# Annual Leave Straddling FAQs

**What are annual leave redemptions (i.e., "vacation buydowns")?**
Most Ventura County and District labor agreements and management resolutions (collectively referred to as Memorandum of Agreement, or MOA) contain provisions entitling employees to redeem or cash out accrued annual leave. Also known as "vacation buydowns," leave redemptions permit employees to sell back to their employer accrued vacation hours in exchange for cash. Most MOAs also specify the annual limit on the amount of leave that can be cashed out.

**Are annual leave redemptions included in the calculation of retirement benefits?**
For Legacy members only, leave redemptions made during active service are included in pensionable earnings ("compensation earnable") and in final average compensation (FAC), up to a certain limit. When leave redemptions occur in a Legacy member's FAC measurement period, they are included in the retirement benefit calculation and can result in a higher benefit than members would have received without having redeemed leave.

For PEPRA members, leave redemptions are not pensionable (pursuant to PEPRA) and therefore will not increase their retirement benefits.

**What did the Alameda Decision say about leave redemptions?**
The Alameda Decision was issued by the California Supreme Court on July 30, 2020. The ruling declared as constitutional Government Code section 31461(b)(2), which is a "PEPRA amendment" to the compensation earnable statute that took effect on January 1, 2013, and excluded from compensation earnable payments for leave redemptions "in an amount that exceeds that which may be earned and payable in each 12-month period during the final average salary period, regardless of when reported or paid."

For retirements on or after January 1, 2013, VCERA can include in a Legacy member's FAC only what was both "earned and payable" in each 12-month period.

**What does "earned and payable" mean?**
"Earned" refers to the number of leave hours an employee is able to accrue. "Payable" refers to the maximum annual cash-out limit permitted by each member's MOA. For County and District MOAs, this means the amount payable each calendar year, as recently affirmed by the Court of Appeal in litigation on this issue.

**What is "leave straddling"?**
Leave straddling occurs when (1) a VCERA member receives multiple leave redemptions from two calendar years within a 12-month period and (2) the total redeemed hours in the FAC period exceed the aggregate redeemable hour limit imposed by the member's MOA for the FAC period.

Put simply, leave straddling is when a member's total cash-outs in the 12-month or 36-month FAC period exceeds the aggregate annual calendar-year cash-out limit in his/her MOA during that FAC period. For example, a member with a 3-year measurement period who is eligible to redeem 100 hours each calendar year can only have up to a maximum of 300 hours included in the FAC period.

**Why is leave straddling a problem?**
When multiple leave redemptions from two calendar years are paid in a 12-month period, the total redeemed hours in that period can exceed the redeemable calendar-year hour limit imposed by the member's MOA. Due to the Alameda Decision, if these "excess hours" are paid during a Legacy member's FAC measurement period, the excess hours must be removed from the member's "compensation earnable" used to calculate FAC. Leave straddling falls into the Alameda Decision's "PEPRA Exclusion" category. VCERA's removal of these excess hours has been upheld by the Court of Appeal in recent litigation on this issue.

**What are the rules governing annual leave redemptions and compensation earnable?**
*Before* the Alameda Decision, VCERA included in compensation earnable in-service leave redemptions in an amount not to exceed the annual leave accrued in the 1-year or 3-year measurement period (i.e., up to what was earned in each 12-month period) <u>minus</u> the number of annual leave hours an employee was required to take per the MOA (e.g., 80 hours for each 12 months in the FAC period) before becoming eligible to redeem hours. *This method had the effect of reducing what was "earned" in each 12-month period by 80 hours, which was more restrictive than the PEPRA Amendment limits, but also had the potential of allowing inclusion of more than what was "payable" in each 12-month period.*

The Alameda Decision confirmed that on and after January 1, 2013, the date of the PEPRA Amendments, VCERA was required to limit what is included in FAC to what was "earned and payable" in each 12-month period of the 1-year or 3-year measurement period. Under the post-Alameda rules, effective as of January 1, 2013, VCERA includes what is both "earned" (i.e., accrued) in the FAC period and what is "payable" (i.e., what is redeemed in cash up to the annual cash-out limit) for each 12 months in the FAC period. Limiting inclusion of leave redemptions to a member's annual cash-out limit has been upheld by the Court of Appeal in recent litigation on this issue.

**What are examples of how leave redemptions were calculated under the previous and current rules?**
<u>Example #1</u>: Member 1 has a 3-year FAC measurement period. Under their MOA, they accrue 288.08 hours of leave per calendar year and, after using 80 hours of leave, they can sell 200 hours per year. They retired in 2013 with a FAC measurement period of July 2010 to June 2013. During that measurement period, they sold 200 hours four times (once each calendar year: 2010, 2011, 2012, and 2013). Under VCERA's prior rules, VCERA would have included up to 208.08 hours (288.08 – 80) for each of the 3 years, for a total of 624.24 hours (208.08 x 3). Under the new rules, which apply because the member retired on or after 1/1/2013, VCERA can include up to 200 hours (what is "earnable and payable" each calendar year under the MOA)

for each of the 3 years, for a total of 600.00 hours (200 x 3). The new rules result in 24.24 less hours being included than what was permitted prior to 2013 (or 8.08 hours per year when averaged across the 3-year measurement period). If Member 1 was paid $1,000 for these “excess” 24.24 hours, the new rules would result in a $27.78 decrease ($1,000 / 36 months in a 3-year FAC) in the monthly FAC used to calculate Member 1’s retirement benefit.

<u>Example #2</u>: Member 2 has a 1-year FAC measurement period. Under their MOA, they accrue 368.16 hours of leave per calendar year and, after using 80 hours of leave, they can sell 200 hours per year. They retired in 2020 with a FAC measurement period of November 2019 to October 2020. During that measurement period, they sold 368 hours (200 in 2019 and 168 in 2020). Under VCERA’s prior rules, VCERA would have included up to 288.16 hours (368.16 – 80). Under the new rules, which apply because the member retired on or after 1/1/2013, VCERA can include up to 200 hours (what is “earnable and payable” each calendar year under the MOA). The new rules result in 88.16 less hours of leave redemption being included than what was permitted prior to 2013. If Member 2 was paid $5,000 for these “excess” 88.16 hours, the new rules would result in a $416.67 decrease ($5000 / 12 months in a 1-year FAC) in the monthly FAC used to calculate Member 2’s retirement benefit.

<u>Example #3</u>: Member 3 has a 1-year FAC measurement period. Under their MOA, they accrue 240 hours of leave per calendar year and, after using 120 hours of leave, they can sell 120 hours per year. They retired in 2023 with a FAC measurement period of December 2022 to November 2023. During that measurement period, they sold 120 hours two times (once each calendar year: 2022 and 2023). Under VCERA’s prior rules, VCERA would have included up to 120 hours (240 – 120). Under this example, the new rules produce the same result (120 is still includable because 120 hours are “earned and payable” each calendar year under the MOA). The new rules would result in no change in the Monthly FAC used to calculate Member 3’s retirement benefit.

**When did the Alameda Decision’s prohibition on leave straddling take effect?**

The California Supreme Court stated that it is <u>the law in effect at the time of retirement</u> that is used to calculate the amount of an employee's pension benefit, and that the PEPRA amendment prohibiting straddling took effect on January 1, 2013. The Court further stated that retirement boards have no authority to adopt or act on an interpretation of CERL’s provisions that is inconsistent with those provisions. In implementing Alameda, VCERA also followed the legal principles that retirement boards have no authority to create “window periods” that permit members to receive retirement benefits that the applicable law does not authorize.

In VCERA’s straddling lawsuit, the Superior Court issued judgment in VCERA’s favor, upholding VCERA’s application of straddling limitations, effective January 1, 2013. The Superior Court rejected “fairness” arguments that PEPRA’s straddling rules should be applied in Ventura only to employees who retire after either the Alameda Decision (7/30/2020) or the date the Board adopted the Resolution that implemented Alameda (10/12/2020). However, the Superior Court ruled that VCERA “may” forego recoupment of overpayments made to retirees prior to the first retiree payroll after the Alameda Decision. Although this part of the Superior Court's ruling was not appealed, a group of retirees submitted documents to the Court of Appeal in support of an argument to apply a later effective date and the Court of Appeal nevertheless unanimously affirmed the Superior Court ruling. Accordingly, the PEPRA Amendments that prohibit straddling *must* be applied to <u>all retirement benefit calculations on and after the Amendment's effective date (1/1/2013)</u>, but VCERA properly exercised discretion not to recoup overpayments prior to the Alameda Decision. Note that based on this discretion and principles of fairness, VCERA will not recoup <u>any</u> overpayments directly from retirees up through the date that benefits are corrected.

**Who is affected by the Alameda Decision's prohibition on leave straddling?**
Legacy members who retired before 2013 will <u>not</u> be affected.

Legacy members who retired on or after January 1, 2013, <u>will only be affected if</u> their FAC included excess redeemed hours due to leave straddling. If this occurred, VCERA will remove the excess hours, recalculate the FAC, recalculate the retirement benefit, and notify the affected retiree that his/her benefit will be reduced prospectively. VCERA will <u>not</u> seek to recover overpaid retirement benefits caused by leave straddling.

PEPRA members never had annual leave redemptions or vacation buydowns included in their retirement earnings because the PEPRA legislation does not permit this, so they remain <u>unaffected</u>.

**Did members overpay contributions on leave straddling?**
No. All leave redemptions by Legacy members are properly included in their compensation earnable, so any contributions they made on prior leave redemptions were appropriate. However, if the timing of those payments results in straddling during the FAC period, the PEPRA Amendments require retirement systems to exclude from final compensation such excess hours. Therefore, VCERA will not issue contribution refunds related to leave straddling.

**Has there been litigation concerning VCERA's position on leave straddling?**
Yes. The Santa Barbara County Superior Court upheld VCERA's implementation of the leave straddling rules, but two unions appealed. On January 4, 2024, the 2nd District Court of Appeal applied the Alameda Decision in determining whether the VCERA Board's October 12, 2020, Resolution on the straddling issue was a correct application of law; the Court further clarified the meaning of what is considered both "earned and payable in each 12-month period of the member's final average salary period." In a unanimous ruling, the Court stated: "A member's compensation earnable during the final compensation period is meant to reflect the average pay the retiring employee received. [Alameda at p. 1058] And, an employee's average pay during this compensation period includes payment for leave cash-outs that is subject to annual limitations." As the Court observed, "A member's terms of employment (e.g., a Memorandum of Agreement or the County Management Resolution) limit the number of hours a member may cash out in a calendar year." Accordingly, the Court concluded that "[t]he Board was

required to comply with section 31461, subdivision (b) and Alameda and exclude compensation for unused leave exceeding their calendar year allowances." This ruling is now binding on VCERA and serves as precedent for other County retirement plans. Appellants have petitioned the Supreme Court for review and these FAQs will be updated as new information becomes available.