# RETIREMENT PRIMER FOR CALIFORNIA COMMUNITY COLLEGE PART-TIME FACULTY

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August 2007

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# INTRODUCTION

*I'm too young to worry about retirement. I don't understand that stuff. I'll never be able to retire because I'm a part-timer.* These are typical part-timer responses when asked about their retirement plans. But most part-timers *will* eventually retire or stop teaching. Understanding how retirement plans work and being able to estimate the amount of one's retirement benefits can help a part-timer prepare for that day.

It is highly unlikely that a part-timer's retirement benefits from teaching will provide enough income for retirement. Nonetheless, participating in some sort of retirement plan is usually better than participating in none at all. To make informed decisions, part-timers should understand their retirement options, understand how their chosen retirement plan(s) work, be able to estimate their benefits from their plan(s), and understand what, if anything, they can do to increase their retirement benefits. This primer will attempt to address those issues. Special attention is given to the California State Teachers' Retirement System Defined Benefit Program (CalSTRS DB) because a large number of part-timers are members of that retirement plan and because its benefit calculations are complex for part-timers.

For more information about the topics covered in this primer, you may wish to consult one or more of the following:

1. Social Security Administration at www.ssa.gov (website includes a calculator for estimating Social Security retirement benefits) or 1-800-772-1213;

2. CalSTRS Member Handbook (has lots and lots of information, includes a chapter on benefits for part-timers, will answer many of your questions, and is available free from CalSTRS at 1-800-228-5453);

3. CalSTRS at www.calstrs.com (website includes a calculator for estimating CalSTRS DB retirement benefits) or 1-800-228-5453;

4. CalSTRS workshop (for workshop descriptions, consult CalSTRS Member Handbook, and to register for a workshop, call 1-800-228-5453 or go to www.calstrs.com/workshops);

5. A CalSTRS benefits counselor, either face-to-face or over the phone (consult CalSTRS Member Handbook for information, state-wide locations, and phone numbers, but be aware that the counselor may not understand CalSTRS DB benefit calculations for part-timers);

6. Your Human Resources department;

7. Your retirement plan administrator (other than Social Security or CalSTRS); and/or

8. A financial advisor. (If you hire a financial advisor for help, conventional wisdom says that you should hire one who charges you a fee. Those who do not charge a fee earn commissions from investment products they sell and are less likely to be objective. Furthermore, very few financial advisors will understand CalSTRS DB benefit calculations for part-timers.)

# <u>1. WHAT TERMS DO YOU NEED TO UNDERSTAND?</u>

Before attempting to comprehend the complex world of retirement plans for part-timers, you need to understand a few basic terms.

A **defined benefit** retirement plan is what we usually think of as a “pension”. It is a retirement plan in which an employee’s <u>retirement benefit is defined in advance by a formula.</u> The formula is usually based on years of service, age at retirement, and final or highest salary. The benefit does <u>not</u> depend on the employee’s individual account balance at time of retirement. The benefit is <u>guaranteed for life</u> by the employer or a government entity, regardless of the amount of contributions or investment return. DB plans usually provide disability pensions, guaranteed death benefits, and cost of living adjustments (COLA). Funds are pooled and invested by professionals employed by the retirement plan.

A **defined contribution** retirement plan is one which works like a “401(k)” plan. It is a retirement plan in which the <u>retirement benefit is the employee’s account balance at time of retirement</u>, including the amount contributed and all earnings *and losses* on the account. There is <u>no</u> benefit defined by a formula and guaranteed for life. Only the contributions to the account are defined. The account balance can be taken as a lump sum or, in most cases, as a lifetime annuity <u>based on the account balance</u>. There are no disability pensions, guaranteed death benefits, or COLA. Funds are invested individually by plan participants.

A **cash balance** retirement plan is a hybrid plan with characteristics of both a defined benefit plan and a defined contribution plan. The retirement benefit is the employee’s individual account balance at time of retirement (similar to a defined contribution plan). But funds are pooled and invested by professionals employed by the retirement plan (similar to a defined benefit plan). And employees often receive a guaranteed rate of return each year (unlike either a defined contribution or a defined benefit plan).

Being **vested** in your retirement plan means having the right to receive retirement benefits. If you are not vested, you will not receive retirement benefits when you retire. (However, depending on the plan, you may receive a refund of your contributions to the plan.)

**Tax deferred** contributions to a retirement plan are not subject to income tax until retirement benefits are received.

An **annuity** is a right to receive payments (usually monthly) for life or for a fixed number of years in return for payment of a sum of money. Annuities are sold directly by life insurance companies or indirectly through other financial institutions. Note that retirement benefits from most defined contribution plans can be taken in the form of an annuity. This does not make them defined benefit plans. The amount of the periodic annuity payments still depends on the member’s account balance in the defined contribution plan at the time of retirement. This is different from a defined benefit plan in which benefits are based entirely on a formula and not dependent on a member’s individual account balance.

# 2. WHAT ARE YOUR RETIREMENT PLAN OPTIONS?

All part-timers must belong to either Social Security or to an "alternative" retirement plan. The options vary from district to district. Social Security is not always an option. No district allows part-timers to belong to Social Security and an alternative plan.

## A. Social Security

Some districts offer Social Security as an option for part-timers. Social Security is a defined benefit plan which provides a guaranteed lifetime pension. It also provides disability pensions, guaranteed death benefits, and COLA. It requires 40 calendar credits (previously calendar quarters) to vest. Retirement benefits are based on a complex formula using one's average annual earnings. Employee contributions are 6.2 percent and are *not* tax deferred. Employer contributions are also 6.2 percent. If not vested at retirement, a part-timer receives neither retirement benefits nor a refund of his or her contributions. The minimum retirement age is 62.

## B. CalSTRS Defined Benefit Program

All districts must offer the CalSTRS Defined Benefit Program ("CalSTRS DB") as an option for part-timers. (Full-timers must belong to CalSTRS DB.) Until recently part-timers were sometimes required to become members under certain circumstances, but legislation effective July 1, 2005, eliminates those requirements. So long as a part-timer is classified as "temporary" (i.e., teaches no more than a 60% load), membership in CalSTRS DB is no longer required. However, practically speaking, once a part-timer becomes a member, it will probably be very difficult to leave and to switch to a different retirement plan.

CalSTRS DB is a true defined benefit plan which provides a guaranteed lifetime pension. It also provides disability pensions, guaranteed death benefits, and COLA. It requires five full-time equivalent years of service credit to vest (discussed later). Retirement benefits are based on a formula. Employee contributions are 8 percent and are tax deferred. Employer contributions are 8.25 percent. The minimum retirement age is 55.

Because of the earnings made by CalSTRS during the 1990's, legislation was passed providing all members of CalSTRS DB teaching any time from 2001 through 2010 with a separate Defined Benefit Supplement (DBS) account. During those 10 years one-fourth of an employee's DB contributions (i.e., 2% of salary) goes into the employee's DBS account, along with contributions for service in excess of one year service credit. Interest is earned at a rate set by the Teachers' Retirement Board. At retirement the employee receives a lump sum representing the employee's DBS account balance at that time in addition to the normal DB lifetime benefit. If the DBS account balance is at least $3500, the benefit can be taken as an annuity. There is no reduction in the DB retirement benefit.

If a member of CalSTRS terminates CalSTRS-covered employment before retiring, he/she can request a refund of his/her contributions, plus accumulated interest, but not the district's contributions. Unless timely rolled over into an IRA or other qualified plan. refunds are taxable and, before age 59 ½, also subject to tax penalties.

## C. CalSTRS Cash Balance Program

Some districts offer the CalSTRS Cash Balance Program ("CalSTRS CB"). It is a "hybrid" plan (part defined benefit and part defined contribution) created specifically for part-timers because many part-timers were not able to vest in DB. Vesting is immediate in CB. The retirement benefit is the employee's individual account balance at time of retirement. There is no guaranteed lifetime pension. However, the employee is not responsible for investing his or her account, pays no management fees, and receives a guaranteed interest rate each year on his or her account. The interest rate is set each year by the CalSTRS Teachers' Retirement Board based on the 30-year Treasury rate, regardless of the performance of CalSTRS investments.

Employee contributions are tax deferred and are usually 4 percent. Employer contributions are usually 4 percent. Alternative rates may be bargained so long as the employer rate is at least 4 percent and the total contribution is at least 8 percent. For example, in Los Angeles the employee contributions are 3.75 percent and the employer contributions are 4.25 percent. The retirement benefit is a lump sum equal to the employee's account balance at time of retirement. If the balance is $3,500 or more, it may be taken in the form of an annuity. The minimum retirement age is 55. Unless rolled over into an IRA or other qualified plan, early withdrawals before age 55 are taxable and subject to tax penalties. There is a six month wait period to receive one's account balance if one terminates CalSTRS-covered employment before retirement. Disability benefits (requiring total and permanent disability) and death benefits are limited to the employee's account balance.

## D. Other "alternative" retirement plans

Some districts offer other retirement plans as an "alternative" to Social Security. These include PARS (Public Agency Retirement System), APPLE, PEAR, and Bencor. These are usually defined contribution plans or hybrid plans offered by private providers under contract with a district. The retirement benefit is the employee's individual account balance at time of retirement. The employee receives a guaranteed interest rate each year but only after the provider deducts management fees for its services. Because they usually require smaller contributions from employers than the CalSTRS DB plan, or even no contribution at all, they are attractive to districts. For example, employees in the PARS plan in Los Angeles contribute 3.5 percent while the employer contributes 4 percent.

## E. Additional options for part-timers with extra money to invest

Some districts offer a tax-deferred 403(b) retirement plan (Tax Sheltered Annuity or "TSA"). For information about various district 403(b) offerings, go to www.403bcompare.com. Some districts offer a tax-deferred 457 retirement plan. For information, contact your Human Resources Department.

Regardless of what districts offer, part-timers may also independently invest in an Individual Retirement Account (IRA). A traditional IRA offers tax-deferred investing, the scope of which depends upon income. A Roth IRA is not tax deferred, but all withdrawals are tax-free. Banks, credit unions, mutual fund companies, and other financial institutions offer IRA's. Tax deferred annuities can also be purchased from life insurance companies, either directly or through other financial institutions. Fees are charged by providers of these additional investment options. Fees for tax deferred variable annuities (other than 403(b) TSA's) are usually very high.

# <u>3. WILL YOU LOSE YOUR SOCIAL SECURITY BENEFITS?</u>

## <u>A. The Windfall Elimination Provision (WEP)</u>

Some part-timers are entitled to Social Security retirement benefits as a result of other employment. If so, those benefits may be *reduced* if benefits from an alternative retirement plan are also received. You probably won't lose all of your benefits, but you will probably lose part of them.  This is thanks to the nefarious *Windfall Elimination Provision* (WEP) passed by Congress during the Reagan administration.  It was supposed to prevent retirement windfalls for government agency employees who earned fat pensions from their government jobs and also earned Social Security benefits from other jobs.  Unfortunately it also applies to California community college part-timers (and full-timers) who do not contribute to Social Security while teaching.

**<u>How much will your Social Security benefits be reduced by the WEP</u>?** Contrary to what some people think, the WEP offset is not equal to your entire Social Security benefit.  For persons retiring in 2007 the maximum offset is $340 per month.  It is adjusted annually for inflation.  Furthermore, it cannot be more than one-half of the alternative pension monthly benefit.  Therefore the maximum offset for a person retiring in 2007 is <u>either</u> $340 per month <u>or</u> one-half of the retiree's alternative pension monthly benefit, whichever is *less*.  For example, if a person's alternative pension monthly benefit is $500 per month, then the maximum offset is $250.00 per month.

**<u>How does the WEP work</u>?** First of all, you aren't entitled to *any* Social Security retirement or disability benefits unless you have earned at least 40 credits (previously calendar quarters) at jobs where you paid Social Security taxes.  If you meet this requirement, then you are entitled to benefits.  However, your Social Security retirement benefits may be reduced (but not eliminated) if you also work for a government agency and contribute to an "alternative" retirement plan.  This includes all other retirement plans available to part-timers, including defined contribution plans and hybrid plans <u>such as CalSTRS CB</u>.

Social Security benefits replace a percentage of a worker's pre-retirement earnings.  The benefits are computed in such a way that lower-paid workers get a higher return than highly paid workers.  Monthly retirement benefits are based on the worker's average pre-retirement monthly earnings adjusted for inflation.  (Your annual SSA statement provides your earnings history.) For a worker retiring in 2007, the first $680 of average monthly earnings is multiplied by 90 percent; the next $3420 by 32 percent; and the remainder by 15 percent.

For persons who also receive an alternative pension, the 90 percent factor is reduced to <u>40 percent</u>**.** 90% of $680 is $612.  But 40% of $680 is only $272, <u>a reduction of $340</u>.  A person retiring in 2007 and subject to the full offset would have his/her monthly Social Security retirement benefit reduced by $340.

**<u>Are there exceptions to the WEP</u>**?  Part or all of the offset can be avoided if a worker has 21 or more years of "*substantial earnings*", as defined in a table, from jobs requiring payment of Social Security taxes.  "Substantial earnings" are $18,150 for 2007; $17,475 for 2006; $16,725 for 2005; and so on.  The more years of substantial earnings a worker has, the less the worker's benefits will be reduced.

For example, if a worker has 21 years of substantial earnings, then the 90 percent factor is reduced to 45 percent instead of 40 percent. The maximum reduction for that worker retiring in 2007 is $306 per month instead of $340.00 per month. If a worker has 22 years of substantial earnings, then the 90 percent factor is reduced to 50 percent. The maximum reduction for that worker retiring in 2007 is $272 per month instead of $328.00 per month. If a worker has 30 or more years of substantial earnings, then there is *no* reduction.

For a more detailed explanation of the WEP, including tables of substantial earnings and percentage reductions, see Social Security Administration Publication No. 05-10045, The Windfall Elimination Provision, available at www.ssa.gov or at 1-800-772-1213.

## B. The Government Pension Offset (GPO)

A potentially more deadly offset is the *Government Pension Offset* (GPO). This offset reduces Social Security spouse's and widow(er)'s benefits of those who receive an alternative pension and did not contribute to Social Security. While it affects fewer persons than the WEP, it reduces spouse's or widow(er)s benefits by two-thirds of the amount of the alternative pension. In some cases this could result in the complete elimination of the spouse's or widow(er)'s benefits.

For an explanation of the GPO, see Social Security Administration Publication No. 05-10007, Government Pension Offset, available at www.ssa.gov or at 1-800-772-1213.

## C. What is being done to repeal the WEP and GPO?

HR 82 and S 206 are the latest bills introduced in Congress to eliminate the WEP and GPO. These and similar bills introduced in the past have gradually been gaining more sponsors, but they have not yet gotten out of committee. To support these bills, contact your U.S. Senators and Congressperson.

# 4. HOW ARE CalSTRS DB BENEFITS CALCULATED?

## A. What is the DB benefit formula?

Retirement benefits for the CalSTRS DB are calculated by a *formula*. Even though you and your district(s) each contribute to your DB account (8% and 8.25% respectively), benefits are *not* based on your account balance. Benefits are usually in the form of lifetime monthly pension payments which may *exceed* your account balance at retirement (depending on how long you live). Here is the formula:

***Annual Unmodified Benefit = Service Credit x Age Factor x Final Compensation***

***Service credit*** is the number of years of credited service. At least five years service credit is required to be *vested*; i.e., to be eligible to receive CalSTRS DB retirement benefits.

For a full-timer, one year of service credit is earned for teaching one school year. But for a part-timer, service credit depends on the "full-time equivalent" ("FTE") for each type of service rendered by the part-timer. Types of service include teaching credit classes, teaching noncredit (adult education) classes, substitute teaching, counseling, library duties, holding paid office hours, etc. There usually should be more than one FTE used within a district.

**What does the FTE represent?** The FTE for each type of service represents the number of hours per school year defined in a district as the equivalent of a full-time load performing only that service. For teaching credit or noncredit classes, the FTE represents the number of teaching hours per school year defined in a district as the equivalent of a full-time load teaching load. By statute it currently must be a minimum of 525 hours per year for teaching credit classes and a minimum of 875 hours per year for teaching noncredit (adult education) classes.

Understanding the FTE concept is essential to understanding how DB benefits are calculated. The FTE directly affects the service credit and final compensation factors in the benefit formula. Unfortunately, FTEs used by districts may be inequitable, vary from district to district, and have changed over time, all causing confusion and/or inequitable retirement benefits for part-timers. (Also note that "FTE" has nothing to do with "full-time equivalent student" ["FTES"] which is used by the state to fund community colleges.)

Let's look at some examples. At City College of San Francisco (CCSF) the FTE for teaching credit classes is 525 hours per year. This is equitable because full-time credit instructors are required to teach 15 class hours per week for 35 weeks in a school year (i.e., 15 x 35 = 525). The FTE for teaching noncredit classes is 875 hours per year. (Prior to 10/21/2004 it was 1050 hours per year.) This is equitable because full-time non-credit instructors teach 25 hours per week (i.e., 25 x 35 = 875). And the FTE for voluntary paid office hours held by credit instructors is 1225 hours per year. Meanwhile, in Los Angeles the FTE for teaching credit classes, which *includes* mandatory office hours, is 600 hours per year. These are just a few of the many FTEs in use throughout the state.

**How does the FTE affect service credit?** For a part-timer, service credit earned for one school year for a particular type of service in a district (e.g., teaching) is calculated by CalSTRS by dividing the part-timer's "**earned salary**" by the part-timer's "**earnable salary**". "Earned salary" is the amount of pay actually earned. For part-timers paid hourly, it is calculated by multiplying a part-timer's hourly rate by the number of hours worked. "Earnable salary" for a particular type of service, on the other hand, is what a part-timer would earn in one school year if he or she worked the full number of FTE hours performing that service. For part-timers paid hourly, it is calculated by multiplying a part-timer's hourly rate by the FTE.

Let's look at some examples. In District 1 full-timers teach 15 hours/week for 35 weeks and District 1 uses an equitable FTE of 525 hours. A part-timer earns $60/hour and teaches 6 hours per week for 35 weeks, or 210 hours. The <u>earned</u> salary is $12,600 (i.e., $60/hr x 210 hrs = $12,600). The <u>earnable</u> salary is $31,500 (i.e., $60/hr x 525 hrs = $31,500). Service credit calculated by CalSTRS would be .4 (i.e., $12,600 ÷ $31,500 = .4). This is equitable, because 6 hours per week is a 40% load.

Although not used by CalSTRS, another method of computing the service credit for part-timers paid hourly is to divide the number of hours worked by the FTE (i.e., 210 hrs ÷ 525 hrs FTE = .4). (This simplified method is used in the examples later in this primer.)

Now suppose that another part-timer also earning $60/hr in District 1 taught 207 hours because one class fell on an unpaid holiday. Earnable salary is $12,420 (i.e., $60/hr x 207 hrs - $12,420). Earnable salary is still $31,500. Service credit calculated by CalSTRS would be .394 (i.e., $12,420 ÷ $31,500 = .394). (Or alternatively, 207 hrs ÷ 525 hrs FTE = .394.)

**Note:** In a "pay by load" district (such as San Francisco or Los Angeles), the above discrepancy would not occur. Both part-timers would have the same earned salary regardless of actual hours taught and would receive the same amount of service credit.

One of the problems involving FTEs is that districts previously used, and some still use, an inequitably high FTE. If an FTE is too high (even in a "pay by load" district), a part-timer will earn less service credit than he or she should receive. For example, if an FTE of 1050 hours (instead of 525 hours) were used for the first part-timer in the preceding examples, then the earnable salary would be $63,000 and service credit would be only .2, or <u>one-half</u> of what it should be (i.e., $12,600 ÷ $63,000 = .2). Therefore part-timers should always make sure that an appropriate FTE is being used by their district(s) for each type of service that they perform.

The total service credit for one school year is the sum of the service credit earned for all types of service, subject to a maximum of one year service credit (which affects some freeway flyers). For example, if the part-timers in the preceding examples also held paid office hours, substituted, taught a non-credit class, and/or taught at another district, service credit would also be earned for *each* type of service using the FTE defined by the employing district for that type of service. Starting July 1, 2002, service credit is earned for teaching summer school, and service credit in excess of 1.0 year is credited to a part-timer's Defined Benefit Supplement (DBS) account (i.e., not lost as in the past).

Your annual CalSTRS statements show your service credit earned for the latest school year and your total service credit as of the date of the statement. You should check your annual statement each year to make sure that you received the proper service credit.

***<u>Age Factor</u>*** is a percentage determined by your age in years and months on the last day of the month in which retirement is effective. It ranges from 1.10% to 2.40%, depending on age. At age 60 ("normal" retirement age) it is 2%. At age 63 it is the maximum 2.4%. <u>Benefits may increase significantly by waiting until age 63 to retire because the Age Factor will increase to .024.</u> Here is a condensed Age Factor Table. The complete Age Factor Table is available in the CalSTRS Member Handbook or at www.calstrs.com.

Condensed Age Factor Table

| Age at retirement (excluding months) | Age Factor | |
|---|---|---|
| 63 | 2.400% | (=.02400) |
| 62 | 2.267% | (=.02267) |
| 61 | 2.133% | (=.02133) |
| 60 | 2.00% | (=.02000) |
| 59 | 1.88% | (=.01880) |
| 58 | 1.76% | (=.01760) |
| 57 | 1.64% | (=.01640) |
| 56 | 1.52% | (=.01520) |
| 55 | 1.40% | (=.01400) |
| 54 | 1.334% | (=.01334) |
| 53 | 1.28% | (=.01280) |
| 52 | 1.22% | (=.01220) |
| 51 | 1.16% | (=.01160) |
| 50 | 1.10% | (=.01100) |

***Final Compensation*** is the average of the three highest consecutive years of *earnable* salary (not earned salary). For those with at least 25 years service credit (rare for a part-timer), it is the highest single year.

Calculating earnable salary for purposes of final compensation is complicated for a part-timer with multiple earnable salaries; i.e., one who performs different types of service with different pay rates and/or different FTEs. The earnable salary for such a part-timer for one school year is a weighted average of the part-timer's earnable salaries for all types of service that year. This weighted average will be less than the part-timer's highest earnable salary for any one type of service. This causes a problem for some part-timers who are freeway flyers their last three years before retirement because it effectively reduces their retirement benefits. See examples 5 through 8 below for further explanation.

[Now for those who are really into math. Here is how CalSTRS does its calculations for part-timers with multiple earnable salaries. For each type of service performed by a part-timer, the employing district reports to CalSTRS the earned salary (amount actually paid), the earnable salary (hourly pay rate times appropriate FTE), and the part-timer's 8% contribution. At the end of the school year CalSTRS computes the service credit for each type of service by dividing the earned salary by the earnable salary. CalSTRS then computes the total service credit for the year by adding all service credit earned for each type of service. CalSTRS computes the total earned salary for the year by adding all earned salaries for each type of service. To compute earnable salary for the year for final compensation purposes (i.e., the weighted average of all earnable salaries), CalSTRS divides the total earned salary for the year by the total service credit for the year.]

You can calculate your earnable salary for final compensation purposes for any past year by using your CalSTRS annual statement for that year. First calculate your total earned salary for that year (sometimes called "calculated earnings" by CalSTRS) by dividing the total of your "current year contributions" for your DB and DBS accounts by .08. This will be your total earned salary from all districts for that year. Then calculate your earnable salary for final compensation purposes for that year by dividing the total earned salary by the "current year service credit".

## B. Examples of calculating DB benefits

**Example 1**: A full-timer (for clarification and comparison purposes) retires at age 60 after 10 years teaching with $75,000 salary last three years.

Service Credit = 10 yrs
Age Factor = .02
Final Compensation = $75,000/yr
**Annual Unmodified Benefit** = 10 yrs x .02 x $75,000/yr = **$14,000/yr [or $1,167/mo]**

Examples 2 through 8 are of part-timers whose only creditable service was teaching.

**Example 2**: A part-timer retires at age 60 after 16.7 years of teaching 9 hrs/week for 35 weeks/yr (60% load), 525 hrs/yr FTE each year, and $100/hr last 3 yrs (70% pro rata of above full-time salary). Note that the benefit is 70% of that of the full-timer in Example 1, even though both had 10 years service credit. This is because the part-timer's salary was 70% pro rata of the full-timer's salary.

Service Credit = 16.7 yrs x ([9 hrs/wk x 35 wks/yr] ÷ 525 hrs/yr)
= 16.7 yrs x (315 ÷ 525)
= 16.7 yrs x .6
= 10 yrs
Age Factor = .02
Final Compensation = $100/hr x 525 hrs/yr = $52,500/yr [or 70% of above full-time salary.]
**Annual Unmodified Benefit** = 10 yrs x .02 x $52,500/yr = **$10,500/yr [or $875/mo]**

**Example 3:** Same as Example 2, but now assume that the part-timer teaches three more years and retires at age 63. Note the significant increase in benefits caused by more service credit and larger age factor (almost 42% increase).

Service Credit = 10 yrs + (3 x .6 yr) = 10 yrs + 1.8 yrs = 11.8 yrs
Age Factor = .024
Final Compensation = $100/yr x 525 hrs/yr = $52,500/yr
**Annual Unmodified Benefit** = 11.8 yrs x .024 x $52,500/yr = **$14,868/yr [or $1,239/mo]**

**Example 4:** Same as Example 2 but now assume that the part-timer teaches just a 20% load (3 units) for three more years and retires at age 63. Note that the increase in benefits is still significant (27% increase).

Service Credit = 10 yrs + (3 x .2 yr) = 10 yrs + .6 yr = 10.6 yrs
Age Factor = .024
Final Compensation = $100/hr x 525 hrs/yr = $52,500/yr
**Annual Unmodified Benefit** = 10.6 yrs x .024 x $52,500/yr = **$13,356/yr [or $1,113/mo]**

**Examples 5 through 8 illustrate the problem for part-timers with multiple earnable salaries during their last three years before retirement. Such part-timers should do the math before their last three years and decide on what action to take.**

**Example 5:** A part-timer retires at age 60 after 16.7 yrs teaching, last 3 yrs include $100/hr at 6 hrs/wk (40% load) in District #1 and $50/hr at 3 hrs/wk (20% load) in District #2, and 525 hrs/yr FTE in both districts. Note that the benefit is lower than that in Example 2 because of the lower pay rate (and hence lower earnable salary) in District 2.

Service Credit = 10 yrs [Same as Example 2]
Age Factor = .02
Final Compensation: This is the problem. If the part-timer just worked in District #1, then Final Compensation (i.e., <u>earnable</u> salary) = $100/hr x 525 hrs/yr = $52,500/yr. If the part-timer just worked in District #2, then Final Compensation (i.e., <u>earnable</u> salary) = $50/hr x 525 hrs/yr = $26,250/yr. So CalSTRS computes Final Compensation as a <u>weighted average</u> of both earnable salaries as follows:

For just District #1 each of last 3 yrs:
Service Credit =1 yr x ([6 hrs/wk x 35 wks/yr] ÷ 525 hrs/yr) = .4 yrs
<u>Earned</u> Salary = $100/hr x 6 hrs/wk x 35 wks = $600 x 35 = $21,000

For just District #2 each of last 3 yrs:
Service Credit = 1 yr x ([3 hrs/wk x 35 wks/yr] ÷ 525 hrs/yr) = .2 yrs
<u>Earned</u> Salary = $50/hr x3 hrs/wk x 35 wks = $5,250

Total for District #1 and District #2 each of last 3 yrs:
Total Service Credit = .4 yr + .2 yr = .6 yr
Total <u>Earned</u> [not earnable] Salary = $21,000 + $5,250 = $26,250

Final Compensation (<u>earnable</u> salary) = $26,250 ÷ .6 yr = $43,750/yr

**Annual Unmodified Benefit** = 10 yrs x .02 x $43,750/yr = **$8,750/yr [or $729/mo]**

**<u>Example 6</u>**. Same as Example 5, but now assume that the part-timer does not teach in District #2 the last three years. Less teaching means less income and less service credit. The part-timer will <u>lose</u> $5,250 gross income (smaller amount after taxes) and .2 yr service credit each of the last three years. But the part-timer would <u>gain $1,120 more per year in benefits for the rest of the part-timer's life</u>. The part-timer would have to decide on the best course of action.

Service credit = 10 yrs – (3 x .2yr) = 10 yrs - .6 yr = 9.4 yrs
Age Factor = .02
Final Compensation = $100/hr x 525 hrs/yr = $52,500/yr [weighted average not used]
**Annual Unmodified Benefit** = 9.4 yrs x .02 x $52,500/yr = **$9,870/yr [or $822/mo]**

**<u>Example 7</u>:** Same as Example 5, but now assume that the part-timer had 20 yrs service credit:

Service credit = 20 yrs
Age Factor = .02
Final Compensation = $43,750/yr [weighted average from Example 5]
**Annual Unmodified Benefit** = 20 yrs x .02 x $43,750/yr = **$17,500/yr [or $1,458/mo]**

**<u>Example 8</u>:** Same as Example 7 but now assume that the part-timer does not teach in District #2 the last three years. Again, the part-timer would <u>lose</u> $5,250 gross income and .2 yr service credit each of the last three years. But the part-timer would <u>gain $2,870 more per year in benefits for the rest of the part-timer's life</u>. Again, the part-timer must decide what to do the last three years.

Service credit = 20 years – (3 x .2 yr) = 20 yrs - .6 yr = 19.4 yrs
Age Factor = .02
Final Compensation = $100/hr x 525 hrs/yr = $52,500/yr [weighted average not used]
**Annual Unmodified Benefit** = 19.4 yrs x .02 x $52,500/yr = **$20,370/yr [or $1,697/mo]**

## C. How can you increase your DB benefits?

You may be able to increase your DB benefits, but it will cost you time and/or money. First, recall the formula used to calculate your retirement benefits:

***Annual Unmodified Benefit = Service Credit x Age Factor x Final Compensation***

You can increase your benefits (i.e., left side of formula) by increasing any of the three multipliers on the right side of the formula.

**How can you increase your "Service Credit"?** *(Note: You may need to do this just to earn the minimum five years service credit required to vest.)* Make sure your district has been using an appropriate FTE(s); teach more (don't forget summer school); substitute more; hold more paid office hours (if available); postpone retirement; don't get sick (unused sick leave is converted to service credit); and "consolidate" your CB funds into DB service credit.

If you can afford to (because it will cost you money), consider the following: "redeposit" any previously withdrawn DB contributions; "consolidate" your CB funds into DB service credit and pay additional funds to purchase service credit for the entire time that you were in CB; if eligible, "purchase" service credit for specific types of past service (maybe even if performed in another state); and if *vested*, purchase up to five years of "air time" service credit (not connected to any specific prior employment). For more information see the CalSTRS publication "Purchase Additional Service Credit" and/or go to www.calstrs.com. After determining the cost, do the math to see if the cost is justified by the expected increase in your retirement benefits.

**How can you increase your "Age Factor"?** Postpone retirement until age 63 (perhaps reduce your load) which has the highest age factor of 2.4%.

**How can you increase your "Final Compensation"?** Recall that "final compensation" is the average of the three highest consecutive years of earnable salary, not earned salary. If you earn $60/hour with a 525 hour FTE, your earnable salary is $31,500 (i.e., $60/hr x 525 hrs/yr), *regardless* of load or salary actually earned.

Negotiate higher salaries. Low pay means low retirement benefits.

If you were to receive a significant raise the year after your planned retirement, then you could postpone retirement, perhaps at a reduced load. This will increase your earnable salary (also service credit and possibly age factor). But do the math to see if it is worthwhile.

Determine the three consecutive years with your highest earnable salary. It may not be your last three years before retirement. For example, perhaps you previously taught in another different district with a higher earnable salary. At retirement CalSTRS will use your last three years unless you specify otherwise.

**Important: If you expect to have multiple earnable salaries during your last three years, then you must be especially careful.** If you are a freeway flyer, you may need to consider *teaching less* those last three years (if you can afford to!). Teach *only* in the district(s) with the highest earnable salary. This may help because your earnable salary for final compensation purposes is an *average* of your earnable salaries from all districts, *weighted* according to the amount of service credit earned in each district. But do the math. See Examples 5 through 8 above.

Note also that the highest earnable salary may not be in the highest paying district. It also depends on the FTE used by each district. For example, if a part-timer earns $60/hour in one district with a 525 hour FTE, then the earnable salary is $31,500/yr (i.e., $60/hr x 525 hr/yr = $31,500/yr). If the same part-timer also earns $50/hour in another district but with an 875 hour FTE, then the earnable salary is $43,750 (i.e., $50/hr x $875 hr/yr = $43,750/yr). The part-timer has a higher earnable salary in the district that has the lower hourly pay rate.

Similarly, you may need to consider eliminating or reducing substitute teaching your last three years. Again, do the math.

## D. How will enactment of AB 1586 affect DB benefits?

**Beginning January 1, 2005, enactment of AB 1586 (Education Code Section 22115(e))** will **increase retirement benefits for over 18,000 part-timers in the CalSTRS Defined Benefit Plan (DB).** It applies to every part-timer who was employed and in DB before July 1, 1996, and retired or will retire as a part-timer after that date. (Unfortunately it does not apply to one who retired or will retire as a full-timer.) It will correct an unintended reduction in retirement benefits caused by prior legislation. It effectively restores service credit "lost" by credit instructors prior to 7/1/96 and by noncredit (adult education) instructors prior to 1/1/99.

Prior to July 1, 1996, credit part-timers generally received only 1/2 and non-credit part-timers generally received only 5/6 of the service credit they had equitably earned. That was because districts were required to use an unrealistic 1050 hour hours/year as a full-time equivalent (FTE). Many part-timers were unfairly prevented from accumulating the five years of service credit required to vest (i.e., be entitled to receive lifetime retirement benefits) in DB.

Ironically, if a credit part-timer did vest and retire prior to 7/1/96 (probably taking up to twice as long as it should have to vest), the reduction in service credit was exactly offset by a proportionally equal increase in "final compensation" in the retirement benefit formula. As a result, a part-timer received an equitable amount of retirement benefits.

For credit part-timers, legislation effective July 1, 1996, required districts to begin using "30 teaching units" (defined as a full-time instructor's annual teaching load, such as 525 hours) as a minimum FTE. Because of confusion over "teaching units", this law was replaced by legislation effective January 1, 1999, which required districts to begin using a minimum of 525 hours FTE. Credit part-timers in districts that complied with the new laws began receiving proper service credit. But the legislation was not retroactive and caused an unintended reduction in retirement benefits for those retiring after 7/1/96. A credit part-timer's service credit was still one-half what it should have been for service prior to 7/1/96 (or until the date his/her district began compliance), but final compensation was no longer twice what it should have been. There was nothing to offset the reduction in service credit. As a result retirement benefits were reduced.

For noncredit part-timers, legislation effective January 1, 1999, required districts to begin using a minimum of 875 hours FTE. Non-credit part-timers in districts that made the change also suffered an unintended reduction in benefits, although not to the same extent as for credit instructors.

AB 1586 will correct the above reductions in benefits caused by the prior legislation. ***From a part-timer's viewpoint, nothing will happen until he/she retires. No additional service credit will be added to a part-timer's account***. Service credit will continue to accrue according to the FTE(s) used by a district. Service credit must still total five years for a part-timer to vest. ***No supplemental statements will be sent by CalSTRS to part-timers***.

Under AB 1586 a part-timer will now receive the larger of two different retirement benefit calculations performed by CalSTRS at the time of retirement. The first calculation will be made as if AB 1586 had not been passed; i.e., service credit will remain inequitably reduced prior to 7/1/96 (credit) or 1/1/99 (noncredit) and final compensation will be based on a minimum of 525 hours (credit) or 875 hours (noncredit).

The second calculation will be made as if the legislation effective 7/1/96 and 1/1/99 never went into effect; i.e., 1050 hours FTE will be used for all service credit earned (before and after 7/1/96 or 1/1/99) and for final compensation in the benefit formula. If the total service credit under this calculation is reduced to less than 5 years, a part-timer will still remain vested. This calculation will result in larger and equitable retirement benefits for most part-timers. Depending primarily upon when a part-timer began teaching and his/her final salary, the increase in retirement benefits could be up to $150 or more per month. If a part-timer only began teaching shortly before 7/1/96 or 1/1/99, any increase will be small.

**Let's do an example.** Assume that a credit part-timer retires at age 60 after 2 years service credit with a 1050 hour FTE prior to 7/1/96 and 5 more years service credit with a 525 hour FTE after 7/1/96, and earns $100/hr her last three years teaching.

(1) The first calculation of her unmodified annual benefit is as follows:

**Annual Unmodified Benefi**t = Service Credit x Age Factor x Final Compensation
= 7 yrs x .02 x ($100/hr x 525 hr/yr)
= 7 yrs x .02 x $52,500/yr
**= $7,350yr [or $612.50/mo]**

(2) The second calculation of her unmodified annual benefit is as follows:

**Annual Unmodified Benefit** = Service Credit x Age Factor x Final Compensation
= 4.5 yrs x .02 x ($100/hr x 1050 hr/yr)
= 4.5 yrs x .02 x $105,000
= **$9,450/yr [or $787.50/mo, an increase of $175/mo]**

Under AB 1586 the part-timer will receive the benefit from the second calculation because it is larger. Note that the increase of $175/mo can also be estimated in just one step by doing the first calculation with only the service credit "lost" prior to 7/1/96:

**Increase in Annual Unmodified Benefit** = 2 yrs x .02 x $52,500/yr
= **$2,100/yr [or $175/mo]**

# 5. WHAT OTHER LEGISLATION AND CalSTRS IMPROVEMENTS HELP PART-TIMERS?

## A. Legislation

In addition to AB 1586, other legislation has benefited part-timers.

**AB 3076 (Education Code Sections 22502(b), 22504(b), 22601.5(b), and 22604(b))**, effective July 1, 2005, excludes part-timers from mandatory membership in CalSTRS DB so long as they are classified as "temporary" employees; i.e., teach no more than 60% of a full-time load. In the past part-timers were sometimes forced into DB against their will because of the amount of load they taught or number of days they taught in one pay period. All part-timers continue to have the right to voluntarily join the DB plan, regardless of what load they teach.

**AB 2982 (Education Code Section 22138.5(a)),** effective January 1, 2003, requires districts to disclose their FTE(s) in collective bargaining agreements and part-timer employment contracts. Part-timers should also make sure that their districts comply with this law and, if necessary, take action to force compliance. Part-timers in CalSTRS DB must know what FTE(s) is used in their district to ensure that they are receiving proper service credit and to be able to estimate their DB benefits.

**AB 2700 (Education Code Sections 22119.2 and 22703),** effective July 1, 2002, allows service credit to be earned for teaching summer school and allows for contributions for service credit that would exceed 1.0 year (which is not allowed) to be credited to a part-timer's DBS account.

**AB 2554 (Education Code Section 22455.5),** effective January 1, 1995, requires employers to notify employees within 30 days of hire of the employees' right to elect membership in DB.

## B. CalSTRS improvements

CalSTRS has established a part-time task force, begun printing articles regarding part-timer issues in its semiannual publication CalSTRS Connections (previously called CalSTRS Bulletin), begun including a section for part-timers in its annual Member Handbook, and begun to better train its counselors and district personnel to deal with part-timer issues,

# 6. WHAT ISSUES STILL FACE PART-TIMERS?

Unfortunately, numerous issues involving retirement remain for part-timers. They include, but are not limited to, the following:

1. Low compensation causes low retirement benefits;

2. Districts are not required to contribute to all part-timer retirement plans;

3. Districts are not required to offer Social Security to part-timers;

4. Social Security Windfall Elimination Provision and Government Pension Offset;

Additional issues remain for part-timers in CalSTRS DB, including, but not limited to, the following:

1. Complexity of DB;

2. Lack of accurate information for part-timers;

3. Non-compliance by some districts re appropriate FTE, which may adversely affect time needed to vest and/or calculation of retirement benefits;

4. Inability to get out of DB;

5. Inability to vest because of inequitable accumulation of service credit and noncompliance by districts with state law;

6. Reduced retirement benefits because of inequitable accumulation of service credit and noncompliance by districts with state law;

7. Reduced retirement benefits for full-timers who were previously part-timers because of inequitable accumulation of service credit as part-timers;

8. Reduced retirement benefits caused by multiple earnable salaries (Examples 5 through 8 above);

9. Inequitable conversion of unused sick leave to service credit (1050 hrs/yr FTE is used).

10. Annual member statement is not broken down by district for freeway flyers.

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