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CLIENT ALERT

July 1, 2011

NEW JERSEY ENACTS SWEEPING LEGISLATION OVERHAULING PUBLIC SECTOR BENEFITS

On June 28, 2011, Governor Chris Christie signed into law Senate Bill 2937 (c. 78, P.L. 2011). The law is now in effect and contains a number of reforms affecting pension and health benefits for public employees. In addition to requiring employees to make higher contributions toward their pension accounts, S2937 aims to lower the taxpayer share of public health benefit costs by increasing the amount employees pay toward their own benefits. The State Department of the Treasury estimates that the Bill will save taxpayers approximately three billion dollars over the next decade.

In order to achieve this cost savings, S2937 includes a number of measures aimed at both the public pension and health benefit systems. For example, the contribution rate for employees currently enrolled in the Public Employees' Retirement System (PERS) or the Teachers' Pension and Annuity Fund (TPAF) will immediately increase, from 5.5% of the employee's base salary to 6.5%. For non-State employees, this increase will be effective with the first payroll check issued on or after October 1, 2011. An additional one-point increase will be phased in over a seven-year period, for a total payment of 7.5% by July, 2018. The Act eliminates the automatic pension benefit cost-of-living adjustment (COLA) for current and future retirees and beneficiaries, but does not reduce adjustments made in prior years. The Act also creates a new tier of pension fund membership (Tier 5) for employees hired on or after June 28, 2011, with modifications to deferred and early retirement eligibility for those employees.

S2937 also requires public employees to pay an increased share of the cost of medical insurance coverage. For employers who participate in the State Health Benefits Program (SHBP) or the School Employees' Health Benefits Program (SEHBP), the cost of coverage is defined as the premium or periodic charges for medical and prescription drug plan insurance coverage, but not any other health benefit coverage. (However, a board of education may through collective negotiations seek to also include in the cost of coverage the premiums for other health benefits, such as dental or vision plans.) For employers who do not participate in the SHBP or the SEHBP, cost of coverage includes the premium or periodic charges for not only medical and prescription insurance, but also dental coverage, vision benefits, and any other health care benefit. The amount of each employee's contribution is based on a variable percentage of the cost of coverage, depending on the individual's base salary and the type of coverage (individual, family, member/spouse/partner-parent/child). The new contribution levels modify, but do not eliminate, the present requirement that employees pay 1.5% of their base salary toward their health benefits. S2937 specifically provides that the current 1.5% share is the minimum an employee must pay, in the event that the new contribution level does not actually equal or exceed 1.5% of that employee's salary. Under the law, then, employees must pay either 1.5% of their salary towards their health benefits, or the new contribution rates, whichever is the higher amount.

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The Act establishes three separate contribution categories, depending on the employee's type of health benefits plan coverage, and phases in the contribution over a four-year period. For example, an employee covered under an individual health plan who earns \$50,000 per year would pay 20% of premium costs, provided that the employee's contribution equals at least 1.5% of salary, at the end of the initial four-year period. An employee earning \$50,000 who elects family coverage, however, would pay 12% of the premiums for the plan. The same employee on a member/spouse or parent/child coverage plan must pay 15% of premiums at the end of the fourth year after enactment.

Under the law's four-year phase-in, the employee must pay one-fourth (1/4) of the final contribution percentage in the first year and an additional one-fourth of the expected contribution each succeeding year, until the total amount of the required contribution is reached at the end of the initial four-year period. Under this schedule, an employee whose contributions must ultimately total 20% of annual premium costs actually pays 5% in Year 1 of the program (or 1.5% of salary if that is greater), 10% in Year 2, 15% in Year 3 and the entire 20% contribution in Year 4. Although the contribution levels vary depending on income and coverage type, the same phase-in schedule is used to determine every employee's contribution obligation during the first four years after the statute's effective date. However, all new employees hired on or after June 28, 2011 must immediately contribute at the highest level (Year 4), unless those employees are covered by a collective negotiations agreement which was in force prior to that date. In that case, all employees hired after the expiration of the collective negotiations agreement will immediately begin contributing at the maximum level.

The healthcare contribution provisions of S2937 have no immediate impact on any employees currently covered by a valid and enforceable collective negotiations agreement which was in effect prior to June 28, 2011. The employees covered under such agreements are not impacted by the new contribution requirements until their respective agreements expire. At that time, the employees will begin paying contributions at the Year 1 phase-in rate, and proceed through the phase-in over the following three years until they reach the total contribution amount in Year 4. (The employee must actually be in a position covered by the collective negotiations unit in order to be exempt from the law's immediate impact; the statute specifically provides that this exemption does not apply to an employee whose position is not within a collective negotiations unit, even if the employer has previously extended the terms of a collective negotiations agreement to that individual's terms and conditions of employment.)

If a collective negotiations agreement has expired prior to the effective date of the law, and has not since been settled--that is, if a new contract is not ratified prior to the enactment of the legislation on June 28, 2011 -- the employees covered under that agreement will be required to contribute towards their respective percentages of healthcare coverage costs.

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Additionally, S2937 does not allow for the reopening, renegotiation or extension of any collective negotiations agreement in force prior to June 28, 2011 so as to extend the agreement beyond the effective date of the law. Any attempt to do so constitutes a new contract, and the employees covered under the revised agreement must begin to make contributions.

The contribution schedules defined in the law are minimum contribution requirements. School districts and other local employers may negotiate with their employees for a higher contribution amount above the levels required by the law. Additionally, employers who do not participate in SHBP/SEHBP and the local majority representatives may negotiate a different schedule of contributions and insurance coverage, provided that the end result achieves the same or greater savings when compared to the minimum contribution level set forth in the Act.

For example, the Act requires employees with individual health care coverage who earn \$70,000 per year to contribute 8% of their healthcare premiums in the first year after contribution deductions begin and a 16% contribution in Year 2, up to a maximum contribution of 32% in Year 4. However, the employer and union may negotiate the contribution level such that the employee at issue makes a 2% contribution toward his or her premium costs in Year 1, and a 22% contribution in Year 2. Negotiating such a schedule should achieve the same or even a greater amount of savings than set forth in the Act's contribution schedule after Year 2, but at a different recovery rate. Alternatively, the parties might negotiate a change in insurance benefits and a lesser employee contribution which results in the same or greater savings as the statutory scheme. In order to establish such an alternative arrangement, a board of education must file a certification with the Department of Education and with the Division of Pensions and Benefits in the Department of the Treasury attesting that the savings under a negotiated schedule will equal or exceed that in the Act. The Department of Education must pre-approve the contribution schedule prior to its implementation. The application will be deemed approved if the Department does not reject it within 30 days of the application's submission.

Although the Act's health coverage contribution requirements "sunset" in 2014 – at which time the health contributions will be deemed incorporated in all collective negotiations agreements but will be negotiable – any public employer which has not fully implemented the mandatory contribution provisions for a particular collective negotiations unit by July, 2014 must continue to do so until the full fourth-year contribution level has been reached.

It is clear that S2937 impacts not only school districts and their employees, but employer-employee relations and the collective bargaining process for all public entities in the State of New Jersey. If you have any questions regarding the implementation or effect of S2937 on your District, please do not hesitate to contact our school law attorneys at SPSK.