# EPMC, PEPRA, PERS and PEMHCA – Controlling Employee Pension and Retiree Medical Benefit Costs

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**Notes:**

# EPMC, PEPRA, PERS and PEMHCA, LOL OR OMG?

## Controlling Employee Pension and Retiree Medical Benefit Costs

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### OVERVIEW

There are a lot of acronyms to deal with in the law. Public sector retirement law is no exception. Despite passage of the California Public Employees' Pension Reform Act ("PEPRA") in 2012 (which became effective on January 1, 2013), public sector employers continue to struggle with the escalating costs of retirement benefits negotiated years (and sometimes decades) earlier. PEPRA may ultimately prove to be the law that helped limit the cost of retiree benefits. However, the full effect of PEPRA will be felt many years from now. Meanwhile, the cost of retirement benefits previously negotiated continues to increase and mitigate any cost savings that PEPRA produces.

### EPMC

EPMC stands for "Employer Paid Member Contributions" and means exactly what it says. It is an employment benefit provided by some employers in which the employer agrees to pay some or all of the statutorily required employee contribution to the CalPERS system. It is an employment benefit as it increases employee take home pay during employment. Also, the level of EPMC provided, if at all, is a matter for negotiation. It can increase up to the maximum (7-9%, depending upon the applicable benefit formula), or be reduced to zero; and is treated like any other employment compensation or benefit, such as salary, uniform allowance, vacation or


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the like. The mere act of providing EPMC does not make it a retirement benefit, and it is not vested absent unusual language making it vested.

PEPRA did not change any of the rules regarding EPMC for classic members (i.e., generally, retirement system members prior to January 1, 2013, the effective date for PEPRA). However, new members must pay at least 50% of the actuarially determined normal cost and no EPMC is allowed. CalPERS determines the normal cost for a particular benefit. CalPERS defines normal cost as “the annual cost of service accrued for the upcoming fiscal year for active employees. The normal cost should be viewed as the long-term contribution rate.”

Some employers chose to not only pay all or part of the employee contribution, but enhance that benefit by reporting the value of the EPMC paid to CalPERS as additional compensation, which increases the base upon which retirement benefits are calculated. While the level of EPMC is not vested, employees whose EPMC is reported as compensation, are hit twice when EPMC is reduced or eliminated. First, their take home pay is reduced during employment as withholding of the statutorily required employee share increases. Second, their retirement benefits may be less than they would have been before the reduction of EPMC (depending on whether they retire close in time to the reduction, or later). For this second reason, employees often assert that the reduction of EPMC that is reported as compensation impairs a vested right. However, at least one published court decision holds (in a non-CalPERS context) that no impairment occurs when EPMC is reduced. *San Diego Police Officers' Association v. San Diego City Employees' Retirement System*, 568 F.3d 725 (9th Cir. 2009). No court has addressed the issue whether an elimination of the reporting of EPMC as compensation, with no reduction of the amount of EPMC paid, impairs a vested right. As will be shown below


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in the discussion of retiree medical benefits, there is a trend in the case law right now making it more difficult to prove a retirement benefit is vested and immune from impairment by the employer. It is not clear how far that line of cases will go in dealing with retiree benefits outside of retiree medical.

## COST-SHARING

The opposite of EPMC is cost sharing. This is where the employer and employees agree that the employees will pay part of the employer's fluctuating employer rate to the retirement system. This may occur in conjunction with a reduction of EPMC to zero or with no reduction at all. Many times, cost sharing is agreeable to employees in lieu of a reduction in EPMC, especially where the EPMC is reported as compensation. Cost sharing allows the employer to achieve cost savings approximately the same as an equivalent reduction of reportable EPMC (but usually less than a commensurate reduction of EPMC). However, where cost sharing is begun when there is no reduction in EPMC, the employees continue to receive EPMC, and where it is reportable as compensation, they preserve their retirement base and their future retirement benefit levels. The employer receives cost savings in exchange.

Cost sharing became easier after PEPRA. The employer and employees are no longer limited in the amount of the employer contribution that employees can agree to pay. As was true pre-PEPRA, cost sharing may not be imposed. Also, there are at least two ways to structure a cost sharing arrangement for CalPERS agencies. First, the agency's CalPERS contract can be amended. This requires cost sharing to apply to all employees in a membership (e.g., all miscellaneous) class. Because a membership class may include more than one bargaining unit, negotiations are more complicated. However, this method has some advantages to employees (e.g., all extra employee contributions are considered member contributions and are included in the member's CalPERS account; and possible tax advantages such as the pre-income tax treatment). Second, an employer and an individual bargaining unit can agree to cost sharing in a collective bargaining agreement. This cost sharing does not involve a CalPERS contract amendment; nor does it need to involve other bargaining units or unrepresented employees. The advantages to the employees obtained by the CalPERS contract method are lost (although the tax issues are likely still a gray area.)

After PEPRA, employers and employees can agree that new members pay more than the 50% of normal cost employee contribution mandated by PEPRA. If there is such an agreement, however, the higher contribution rate must also be applied to unrepresented and management level new members. At this point, there is neither administrative guidance nor court decisions that would indicate what advantages, if any, this method of increasing employee costs has over the more traditional cost sharing methods described above.

## PART-TIME EMPLOYMENT

With the coming penalties for employers subject to, but not in compliance with, the Affordable Care Act, employers have been increasingly looking to limit employees' hours. However, even if an employer can structure work schedules to avoid ACA liability, that does not translate to a savings in retirement costs. While the main weekly threshold for ACA liability is 30 hours, an employee can qualify for CalPERS membership with as little as 20 hours averaged per week. Also, there is a rule that once an employee is a CalPERS member, the employee remains a CalPERS member. Therefore, reducing an employee's hours to avoid ACA liability will not change the existing employees' CalPERS membership status. Moreover, when recruiting for part-time positions, which the employer has budgeted to be non-CalPERS positions, employers must ensure that the person they hire is not a CalPERS member. A person who is a CalPERS member brings that status to the new part-time position. At this point in time, there is no prohibition against inquiring as to the CalPERS status in the hiring process.


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## RETIREE MEDICAL AND VESTED BENEFITS

When the California Supreme Court held, in the Retired Employees Association of Orange County, Inc. ("REAOC") case [1] that it was possible for vested rights to be implied (as opposed to expressly written into a contract) many employers were concerned that this would open up a Pandora's Box of potential new, enforceable claims for unwritten vested retirement benefits. While REAOC may have prompted additional litigation in this area, the trend of the cases is decidedly employer friendly, setting a very high threshold for employees to successfully assert vested rights to retiree medical benefits. It is not clear yet whether the same analysis utilized by the courts in retiree medical cases will also be used in cases involving retiree benefits unrelated to medical. However, there does not appear to be a very strong case for limiting these theories to retiree medical only.

For agencies that participate in the medical programs offered by CalPERS, which are subject to the Public Employees' Medical and Hospital Care Act ("PEMHCA"), restructuring employee and retiree medical benefits is more difficult than for non-PEMHCA agencies. There are several reasons for this. First, PEMHCA agencies are subject to the PEMHCA minimum and equal contribution rules. All eligible employees and annuitants (retirees who meet specific statutory requirements) must receive a contribution toward insurance from the employer of at least $119 per month in 2014. That amount increases each year and is published by CalPERS. The equal contribution rule prohibits the employer from making different contributions to employers and annuitants within the same "group or class." Group or class is defined in Government Code section 20636(e)(4), but generally applies to a bargaining unit or other logical

[1] *Retired Employees Association of Orange County, Inc. v. Orange County* (2011) 52 Cal.4th 1171.


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work related grouping. Therefore, it is possible to comply with PEMHCA's requirements by providing a contribution that is equal (and at or above the minimum) between employees and annuitants in one bargaining unit, but a different contribution than that provided to the employees and annuitants of a different bargaining unit. Second, PEMHCA prohibits an employer from offering a non-PEMHCA plan except for limited exceptions. Third, PEMHCA discourages employers from opting in and out of CalPERS' medical program. The window of opportunity to opt out is small. An employer resolution to opt out for the following calendar year must be filed with CalPERS within 60 days of CalPERS' announcement of the rates for the next calendar year. Given that health insurance is a negotiable subject, and that factfinding may extend the negotiations process, employers need to begin negotiating this subject well before the next year rates are even known (usually in the late spring). Also, for those agencies that do meet the timelines for opting out, the decision is irreversable for 5 years.

For those agencies that do not want to opt out of CalPERS medical or want to but cannot at least for the next calendar year due to the strict timelines, there are some strategies for controlling employee and retiree medical costs. An employer should strive to state the amount that it will contribute as a fixed dollar amount rather than as a percentage of the full premium. This will eliminate an automatic escalator of the employer's costs in the likely event that premiums rise. Instead, future increases can be negotiated. Employers should also state the amount of its PEMHCA contribution at an amount at or above the minimum for that year, and equal between employees and annuitants within a group/class. After doing so, additional contributions for employees can be put into a cafeteria plan. Retirees should not be able to assert that those cafeteria plan contributions must also be made for them under the equal contribution rules. Moreover, contributions in excess of the PEMHCA minimum can be made among groups of retirees to a Health Reimbursement Account. Employees and other retirees should not be able to use the equal contribution rule as the basis for claiming entitlement to those additional contributions.

## CONCLUSION

If you are not already familiar with the acronyms in the title of this paper, you probably will be eventually. PEPRA did not eliminate the need for continued diligence in controlling retirement costs. These issues will likely require additional litigation to address ambiguities in the law.


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