A trailer bill of the 2014-15 State Budget, Assembly Bill (AB) 1469 (Bonta, D-Alameda) lays out the plan to resolve the California State Teachers’ Retirement System (CalSTRS) unfunded liability by 2046 through contribution rate increases for employers, employees, and the state.

**Contribution Rate Increases**

Taking a slightly different tack than either Governor Jerry Brown’s proposal or the legislative alternative proposal, the final plan has a small employer contribution rate increase in 2014-15 (0.63%) and consistent increases (1.85% each year until a final 0.97% increase) up to final implementation of a 19.1% contribution rate in 2020-21. This final plan does not contain the significant spike in the fourth year of implementation that was included in the Legislature’s alternative proposal.

For employees, whether pre- or post-PEPRA (the Public Employees’ Pension Reform Act of 2013), the contribution rate increase for 2014-15 will be 0.15%. Rates will diverge in 2015-16, when pre-PEPRA employees will see a bigger increase. In reaction to the Governor’s original proposal, CalSTRS noted that its system is not yet ready to accommodate different employee contribution rates, but would be for 2015-16.

Below are the rate increases as specified in the bill:

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</thead>
<tbody>
<tr>
<td>Employers</td>
<td>8.88%</td>
<td>10.73%</td>
<td>12.58%</td>
<td>14.43%</td>
<td>16.28%</td>
<td>18.13%</td>
<td>19.1%</td>
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<tr>
<td>Pre-PEPRA</td>
<td>8.15%</td>
<td>9.2%</td>
<td>10.25%</td>
<td>10.25%</td>
<td>10.25%</td>
<td>10.25%</td>
<td>10.25%</td>
</tr>
<tr>
<td>Employees</td>
<td>8.15%</td>
<td>8.56%</td>
<td>9.205%</td>
<td>9.205%</td>
<td>9.205%</td>
<td>9.205%</td>
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In addition, the state’s contribution rate increases 4.311% over three years. All of these rate increases take effect on July 1 of each year and are calculated on the member’s compensation that is creditable to the Defined Benefit Program as of that date.

**Rate Flexibility**

The plan gives CalSTRS more flexibility than it had in the past, but is still less than that granted to CalPERS. Once the statutory rates are achieved (after seven years for employers and after three years for the state), the CalSTRS Board will have the authority to increase or decrease the contribution rate to reflect what is needed to exhaust the unfunded liability by 2046. For employers, the rate cannot change by more than 1% in any given year, cannot exceed an increase of 12% of creditable compensation (the 19.1% rate already represents a 10.85% increase), and cannot be increased in order to supplant the state’s obligation. The state’s rate cannot change by more than 0.5% in any given year.

As discussed throughout this legislative session, a guarantee of the retirement improvement factor was used to compensate employees for the increased contribution rate. While there is no change to how the improvement factor is applied, the vesting of the right is believed to be worth the corresponding employee rate increase. AB 1469 reserves the right to adjust the amount of the improvement factor if this trade-off ceases to be legally required. The findings and declarations of AB 1469 state: “The Legislature hereby increases the contributions of active members by an amount not to exceed the normal cost of the improvement factor . . . The provisions of [this] act . . . were based on various legal understandings and would not have been adopted without those understandings.”

**The Fine Print**

The bill states the increased employer contribution rates “do not constitute a new functional responsibility for schools and community
colleges” and “do not constitute a reimbursable mandate.” It contemplates legal actions that may find that the increased employer contributions may necessitate a rebenching of the Proposition 98 minimum guarantee or be found to be a mandate. If either of these are found to be true in a “final unappealable judicial decision”, the bill includes legislative intent that the provisions cease to be effective. Any challenges to these findings will need to be filed within 60 days of the bill’s effective date.

**Going Forward**

Finally, AB 1469 requires reporting by CalSTRS on the health of the defined benefit program. Beginning in 2019 and every five years thereafter, CalSTRS will be required to report on the unfunded liability and identify adjustments in contribution rates required to eliminate the unfunded liability by 2046.

—Michelle McKay Underwood

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