

# MEMORANDUM #33, 2011

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## MEMORANDUM

TO: All Retirement Boards

FROM: Joseph E. Connarton, Executive Director

RE: Regular Compensation

DATE: November 23, 2011

On June 16, 2009, Governor Patrick signed Chapter 21 of the Acts of 2009, “An Act Providing Responsible Reforms in the Pension System.” Among other things, Chapter 21 of the Acts of 2009 changed the definition of “regular compensation” for payments made after June 30, 2009. Since that time, PERAC has enacted new regulations and the Appeals Court of Massachusetts has issued a decision further limiting what may be included in regular compensation for retirement purposes.

PERAC has issued several memoranda offering guidance regarding the implementation of Chapter 21 of the Acts of 2009, provided trainings, and made presentations at the semi-annual MACRS conferences on the issue of what is to be included in regular compensation for retirement purposes. Certain questions have persisted, however, and the purpose of this memorandum is to follow up on recent legislative and judicial changes in regard to regular compensation.

To determine what constitutes, and what does not constitute, regular compensation on or after July 1, 2009, one must look to the statute, regulations and relevant case law. This includes:

- Massachusetts General Laws Chapter 32, Section 1, (as amended by Chapter 21 of the Acts of 2009);
- 840 CMR 15.03 (as amended May 28, 2010);
- Pelonzi v. Retirement Board of Beverly, 451 Mass. 475 (2008) and
- O’Brien v. Contributory Retirement Appeal Board, 76 Mass. App. Ct. 901 (February 18, 2010)

## WHAT ARE SOME CHARACTERISTICS OF PAYMENTS WHICH MAY BE INCLUDABLE IN REGULAR COMPENSATION?

- base salary or other base compensation
- payment for services performed
- pre-determined, non-discretionary, guaranteed payments
- paid to similarly situated employees
- payment for the character of the work
- payment for an employee’s length of service
- payment for the time at which work takes place

- educational incentives
- payments for holding certification, licensing, training
- payments made as a percentage of back pay

## **WHAT IS EXCLUDED FROM REGULAR COMPENSATION BY STATUTE, REGULATION AND CASE LAW?**

Most of the following were already excluded from regular compensation by statute prior to Chapter 21 of the Acts of 2009:

- overtime
- commissions
- bonuses, other than cost of living bonuses
- amounts derived from salary enhancements or salary augmentation plans
- indirect, in-kind or other payments for such items as:

- = housing or lodging
- = travel
- = clothing allowances
- = annuities

- welfare benefits
- lump sum buyouts for workers' compensation
- job-related expense payments
- automobile usage
- insurance premiums
- dependent care assistance
- 1-time lump sum payments in lieu of or for unused vacation or sick leave
- payment for termination, severance, dismissal
- any amounts payable as premiums for working holidays

= certain employees excepted

- early retirement incentives
- any other payment made as a result of the employer having knowledge of the member's retirement
- tuition
- payments in kind
- all payments other than payment received by an individual from his employing unit for services rendered to such employing unit, regardless of taxability

## **WHAT MUST BE CONSIDERED IN DETERMINING WHETHER OR NOT A PAYMENT WILL BE INCLUDED IN A PERSON'S REGULAR COMPENSATION?**

When questions arise regarding whether something should be included in regular compensation or not, retirement boards should consider the following:

- Is the payment one which meets one of the criteria of regular compensation?
- Is the payment for service provided to the employer by the employee?
- Is the payment part of the base salary of the employee?
- Is the payment included in the base compensation of the employee, meaning it is paid on an annual basis, even though it does not become part of the base salary?
- Is the payment excluded by either the statutory or regulatory definition of regular compensation or by the case law?

- Is the payment for services or for a tool supplied to the employee for the employer's convenience?

**IF A PAYMENT IS INCLUDED IN BASE SALARY, IS THAT PAYMENT AUTOMATICALLY CONSIDERED REGULAR COMPENSATION?**

As a preliminary matter, it is important to note that the employer and employee do not get to announce that a given payment is regular compensation. The determination of whether a payment is regular compensation resides with the statute, the regulations and the case law.

That being said, the inclusion of a payment in base salary does not necessarily mean that that payment should be included in regular compensation for retirement purposes. A retirement board should first look at whether a payment meets one of the criteria of regular compensation. After the board determines that a payment could fit those criteria, then the inquiry becomes whether that payment has been explicitly excluded by the statute, the regulations or case law.

**MUST PAYMENTS BE INCLUDED IN THE BASE SALARY IN ORDER TO BECOME PART OF REGULAR COMPENSATION? FOR EXAMPLE, IF A HAZARDOUS DUTY STIPEND IS PAID ANNUALLY, IS THAT REGULAR COMPENSATION ALTHOUGH IT DOES NOT BECOME PART OF THE BASE SALARY?**

Regular compensation is now defined as "compensation received exclusively as wages by an employee for services performed in the course of employment for his employer." Wages are defined in G.L. c. 32, § 1 as "the base salary or other base compensation of an employee paid to that employee for employment by an employer..." There is a difference between "base salary" and "base compensation" or there would have been no need for the Legislature to include both terms. It follows then that a payment could be "base compensation" and regular compensation without being rolled into the "base salary" year after year.

The analysis of whether a payment is to be included in regular compensation must always begin with the question of whether such a payment could be classified as regular compensation. As to the question above, a hazardous pay stipend could be regular compensation ("the character of the work" see 840 CMR 15.03 (3) (b)). Then an analysis must be conducted as to whether or not it should be excluded from regular compensation. One time payments, or payments in the nature of a bonus, must be excluded from regular compensation. In the example given above, the payment is paid annually. Therefore, it would be considered regular compensation even though it does not become part of the base salary. The hazardous duty pay would be part of the base compensation of the employee, and so would be includable in regular compensation.

**A LIBRARY WORKER WORKS 30 HOURS A WEEK, BUT OCCASIONALLY WORKS 4 TO 6 HOURS BEYOND THAT IN A WEEK. ARE THOSE 4 TO 6 HOURS EXCLUDABLE FROM REGULAR COMPENSATION?**

One of the enduring characteristics of regular compensation is predictability. The regulation in regard to pre-July 1, 2009 payments provides that to be regular compensation a payment must be "recurrent, repeated and of indefinite duration." In the place of "recurrent, repeated and indefinite duration" the new regulation in effect for the time period of July 1, 2009 onward reflects this predictably concept with the terms "base salary," "base compensation" and "pre-determined, non-discretionary, guaranteed payments."

The new regulation, and the new statute for that matter, specifically exclude "amounts derived from salary enhancements or salary augmentation plans which will recur for a limited or definite term." Although a person working a couple of extra hours now and then is not a salary augmentation plan, the principle remains the same. The resulting pay increase would be a payment of a limited term, a payment which is not a part of the person's regular pay, and so should be excluded from regular compensation.

## **WHY ARE ITEMS SUCH AS A CAR ALLOWANCE OR A NAME TAG ALLOWANCE NO LONGER INCLUDABLE IN REGULAR COMPENSATION?**

On February 18, 2010, the Appeals Court of Massachusetts issued a decision in the case of O'Brien, supra. Expanding on certain language in the Supreme Judicial Court case of Pelonzi, supra, the O'Brien Court explained that tools provided by an employer to an employee as a convenience for the employer should not be considered regular compensation. At issue in O'Brien was a clothing allowance, and at issue in Pelonzi was the personal use value of an employer-supplied automobile. As the Appeals Court found in O'Brien:

Pelonzi effectively forecloses O'Brien's claim that the uniform allowance qualifies as "regular compensation" for the purpose of computing the retirement allowance to which he is entitled. O'Brien's uniform allowance was not intended by his employer to compensate him "for his service," but rather "it was given to him to use" in connection with his official duties and job title as a correction officer. [Citations omitted].

The definition of regular compensation being keyed to services of an employee provided to an employer, the question of whether a payment is for a service or a tool must be answered in conducting an analysis of whether a given payment qualifies as regular compensation. This analysis extends to any payment which may be a "tool" supplied to an employee for the employer's convenience.

## **WHEN IS "STANDBY" PAY INCLUDABLE IN REGULAR COMPENSATION?**

Some examples may prove useful.

In "Office A" someone must be on standby each weekend. Four people work in Office A, and all four people rotate this duty, each of them being on standby every fourth weekend.

In "Office B" each employee must be on standby once every three weeks.

In "Office C" each employee is required to be on standby every other Saturday.

In each case, if a situation arises in their office when they are on standby, they must be prepared to address such a situation. In order to be alerted as conditions arise, they carry a beeper, and must curtail their activities in certain respects, i.e., not leaving the city limits.

In each instance above, the pay received for standby services would be regular compensation because the employee is performing a service to the employer. The payments are pre-determined, non-discretionary and guaranteed, in addition to being paid to similarly situated employees.

If you have any questions, please do not hesitate to contact this office.

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