

NCTR 90TH ANNUAL CONVENTION LEGAL UPDATE WORKSHOP



STATE LEGISLATION AND COURT DECISIONS

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(The views expressed are solely those of the author and not of NYSTRS)

WHAT WE WILL COVER



1. Legislated changes affecting new entrants
2. Legislated changes affecting existing participants
3. Five court decisions ruling on participant challenges to legislated changes
4. Two court decisions discussing the duties of plan trustees

(Discussion is not all-inclusive as the author's intent is to focus on those developments considered to be of interest to attendees)

IMPORTANT CAUTION



- PUBLIC PLAN LEGAL ISSUES WILL OFTEN BE SIMILAR REGARDLESS OF STATE
- BUT PRECISE OUTCOMES MAY VARY FROM STATE TO STATE BECAUSE:
 - CONSTITUTIONAL PROVISIONS DIFFER
 - STATUTES DIFFER
 - COURT DECISIONS DIFFER

LEGISLATIVE DEVELOPMENTS



THE STORY ON THE LEGISLATIVE FRONT:

**State Legislatures Continue to Enact
Changes to Teacher Defined Benefit
Plans in Response to the Worst
Market Meltdown Since the Great
Depression**

CAUTION ON PLAN CHANGES



- LEGISLATURES ARE GENERALLY NOT CONSTRAINED WHEN LEGISLATING AS TO NEW ENTRANTS
- WHEN LEGISLATING AS TO EXISTING PARTICIPANTS, LEGISLATURES MAY BE CONSTRAINED, DEPENDING UPON THE LEGAL PROTECTIONS ACCORDED EXISTING PARTICIPANTS

LEGISLATED CHANGES – NEW ENTRANTS

(Source: National Conference of State Legislatures “Highlights of State Pension Reform in 2012” (August 2012))



Changes Have Been Made in **Ten** States Affecting **New Entrants** Entering on or after a Specified Date:

New York - April 1, 2012

South Carolina - July 1, 2012

Wyoming - September 1, 2012

Michigan - September 4, 2012

Alabama - January 1, 2013

California - January 1, 2013

Louisiana - July 1, 2013

Ohio - July 1, 2013

Virginia - January 1, 2014

Kansas - January 1, 2015

LEGISLATED CHANGES – NEW ENTRANTS

(Source: National Conference of State Legislatures “Highlights of State Pension Reform in 2012” (August 2012))



Some or all of the following DB design changes apply to new entrants in **five** states (Alabama, California, New York, South Carolina, and Wyoming):

- Increased Employee Contributions
- Increased Age Requirements for Unreduced Retirement Benefits
- Increased Reductions for Reduced Retirement Benefits
- More Restrictions on Pensionable Compensation
- Reduced Service Factor
- Less Favorable Final Average Salary Calculation
- IRC §415 Excess Benefit Plan in California Shut to New Entrants

EXAMPLE OF FINANCIAL IMPACT: NYSTRS



	TIER 4 (7/27/76-12/31/09)	TIER 5 (1/1/10-3/31/12)	TIER 6 (starting 4/1/12)
EMPLOYEE CONTRIBUTION RATE	3% (10 yrs. only)	3.5%	3-6% (rate depends on comp)
LONG -TERM EXPECTED EMPLOYER COST (% OF PAY)	10.9%	7.9%	4.6%
LONG -TERM EXPECTED EMPLOYER/ EMPLOYEE SPLIT	89/11	69/31	49/51

LEGISLATED CHANGES – NEW ENTRANTS

(Source: National Conference of State Legislatures “Highlights of State Pension Reform in 2012” (August 2012))



In Virginia, a **Hybrid DB/DC Plan** is being established for new entrants:

- 4% Employee DB Contribution
- 1% DB Service Factor

- 1% Mandatory Employee DC Contribution
- 1% Employer Match of Mandatory DC Contribution
- Total Employer DC Matches Capped at 3.5% on Total Employee Contributions of 5% or More
- Full Vesting of Employer Contributions After 4 Years of Continuous Membership

LEGISLATED CHANGES – NEW ENTRANTS

(Source: National Conference of State Legislatures “Highlights of State Pension Reform in 2012” (August 2012))



In Kansas, a **Cash Balance Plan** is being established for new entrants:

- 6% Employee Contribution
- 3-6% Employer Credit Depending upon Accrued Service
- 5.25% Guaranteed Minimum Interest Credit; Possible Additional Credits Depending upon Investment Experience
- 5 Year Vesting of Employer Credits
- Account Balances Annuitized at Retirement with Employee Option to Cash Out Up to 30% of Account

LEGISLATED CHANGES – NEW ENTRANTS

(Source: National Conference of State Legislatures “Highlights of State Pension Reform in 2012” (August 2012))



Louisiana has also adopted a **Cash Balance Plan** for new entrants:

- Mandatory for Post-Secondary Employees
- Optional for Other Educational Employees
- 8% Employee Contribution
- 4% Employer Credit
- Interest Credit 1% Below Actuarial Rate of Return; Possible Additional Credits Depending upon Investment Experience
- 5 Year Vesting of Employer Credits
- Account Balances Annuitized at Retirement with Employee Option to Take Partial Lump Sum

LEGISLATED CHANGES – NEW ENTRANTS

(Source: Michigan Legislative Website)



Michigan-

New entrants must **choose** between the **existing hybrid plan** (established for those joining between July 1, 2010 and September 4, 2012) **or** a **DC plan** which provides for 50% employer matching contribution for employee contributions of up to 6% of salary

LEGISLATED CHANGES – NEW ENTRANTS

(Source: Ohio STRS Website)



Ohio -

- Eligibility period for disability increased from 5 to 10 years
- Eligibility period for survivor benefits increased from 1.5 to 5 years
- Periods for applying for disability and survivor benefits reduced
- Changes also affecting existing participants discussed below

BENEFIT ACCRUALS OF EXISTING PLAN PARTICIPANTS ENJOY VARYING DEGREES OF LEGAL PROTECTION

(Source: Alicia Munnell and Laura Quinby “Legal Constraints on Changes in State and Local Pensions” Center for Retirement Research (August 2012))



	PAST AND FUTURE	PAST AND MAYBE FUTURE	PAST ONLY	NONE
STATE CONSTITUTION	3 STATES	1 STATE	3 STATES	
CONTRACT	15 STATES	7 STATES	12 STATES	
PROPERTY	2 STATES	3 STATES	1 STATE	
PROMISSORY ESTOPPEL	1 STATE			
NONE				2 STATES

LEGISLATION - EXISTING PARTICIPANTS

(Source: National Conference of State Legislatures "Highlights of State Pension Reform in 2012" (August 2012))



Changes Were Made in **Seven** States Affecting **Existing DB Participants**:

South Carolina - Employee contributions have been increased and service credit purchases have been mandated to be actuarially neutral

Virginia - Various benefit reductions have been made for members who are not vested on January 1, 2013

Wyoming - Discretionary post-retirement benefit increases have been discontinued until the plan is fully funded

LEGISLATION - EXISTING PARTICIPANTS

(Source: CALSTERS Website)



California -

- No earnings permitted in first 180 days of retirement
- Felons made subject to benefit forfeiture
- Retroactive increases in benefits prohibited
- Employer and employee contribution holidays prohibited
- Purchase of “airtime” prohibited

LEGISLATION - EXISTING PARTICIPANTS

(Source: KPERS Website)



Kansas -

If the IRS approves, participants entering prior to July 1, 2009 must elect to either (1) maintain their current contribution rate but drop to a 1.40 service factor for future service, or (2) have their contribution rate increased to 6% for future service but also get a .10 increase in their service factor; if no approval, option 2 is imposed

Participants who entered between July 1, 2009 and January 1, 2015 received a .10 increase in the service factor for all service but lost the COLA.

New law also provides for the Kansas Public Employees' Retirement System to eventually receive the full actuarially required contribution

LEGISLATION - EXISTING PARTICIPANTS

(Source: Source: National Conference of State Legislatures "Highlights of State Pension Reform in 2012" (August 2012))



Michigan -

Members who joined prior to July 1, 2010 must choose one of the following options to take effect in December 2012:

- Increase contribution rate and maintain a 1.5% multiplier
- Maintain current contribution rate but drop to 1.25% multiplier for future years of service
- Freeze existing benefits and move to a DC plan with 4% employer contribution for future service

New law also has provisions relating to health insurance benefits

LEGISLATION - EXISTING PARTICIPANTS

(Source: OHIO STRS Website)



Ohio -

Beginning July 1, 2013:

- Phased increase in participant contribution rate from 10 to 14%
- 2% COLA delayed until fifth anniversary of retirement for new retirees (with existing retirees missing one year of COLA)

Beginning January 1, 2014 (subject to a limited grace period):

- Subsidies for purchase of service credit eliminated

Beginning August 1, 2015:

- 5-year FAS instead of 3-year FAS
- Reduction in benefit formula
- Increases in age and service requirements for unreduced and reduced retirement benefits phased in over extended period

LEGAL PROTECTIONS FOR EXISTING PUBLIC PLAN PARTICIPANT BENEFIT ACCRUALS

(Source: Alicia Munnell and Laura Quinby “Legal Constraints on Changes in State and Local Pensions” Center for Retirement Research (August 2012))



	PAST AND FUTURE	PAST AND MAYBE FUTURE	PAST ONLY	NONE
STATE CONSTITUTION			MI	
CONTRACT	CA, KS	SC	VA	
PROPERTY	WY	OH		
PROMISSORY ESTOPPEL				
NONE				

SUMMARY OF LEGISLATION DISCUSSION



- Changes affecting new entrants in **ten** states, with a hybrid plan in Virginia, cash balance plans in Kansas and Louisiana, and a participant election in Michigan
- Changes affecting existing participants in **seven** states, with participant elections required in Kansas and Michigan and significant changes being rolled out in Ohio

COURT DECISIONS - BENEFITS



Williams v. Scott, Case No. 2011 CA 1584 (Second Circuit Court of Florida, March 6, 2012)

- The Florida Retirement System had been non-contributory up to July 1, 2011
- 2011 legislation implemented 3% employee contributions and also eliminated COLA for service credited after July 1, 2011
- Question presented: Did the legislation substantially impair the contractual rights of employees who were members prior to July 1, 2011?

COURT DECISIONS - BENEFITS



- Defendants argued changes were consistent with a prior Florida Supreme Court decision allowing the Legislature to alter benefits accruing for future service
- The court disagreed, holding the changes were “qualitative changes to the plan” which changed the fundamental nature of the plan
- The court also held the changes had a substantial impact on employee future benefits and the state had other reasonable alternatives for shoring up the system
- Florida Supreme Court heard argument on appeal of this decision on September 7, 2012

COURT DECISIONS - BENEFITS



Tice v. State of South Dakota, Civil No. 10-255 [unreported decision] (Circuit Court of South Dakota, April 11, 2012)

- Statute governing South Dakota Retirement System provided for enhanced retiree benefits based upon earnings in excess of actuarial assumed rate
- 2010 legislation reduced the improvement factor
- Question presented: Did the legislation represent a substantial impairment of a contractual relationship?
- Court answered no, reaching a result similar to the result in Minnesota and Colorado COLA cases decided in 2011

COURT DECISIONS - BENEFITS



- Legislation does not create private contractual rights absent a clear statement of intent to do so; here no such statement
- Reduction in COLA was appropriate to protect the financial integrity of the fund for the benefit of all participants and retirees
- Finding a contractual right would encourage Legislature to eliminate all COLA-type benefits going forward
- Court also held no property right to “forever 3.1% COLA”

COURT DECISIONS - BENEFITS



Cherry v. Mayor and City Council of Baltimore, Civil Action No. MJG-10-1447, 2012 U.S. Dist. LEXIS 134772 (D. Md., September 20, 2012)

- 1983 ordinance allowed for a skim of “excess” investment earnings to fund additional variable benefits for police and fire retirees
- 2010 ordinance replaced the variable benefit with a tiered COLA
- The court had already ruled the ordinance constituted a substantial impairment of vested contractual rights
- Question presented: Was the ordinance nonetheless justified as reasonable and necessary to serve an important public purpose?

COURT DECISIONS - BENEFITS



- The court held the ordinance served an important public purpose because it restored the actuarial soundness and sustainability of the plan, while ensuring the financial integrity of the City
- The ordinance, however, was not “necessary” in that it impaired the contractual rights of some participants far more drastically than it did others
- The court suggested implementation of a uniform fixed percentage annual COLA might have been considered “reasonable and necessary”

COURT DECISIONS - BENEFITS



In re Request for Advisory Opinion Regarding Constitutionality of 2011 PA 38, 490 Mich. 295 (2011)

- Question presented: Does the Michigan constitutional guarantee of public employee pension benefits bar the legislature from reducing or eliminating a long-standing statutory exemption of public employee pensions from state income tax
- According to the majority in a 4-3 decision, the exemption was not an “accrued financial benefit” protected by the Michigan constitution

COURT DECISIONS - BENEFITS



- Nothing in the statute indicated the legislature intended to make the exemption contractual, rather than simply an expression of public policy
- Withdrawing the exemption for employees far from retirement, while keeping it for current retirees or employees close to retirement, did not violate equal protection
- One dissenter argued the exemption had always been understood to partially compensate public employees for lower compensation, while another argued taking the exemption away had the same net financial impact as cutting benefits

COURT DECISIONS - BENEFITS



NYS Office of Victim Services v. Raucci, 97 A.D.3d 235 (3d Dep't 2012)

- Question presented: Does a plan anti-assignment provision prevent crime victims from tapping a perpetrator's public employee pension under New York's "Son of Sam" law?
- Holding: the more recently enacted "Son of Sam" law provisions controls over the older anti-assignment provision

COURT DECISIONS - BENEFITS



- The court acknowledged the anti-assignment clause protects pension payments, even after they have been paid to a retiree
- However, the court found no intent in the “Son of Sam” law to exempt public employee pension benefits from victim claims
- The court did not explicitly discuss the New York’s constitutional guarantee of public employee pension benefits, although the court appeared to suggest the claims of crime victims represented a permissible “limited exception” to the anti-assignment clause
- New York’s highest court has accepted an appeal of this decision

COURT DECISIONS - TRUSTEES



White v. Public Employees Retirement Board, 351 Ore. 426
(2011)

- Certain participants challenged a decision of the board of the Oregon Public Employees Retirement System to settle a suit by employers over employer contributions
- Plaintiffs argued it would have cost little to pursue an appeal which, if successful, would have been beneficial to them

COURT DECISIONS - TRUSTEES



- According to the court, trustees have the same obligation with respect to litigation as in all other matters, to act with prudence, loyalty and impartiality
- The board could reasonably believe it would not prevail on appeal and reaching an immediate settlement would have distinct administrative advantages, as well as help protect the long-term viability and stability of the fund
- The board could consider the benefits to participants generally and not just the interests of the plaintiffs whose own benefits would have been improved, had the appeal been successful

COURT DECISIONS - TRUSTEES



Stapleton v. Public Employees Retirement Assn., Case No. 11CV6530 (Colorado District Court, April 3, 2012)

- State treasurer who is an *ex officio* member of the system board requested certain information about system retirees receiving the highest benefits
- “[A]s to what I plan to do with the data I really cannot tell you” – “This is my prerogative”
- State treasurer sued for a mandatory injunction when the board denied his request

COURT DECISIONS - TRUSTEES



- The court began by noting the state treasurer has the same fiduciary duties as all other board members
- The state treasurer's statutory duties regarding public funds do not extend system trust funds
- Because the information requested is confidential under law, any request for such information by a trustee must be reasonably calculated to further the interests of system members and beneficiaries
- The state treasurer failed to articulate any legitimate reason for his request under that standard



QUESTIONS?