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Date: March 19, 2009
Reference No.:
Circular Letter No.: 200-016-09
Distribution: IV, V, VI, X, XII
Special:

Circular Letter

TO: **ALL CALPERS EMPLOYERS**

SUBJECT: **INFORMATION ON FURLOUGHS**

CalPERS has received numerous inquiries from employers who are considering implementing work furloughs. Given the level of interest, we are providing all employers the following information which documents the impacts of furloughs on member benefits, member/employer contributions, as well as the proper reporting of furloughed time.

Member Benefits

A member's retirement allowance is computed based on benefit formula, final compensation and service credit. The benefit formula is unaffected by a furlough. However, there may be an impact on final compensation and service credit.

Final Compensation:

Final compensation is the highest average annual compensation earnable over a 12 or 36 month period depending on member classification and bargaining unit, as set forth in the law. Compensation earnable is comprised of payrate and special compensation. Special compensation is a payment received for special skills, knowledge, abilities, work assignment, workdays or hours or other work conditions. A furlough does not change payrate, nor would it change special compensation in most instances when items of special compensation are paid as a flat dollar amount or a percentage of payrate. However, a furlough could reduce special compensation amounts that are paid as a factor of earnings (e.g., Reporting the Value of Employer Paid Member Contributions). Therefore, in some cases final compensation could be reduced, but only for members with earnings-based special compensation whose highest 12 or 36 month period at retirement includes furlough time.

Service Credit:

One year of service credit is granted for full time employment for any of the following: 10 months of service for persons employed on a monthly basis; 215 days of service for persons employed on a daily basis; or 1,720 hours of service for persons employed on an hourly basis.

Part time members accrue a ratio of service credit rendered toward the criteria outlined. Under a furlough plan, all members will accrue service at a slower rate during the fiscal year. However, since one year of service credit can be accrued in less than a year, full time members employed continuously throughout the fiscal year may be able to accrue a full year of service credit. For example, a full time member working continuously during a two day per month furlough plan would still earn a full year of service credit.

Part time members would generally have a reduction to the overall amount of service credit accrued. The overall reduction will depend upon the percent of full time normally worked and the number of furlough hours.

Members with appointments of less than 12 months may see an impact. In addition, members who take a leave of absence, or are hired or separate from service during a furlough plan, may see a reduction to the overall amount of service credit accrued because of their slower accrual rate. Their service will be based on the ratio of service accrued up to the separation or leave date to the full time amount required.

Member/Employer Contributions:

The Public Employees' Retirement Law provides that member contribution rates are to be applied to actual earnings, not compensation earnable. Therefore, when the member contribution rate is multiplied by the furlough-reduced member earnings, it will result in reduced member contributions payable to CalPERS.

The employer contribution rates set by the CalPERS Board are a percentage of payroll, and thus tied to actual earnings. Therefore, a furlough that reduces payroll would necessarily result in reduced employer contributions to CalPERS.

To the extent contributions received are less than would have been received had there not been furloughs, CalPERS may well be collecting less in both employer and member contributions than it would otherwise have received. However, this is not necessarily a problem. There will be other factors that impact liabilities. In the current economic environment, wage inflation may be less than assumed. This could cause gains that would not otherwise have been anticipated. Similarly, it is very likely that CalPERS will experience significant asset losses during the current fiscal year. The CalPERS funding policies have mechanisms to deal with all gains and losses, whether from member contributions, employer contributions, salary experience, investment experience or otherwise. CalPERS makes adjustments to future employer contribution rates as appropriate.

It is within the Board's power to determine, at any time, that an employer's contribution must be adjusted in order to avoid the creation of an unfunded liability that may result during a period when employer contributions are affected by furloughs. Reduced member and employer contributions due to furloughs could potentially create an

unfunded liability. For the State and schools, this may not be known until the June 30, 2009 valuation which is expected to be completed in May, 2010. For public agencies, it may not be known until October, 2010.

The Board has taken no action at this time to collect additional member and employer contributions due to furloughs, but reserves the right to change rates in the future.

Finally, please note that under standard actuarial processes at CalPERS, unfunded liabilities are amortized over 30 years in the employer rates and accrue interest at 7.75% per annum. Under Board policy, employers have the right to submit additional payments to CalPERS and may therefore choose to make contributions to CalPERS based on unreduced earnings.

Service Purchase Option:

There is no provision in the Public Employees' Retirement Law which allows members to purchase furlough time.

Proper Payroll Reporting:

Under a furlough plan, employers should continue to report the full time pay rate for their members. They should also report the actual earnings as they have been reduced due to the furlough.

CalPERS will also be issuing a separate circular letter to provide you with information regarding the impact of layoffs in the near future.

If you have any specific questions about furloughs as they relate to CalPERS, please contact the CalPERS Employer Contact Center at **888 CalPERS** (or **888-225-7377**).

Lori McGartland, Chief
Employer Services Division