCERA's tax-qualified status only exempts retirement contributions and investment earnings from taxation. The *Alameda* decision confirmed that the affected pay codes should not have been pensionable. Allowing the Corrective Distribution to retain pre-tax or tax-protected status via a rollover to another pre-tax account is contrary to the Supreme Court's determination that the affected pay codes are either not "compensation" or not pensionable.

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