OCTOBER 2020

INSIGHT

Pension Plans Legislative Update

IN THIS ISSUE

While Washington's attention has mostly shifted to the nomination of 7th Circuit Court of Appeals Judge Amy Coney Barrett to the Supreme Court, House Speaker Nancy Pelosi (D-CA) and Treasury Secretary Steven Mnuchin have been attempting to reach a deal on another COVID-19 stimulus relief package. Those talks failed to reach a deal prior to the expiration of the payroll support provided to U.S. airlines earlier this year, likely sending tens of thousands of Americans to the unemployment rolls.

On October 1, 2020, House Democrats passed a new $2.2 trillion COVID-19 relief package. The bill, known as HEROES 2.0, restates many Democratic priorities and includes over $400 billion in aid to state and local governments. However, HEROES 2.0 is unlikely to advance in the Senate.

It remains to be seen whether President Trump's subsequent COVID-19 diagnosis will change the calculus for stimulus negotiations. Speaker Pelosi and Secretary Mnuchin have some time to come to an agreement before the next deadline, as Senate Majority Leader Mitch McConnell (R-KY) announced that his chamber would not return to Washington until the week of October 19th in the wake of three Republican Senators – Thom Tillis (NC), Mike Lee (UT), and Ron Johnson (WI) – being diagnosed with COVID-19.

Federal Retirement News

- On August 6, 2020, Senator Sherrod Brown (D-OH) spoke on the Senate floor to urge his colleagues to take up a solution for the multiemployer pension crisis. Stakeholders had been hopeful that a solution could be included in this most recent round of coronavirus stimulus negotiations.

- On September 8, 2020, Senator Ted Cruz (R-TX) introduced the *RECOVERY Act* (S. 4537), a comprehensive economic relief bill. Among its many provisions are several retirement related items, including: 1) allowing participants in certain retirement plans to continue to contribute in 2021 and 2022, not to exceed the participant's unused 2020 contribution amount; 2) allowing certain retirement plan cash-outs to be treated as loans; and 3) indexing capital gains to inflation.

- On August 21, 2020, Representative Brad Schneider (D-IL) introduced the *Preserving Employee Retirement Savings Act of 2020* (H.R. 8083) to establish a temporary 20% tax credit for employers that continue to offer matching retirement contributions during the COVID-19 pandemic.

- On July 22, 2020, Senators Mark Warner (D-VA) and Steve Daines (R-MT) introduced the *Emergency Portable Benefits for Independent Workers Act* (S. 4276) to appropriate $500 million to the Department of Labor to help states to create portable benefits programs for independent workers. The funds would also go to help states modernize their unemployment insurance computer systems.

Public Pension Funding Challenges During COVID-19

The economic shock of COVID-19 has left state governments scrambling to plug unexpected budget holes. Tax revenues are down while spending is on the rise. Although the federal government gave roughly $150 billion in aid to state and local governments this year through the Coronavirus Aid, Relief and Economic Security (CARES) Act, states continue to debate ways to rectify deficits. Historically, states tend to reduce or defer pension funding in times of economic crisis, and the COVID-19 induced recession is following that pattern.

Examples of this trend can be seen throughout the country. Some states are addressing the issue through cuts. In Colorado, legislators proposed eliminating a $225 million pension payment from the state budget, just two years after passing a reform package aimed at lowering the state's unfunded liability. By some estimates, this would result in a $990 million long-term loss to the pension fund. Other options discussed in the state included delaying automatic contribution increases and shifting some of the employer contributions from employers to employees. Employees are facing either higher contributions in the immediate, or the prospect of increased long-term underfunding of their retirement plan. Similarly, the Oklahoma legislature voted to override the governor's veto of a budget bill that cut millions from state public pension funds. However, many states have already budgeted for the next fiscal year and, therefore, shortfalls may continue to develop over time.

States are also discussing cutting additional funding or delaying payments to pension plans. California Governor Gavin Newsom proposed eliminating $2.4 billion in supplemental payments to the California Public Employee Retirement System (CalPERS) and the California State Teachers' Retirement System (CalSTRS). In addition, South Carolina delayed pension contribution increases that were due to go into effect this year. Furthermore, New Jersey is deferring its 2021 pension payment until later in the year.

Oregon lawmakers voted to fill the state's budget gap by sweeping special funds earmarked for paying down pension liabilities. These funds were only recently upheld in *James v. State of Oregon*, as described in detail in the article on page 4. They consist of employee contributions diverted from defined contribution accounts to shore up the state's defined benefit plan. Although the Oregon Legislature raided reserve funds and cut $362 million in general fund spending, it did not cut or freeze state employee pay.

However, many states are considering drastic changes to state employment. For example, Nevada established a hiring freeze, instituted state employee furloughs of 6-12 days, tapped budget reserves, and made broad cuts in state agency budgets. Nevada's Governor released a report clearly outlining the reasons for personnel cuts, noting, "The inescapable nexus between the structure of Nevada's economy and the structure of its fiscal system suggest Nevada's economic crisis will continue to manifest as a fiscal crisis at the state and local levels well into Fiscal Year 2021." The Governor's report cited the failure of Congress to pass meaningful state and local government aid post the CARES Act as a reason that states around the country will "be forced to take deep cuts in services and programs…" Similarly, Alabama, Delaware, Michigan, New Mexico, Rhode Island, Utah and Wyoming instituted state employee furloughs, pay cuts and freezes, or layoffs.

States are also increasing employer contributions in order to fill budget gaps. Employer contributions to the Florida Retirement System—the nation's fourth largest public plan—are on the rise by over $400 million. This year, legislation was passed with broad support to chip away at the state's $11 billion unfunded pension liability. The state revised employer contributions upward based on its 2019 Actuarial Valuation Report. More than half of the increase comes from public school districts. Similarly, contribution rates for the New York Employees' Retirement System were increased from 14.6% to 16.2% of payroll for the next fiscal year. In addition, the New York Police and Fire Retirement System increased employer contributions from 24.4% to 28.3%. Evolving mortality assumptions and market volatility were given as explanations for these changes.

Market volatility, COVID-19 uncertainty, and declining revenues will likely continue to plague states for the near future. If the Great Recession is a guide, discussions around limiting pension payments and benefit changes will remain as well.

Arizona Supreme Court Rulings on Vacation and Sick Leave Payouts

In July 2020, the Arizona Supreme Court sided with the City of Phoenix in the decisions for a pair of cases. The Court upheld changes to the City's pension plan that prohibited including payouts for future accruals of vacation and sick leave in the calculation of pension benefits.

In *Piccioli v. City of Phoenix* ("*Piccioli"*), plaintiffs challenged a 2012 change to City benefit regulations removing from the definition of pensionable compensation of all payouts for future accrued sick leave. Plaintiffs argued that this was an unlawful diminishment and impairment of benefits under the Contract and Pension Clauses of the Arizona Constitution. The lower court found for the employees, ruling that unused sick leave is non-monetary compensation that was set by the City Council via collective bargaining agreements. Further, the court noted that it was commonly and widely known that accrued sick leave would be included in final average compensation. The Court of Appeals reversed, holding that the City was not compelled under the terms of the pension plan to include lump-sum, irregular cash payouts for accrued sick leave in determining pension benefits. It further noted that the City did not violate constitutional principles by ending the practice prospectively. The Supreme Court affirmed the Appeals Court decision.

Similarly, the Arizona Supreme Court held in *American Federation of State County and Municipal Employees, AFL-CIO, Local 2384 v. City of Phoenix* ("*AFSCME*") that terms of the City's pension plan did not require future accrued vacation leave payouts to be used in calculating employee pensions. Similar to *Piccioli*, the City prospectively prohibited vacation leave accrued after July 1, 2014 from applying to current employee pension benefit calculations. Plaintiffs again argued unlawful diminishment and impairment of a longstanding benefit. The lower court found for the City in this case, holding that compensation is defined as salary or wages that is paid at regular, periodic intervals; thus, one-time vacation payouts do not constitute compensation for the purposes of benefit calculations. The Appeals Court and Supreme Court affirmed.

California Supreme Court Ruling on Pension Reform

On July 30, 2020, the California Supreme Court issued a long-awaited ruling regarding California's 2013 pension reform legislation, known as the California Public Employees' Pension Reform Act ("PEPRA"). The Court's opinion in *Alameda County Deputy Sheriff's Association v. Alameda County Employees Retirement Association* ("*Alameda"*) gave a limited win to pension reformers who have taken aim at the "California Rule"—the vested rights doctrine developed through California case law, which treats pension benefits as deferred compensation that cannot be impaired after the start of employment.

At issue in *Alameda* was the exclusion of certain items from the definition of compensation used to calculate pension benefits, including: accumulated leave beyond the final compensation period; payments for services rendered outside normal working hours; pension benefit enhancements; and sums paid post-termination. This definitional change was one of several changes made by PEPRA, which also capped pensions and raised the retirement age for new employees.

The plaintiffs in *Alameda* argued that, as legacy employees (those hired prior to the passage of PEPRA), they had a constitutional, contractual, and equitable right to have their benefits calculated without regard to the PEPRA changes under the California Rule and preexisting settlement agreements. The state argued that PEPRA was needed to tackle unfunded pension liabilities, which ultimately drain revenue from schools and public services.

However, the Court did not address the broad issue of budget liabilities. The opinion notes that PEPRA was, "enacted for the constitutionally permissible purpose of closing loopholes and preventing abuse of the pension system…it would defeat this proper objective to interpret the California Rule to require county pension plans either to maintain these loopholes for existing employees or to provide comparable new pension benefits that would perpetuate the unwarranted advantages provided by these loopholes." In other words, legislation that alters the calculation of pre-existing benefits may be permissible if it is done for the purpose of preventing abuse, such as pension spiking. The court noted that counties are required to implement the legislative changes in PEPRA, despite settlement agreements that conflict with the law.

However, *Alameda* did not address broader questions around the validity of the California Rule. It also did not take a position on whether pension reform for the sole purpose of relieving budgetary pressure would be upheld in the future. Thus, although pension reformers retained the ground gained in passing PEPRA, the Court's narrow ruling did not necessarily make way for substantial future pension reform. Moving forward, several cases held in abeyance while the Court heard *Alameda* await consideration.

Oregon Supreme Court Rules Pension Reforms Constitutional

In *James v. State of Oregon* ("*James*"), the Oregon Supreme Court unanimously upheld a reform package passed by the legislature that altered employee contributions and imposed a cap on the salary used to calculate member benefits.

In 2019, the Oregon Legislature passed Senate Bill (SB) 1049, which redirects 2.5% of employees' mandatory 6% contribution from an individual defined contribution account to an Employee Pension Stability Account ("EPSA"). The diversion of employee contributions into the EPSA occurs in years when the defined benefit plan is less than 90% funded and will be used to help fund the member's pension benefit. The second challenged component of SB 1049 was a salary cap used for determining pension benefits. The legislature set that cap at $195,000 for 2020; the cap will be indexed for inflation.

Plaintiffs argued in *James* that SB 1049 impaired their contractual rights and was an unconstitutional taking of property without just compensation under the Oregon Constitution. They noted that employees' defined contribution savings could be reduced by 5% to 14%. The state responded that the reforms do not impair benefits that members have already earned, but instead make prospective changes.

The Supreme Court upheld the reforms and agreed with the State in this case. The Court noted that the "challenged amendments do not operate retrospectively to decrease the retirement benefits attributable to work that the member performed before the effective date of the amendments." Further, the Court states that employees did not have a preexisting statutory promise that benefits would not be changed prospectively.

Notably, EPSA funds were subsequently used to shore up Oregon's budget gap this year in the wake of COVID-19.

HHS Proposed Rule and DOL Final Rule on Good Guidance

In August 2020, the Departments of Labor (DOL) and Health and Human Services (HHS) issued separate rules regarding their procedures for issuing "subregulatory" guidance (i.e., guidance issued outside of the formal notice and comment process).

DOL and HHS set forth the new rules in response to President Trump's Executive Order 13891, "Promoting the Rule of Law Through Improved Agency Guidance Documents." The executive order opined that federal agencies have sometimes used subregulatory guidance "inappropriately" in an effort to regulate the public without following rulemaking procedures, and that the public often lacks sufficient notice of guidance documents. To address these issues, the executive order requires federal agencies to issue regulations setting forth new processes and procedures for issuing guidance documents.

The key elements included in both DOL's final rule and HHS's proposed rule on this subject include:

- **Definition of Guidance.** The regulations define "guidance" using the definition from the executive order, meaning a "guidance document" is "an agency statement of general applicability, intended to have future effect on the behavior of regulated parties that sets forth a policy on a statutory, regulatory, or technical issue or an interpretation of a statute or regulation." The regulations add that guidance can come in many forms, including "letters, memoranda, circulars, bulletins, or advisories, and may include video, audio, and web-based formats."

- **Exceptions.** The regulations establish a variety of exceptions as to what constitutes a guidance document. These include rules promulgated pursuant to notice and comment under the Administrative Procedure Act (APA), rules exempt from rulemaking requirements under the APA, decisions of agency adjudications, internal guidance not intended to have substantial future effect on the behavior of regulated parties, legal briefs, and pre-enforcement rulings directed to a particular party, among other exceptions.

- **Procedures for Issuing Guidance.** The regulations require that, going forward, a guidance document must: 1) include a statement that it does not bind the public; 2) avoid using mandatory language (e.g., "shall," "must," "required," or "requirement"); 3) be written in plain and understandable language; 4) prominently display the term "guidance"; 5) include a citation to the relevant statute or regulation; and 6) note if it is a revision to previously issued guidance.

- **Procedures for Significant Guidance.** The regulations also impose specific requirements for guidance considered "significant," which includes guidance that: 1) leads to an annual effect on the economy of $100 million or more or adversely affects in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities; 2) creates a serious inconsistency or otherwise interferes with an action taken or planned by another agency; 3) materially alters the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or 4) raises novel legal or policy issues. Generally, significant guidance must undergo at least a 30-day notice and comment period, be submitted for review to the Office of Management and Budget (OMB), undergo a regulatory impact analysis, and comply with the applicable requirements that would otherwise apply to regulations or rules.

- **Petitions to Withdraw or Modify Guidance.** The regulations also provide that any member of the public may petition an agency for withdrawal or modification of a guidance document issued by the agency. Upon review, the agency may decide to withdraw, modify, or retain the guidance document, but in any case, the agency must provide a written response to the petitioner within 90 days after receiving the petition.

While DOL issued its regulation as a final rule effective September 28, 2020, HHS issued its regulation as a proposed rule, with a comment period ending September 16, 2020.

The executive order also requires each agency to establish a single, searchable, indexed database that contains all guidance documents in effect from the agency. The executive order directs each agency "to review its guidance documents and, consistent with applicable law, rescind those guidance documents that it determines should no longer be in effect." It is understood that DOL and HHS went through this process in creating their guidance portals.

ACA Section 1557 Nondiscrimination Final Rule: Litigation Update

In August and September 2020, two federal courts set aside portions of a recent final rule revising the Department of Health and Human Services' (HHS) interpretation of Section 1557 of the Affordable Care Act (ACA), the nondiscrimination provision, as it relates to transgender individuals.

By way of background, in 2016, HHS promulgated a final rule that offered a variety of protections for transgender individuals, including explicit prohibitions on discrimination on the basis of gender identity or sex stereotyping, limits on religious entities invoking certain religious exemptions from providing treatment, and prohibitions on categorical coverage exclusions, among others (the 2016 Rule). In 2020, the Trump administration issued a new final rule revising or repealing the 2016 Rule in significant respects (the 2020 Rule). The two recent federal court decisions enjoin HHS from enforcing certain portions of the 2020 Rule, thus reinstating certain protections for transgender individuals included in the 2016 Rule.

Walker and Gentili v. Azar

On August 17, 2020, the District Court for the Eastern District of New York in *Walker and Gentili v. Azar* issued a preliminary injunction enjoining HHS from enforcing the 2020 Rule's repeal of the 2016 Rule's definition of discrimination "on the basis of sex," which explicitly prohibited discrimination based on sex stereotyping and gender identity. The plaintiffs, two transgender women, sought a declaration that the 2020 Rule was invalid under the Administrative Procedure Act (APA) and the Court should vacate the 2020 Rule in its entirety. In the meantime, the plaintiffs asked the Court to stay the 2020 Rule's effective date (which was August 18, 2020), and preliminarily enjoin HHS from enforcing it. The plaintiffs specifically argued that the injunction should be nationwide.

The Court concluded that the plaintiffs had standing to seek a stay and a preliminary injunction. Judge Block cited *Bostock v Clayton County*, holding that the 2020 Rule was contrary to *Bostock* and that HHS acted arbitrarily and capriciously in enacting it. In *Bostock*, the Supreme Court held that discrimination based on sex encompassed discrimination based on gender identity, and concluded that such discrimination "has always been prohibited by Title VII's plain terms," and that "that should be the end of the analysis." [1] The 2020 Rule took the position that "[t]he plain meaning of 'sex' under Title IX encompasses neither sexual orientation nor gender identity."[2]

The District Court stayed the repeal of the 2016 definition of discrimination on the basis of sex, and as a result, the definitions of "on the basis of sex," "gender identity," and "sex stereotyping" currently set forth in 45 C.F.R. § 92.4 will remain in effect. The preliminary injunction appears to apply nationwide, but *only* applies to the repeal of the 2016 definitions relating to discrimination "on the basis of sex." However, the plaintiffs have asked the Court to "confirm" that the preliminary injunction applies to the entire rule, but the Court has not yet issued any clarifying order. Therefore, it is possible that the court will revise its ruling to clarify that the *entire* 2020 Rule has been enjoined, but the current judgment does not appear to be that broad.

Whitman-Walker Clinic, Inc. v. HHS

On September 2, 2020, the District Court for the District of Columbia in *Whitman-Walker Clinic, Inc. v. HHS* preliminarily enjoined HHS from enforcing two portions of the 2020 Rule relating to sex discrimination.

Like the plaintiffs in *Walker and Gentili*, the plaintiffs in *Whitman-Walker Clinic* - a coalition of private health care facilities, service organizations, national associations of health professionals, and individual physicians - challenged the entire rule, including HHS's repeal of the 2016 Rule's definition of discrimination "on the basis of sex," which explicitly prohibited discrimination based on sex stereotyping and gender identity.

In a lengthy opinion, the court held that the plaintiffs were entitled to a nationwide injunction as to the repeal of the 2016 Rule's definitions relating to discrimination "on the basis of sex." The court also enjoined HHS from enforcing the Title IX religious exemptions incorporated into the 2020 Rule. However, the court did not set aside the 2020 Rule in its entirety.

[1] *See Bostock v. Clayton Cnty., Ga.*, 140 S. Ct. 1731 (2020).
[2] 85 Fed. Reg. 37,160, 37,194 (June 19, 2020).

Next Steps

Similarly, there are pending cases in the SDNY (*New York, et. al. v. HHS*) and Massachusetts (*BAGLY (Boston Alliance), et. al. v. HHS*) in which the District Courts have been asked to address the permissibility of the *entire rule*, including the language access provisions and/or the notice and tagline provisions (among other issues). Depending on the outcome of the pending cases, there is a possibility that another court will issue an injunction vacating the entire 2020 Rule.

DOL Amends FFCRA Regulations Following District Court Decision

On September 16, 2020, the Department of Labor (Department) published revisions and clarifications to its April 1, 2020 temporary final rule (Final Rule), which interpreted the emergency paid sick leave and expanded family and medical leave entitlements under the Families First Coronavirus Response Act (FFCRA). The revisions were in response to a district court decision finding certain portions of the Final Rule invalid.

By way of background, FFCRA created two new emergency paid leave requirements (together, FFCRA leave) in response to the public health emergencies arising out of COVID-19. The first, the *Emergency Paid Sick Leave Act* (EPSLA), entitles certain employees of covered employers to take up to two weeks of paid sick leave if the employee is unable to work for specific reasons related to COVID-19. The second, the *Emergency Family and Medical Leave Expansion Ac*t (EFMLA), permits certain employees of covered employers to take up to 12 weeks of expanded family and medical leave (ten of which are paid) if the employee is unable to work because he or she needs to care for a son or daughter whose school, place of care, or child care provider is closed or unavailable due to reasons related to COVID-19.

On April 14, 2020, the State of New York filed suit in the United States District Court for the Southern District of New York (District Court) arguing that four features of the Final Rule - 1) the "work-availability" requirement; 2) the definition of health care provider; 3) the provisions relating to intermittent leave; and 4) certain documentation requirements — unduly restricted paid leave. On August 3, 2020, the District Court held that certain provisions of the Final Rule were invalid.

In response, the Department published the revised rule, which reevaluated the four parts of the Final Rule that the District Court addressed in its opinion. First, the Department reaffirmed and explained the work-availability requirement under the Final Rule. The Final Rule had provided that FFCRA leave is only available if the employee has work from which to take leave. The revised rule reaffirms the work-availability requirement and provides a more robust explanation for its original reasoning regarding the work-availability requirement. The revised rule also clarifies that the work-availability requirement applies to all FFCRA leave (under the Final Rule, the Department had provided that the work-availability requirement only applied to certain qualifying reasons for leave under the EPSLA).

Second, the Department reaffirmed and explained the employer approval requirement for intermittent leave. The Final Rule permits intermittent leave (leave taken in separate blocks of time due to a single qualifying event, with the employee reporting to work intermittently during an otherwise continuous period of leave) in certain situations, but only with the employer's consent. The revised rule reaffirms that where the Department's regulations permit intermittent FFCRA leave, an employee must obtain employer approval to take such an intermittent leave. In its explanation, the Department noted that the consent requirement for intermittent leave is consistent with longstanding FMLA principles and that such a requirement promotes a balance between the employee's need for leave and the employer's interest in avoiding disruptions of business operations.

Third, the Department narrowed the definition of a "health care provider" that is exempt from FFCRA leave. Under the FFCRA, employers may exclude health care providers and emergency responders from FFCRA leave. Under the Final Rule, the Department defined "health care provider" expansively to include practically any employee whose employer provides health care services. The District Court held that the Department's definition was too broad, and that by focusing on the identity of the employer rather than the "skills, role, duties, or capabilities" of the employee, the Department was excluding certain employees of health care facilities whose positions do not relate to the provision of health care services. Thus, in the revised rule, the Department narrowed the definition of "health care provider" to only include employees who: 1) are health care providers under the FMLA regulations; or 2) are employed to provide "diagnostic services, preventative services, treatment services, or other services that are integrated with and necessary to the provision of patient care."

Finally, the Department clarified the timing for when an employee must provide documentation supporting a FFCRA leave request. The Final Rule requires that employees submit to their employer, prior to taking FFCRA leave, documentation indicating their reason for leave, the duration of the requested leave, and, when relevant, the authority for the isolation or quarantine order qualifying them for leave. The District Court held that the requirement that documentation be given "prior to" taking leave is inconsistent with certain unambiguous provisions under the statute that address notice requirements for FFCRA leave. Given the incompatibility, the District Court found that "the documentation requirements, to the extent they are a precondition to [FFCRA] leave, cannot stand." The revised rule clarifies that employees do not need to provide documentation prior to taking FFCRA leave. Instead, the employee may give the employer documentation to support the need for FFCRA leave as soon as practicable.

The revisions to the Final Rule were effective September 16, 2020 and apply until December 31, 2020, when the FFCRA leave provisions are set to expire.

About GRS

Founded in 1938, Gabriel, Roeder, Smith & Company (GRS) is a national actuarial and benefits consulting firm. GRS is dedicated to bringing clients innovative, sustainable solutions that the firm helps put into action. The firm supports the long-term success of pension, OPEB, and health and welfare benefit plans. Associates deliver high-quality services that reflect GRS' core values, which include professionalism and ethics in all aspects of business. The firm attracts the best talent in the industry by providing a collaborative work environment that respects the diversity and professional aspirations of our associates.

To locate a GRS office, please visit our website at: www.grsconsulting.com.