TO: Members of the Legislative Commission on Pensions and Retirement

FROM: Lawrence A. Martin, Executive Director

RE: S.F. 435 (Betzold); H.F. 2114 (Smith); Clarification and Updating of Omitted Salary Deduction Recovery Provisions

DATE: March 28, 2005

Summary of S.F. 435 (Betzold); H.F. 2114 (Smith)

S.F. 435 (Betzold); H.F. 2114 (Smith) amends the omitted salary deduction recovery portions of Minnesota Statutes, Chapters 352 (General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General) and Correctional Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Correctional)), 352B (State Patrol Plan), 353 (General Employee Retirement Plan of the Public Employees Retirement Association (PERA-General) and Public Employees Police and Fire Plan (PERA-P&F)), 353E (PERA Local Government Correctional Service Retirement Plan (PERA-Correctional)), 354 (Teachers Retirement Association (TRA)), 354A (first class city teacher retirement fund associations), 422A (Minneapolis Employees Retirement Fund (MERF)), and 490 (Uniform Judges Retirement Plan) by updating the language and style of the omitted salary deduction recovery provisions and by making the provisions more uniform.

Background Information on Omitted Salary Deductions

Minnesota public pension plans, with the exception of volunteer firefighter relief associations, are contributory retirement plans. Contributory retirement plans are retirement plans where the active membership participates in the funding of the retirement plan through mandatory member contributions. Public sector pension plans are typically contributory retirement plans, while private sector pension plans are typically noncontributory retirement plans.

In Minnesota, the Commission's policy in setting the member contribution rates has been to require general employee retirement plan member contributions to equal at least one-half of the actuarial normal cost of the plan and to require public safety employee retirement plan member contributions to equal 40 percent of the actuarial cost of the plan.

The various retirement plans provide for collecting the mandatory member contributions by payroll deductions by the employing unit.

A primary issue is the issue of the member responsibility for the payment of any omitted deduction amount. Since the payment and receipt of member deductions triggers the crediting of allowable service for vesting, benefit eligibility, and benefit calculation purposes, when there are omitted deductions, the plan member will suffer the consequences and has an interest in making necessary corrections. Two of the three statewide major pension plans provide for the member payment of omitted member deductions, but Teachers Retirement Association (TRA), the three first class city teacher retirement fund associations, and MERF have no comparable authority.

Another significant issue is the issue of the employer responsibility for the payment of any omitted deduction amount. There is considerable variability in the employer authority or requirement for the payment of omitted member deductions, with no employer payment provision for MERF, with an immediate automatic employer responsibility for the four teacher retirement plans, and a variable requirement for MSRS-General and PERA-General after a certain period of time without member payment. It is unclear what the policy basis might be for treating various plan members differently and more advantageously.

Another issue of significance is the issue of whether or not there should be a limitation on the payment of omitted deductions and, if there should be a limit, the length until that limit is met. The seven plans differ, with no limit for MSRS-General and MERF, a three-year limit for PERA-General and the first class city teacher retirement fund associations, and a 46-year limit (1957) for TRA. The differences have no specified or easily inferred policy basis. Consideration should be given to treating all public pension plan members consistently in whether and when omitted deductions can be corrected.

If the required payroll deduction of a member contribution does not occur, it normally would be caused by an employing unit accounting error. Most retirement plans, but not all plans, have omitted member deduction recovery requirements, but those requirements vary between plans. The following summarizes the difference between major aspects of the omitted deduction provisions of the various general employee retirement plans:

Plan	Omitted Deduction – Member Payment
MSRS-General	If deduction is not taken for 60 days or less, deduction is to be made from later payroll abstract. [Minnesota Statutes, Section 352.04, Subdivision 8]
PERA-General	Omission of a deduction must be immediately reported to PERA, with payment of the omitted deduction consistent with PERA executive director reporting procedures and methods. If the entire deduction omission period is 60 days or less, the employer may report and submit omitted deduction payment to PERA under regular reporting and remittance procedures. [Minnesota Statutes, Section 353.27, Subdivision 12]
TRA	Omitted deductions after 6/30/1957 and before 7/1/1991 may be paid any time before retirement by the member, plus annual compound interest at 8.5 percent from the end of the fiscal year in which the shortage occurred to the date of payment, with formula service credit downwardly adjusted if the shortage is not paid. [Minnesota Statutes, Section 354.50, Subdivision 5]
DTRFA	No requirement for member payment of omitted deductions.
MTRFA	No requirement for member payment of omitted deductions.
SPTRFA	No requirement for member payment of omitted deductions.
MERF	No specific provision.

Plan	Omitted Deduction – Employer Payment
MSRS-General	If deduction is not taken for more than 60 days, employer is obligated to pay both member and employer contribution plus 8.5 percent of the total annual amount if under one year or interest at the compound annual rate of 8.5 percent if period exceeds one year. [Minnesota Statutes, Section 352.04, Subdivision 8]
PERA-General	If deduction is omitted for more than 60 days, the employer must furnish sufficient data to allow PERA to determine omitted amounts, future deductions must be made, and the employing unit required to pay the omitted deduction amount, plus the associated employer contribution amounts, and interest on the total at the compound interest rate of 8.5 percent from the date the amount was first payable to the date of actual payment. The employer may not hold the member liable for the omitted deduction amount or attempt to recover the amount from the member. [Minnesota Statutes, Section 353.27, Subdivision 12]
TRA	Omitted deductions after 6/30/1981 are the sole obligation of the employing unit and must be paid following notification by TRA with annual compound interest at the rate of 8.5 percent from the end of the fiscal year in which the shortage occurred to the date of the payment. The employer must pay the employer contribution applicable to omitted deductions after 6/30/1986. [Minnesota Statutes, Section 354.50, Subdivision 5]
DTRFA	Omitted deductions are the sole obligation of the employing unit and must be paid following notification by the plan with monthly compound interest at the rate of 0.71 percent from the date the payment was due to the date that payment is made, with a minimum interest charge of $10. [Minnesota Statutes, Section 354A.12, Subdivision 1a]
MTRFA	Omitted deductions are the sole obligation of the employing unit and must be paid following notification by the plan with monthly compound interest at the rate of 0.71 percent from the date the payment was due to the date that payment is made, with a minimum interest charge of $10. [Minnesota Statutes, Section 354A.12, Subdivision 1a]
SPTRFA	Omitted deductions are the sole obligation of the employing unit and must be paid following notification by the plan with monthly compound interest at the rate of 0.71 percent from the date the payment was due to the date that payment is made, with a minimum interest charge of $10. [Minnesota Statutes, Section 354A.12, Subdivision 1a]
MERF	No specific provision.

Plan	Omitted Deduction For Subsequently Terminating Employee
MSRS-General	For omitted member deduction for employee who terminates before the omission is corrected, and the period is 60 days or under, no member contribution is collected, but employer is obligated to pay the employer contribution, and the unpaid member contribution is considered to be a refund open for repayment in the event that the person returns to State employment. If the period is over 60 days, employer is obligated to pay member and employer contributions, plus amount in lieu of interest or interest at 8.5 percent. [Minnesota Statutes, Section 352.04, Subdivision 8]
PERA-General	If there are omitted member deductions for a person who has terminated, no omitted member deductions are payable, but the employing unit is liable for the employer contributions associated with the member deductions, plus interest at a compound annual rate of 8.5 percent. A terminated member for whom deductions were omitted or a current member with a prior period covered by an omitted deduction period may pay the omitted deduction amount within a period of six months after initial notification of eligibility to pay the amount, or, if the person is covered by another Minnesota public pension plan, within six months of the termination of subsequent public service. If the terminating member is immediately eligible to begin receipt of an annuity, the terminating member shall pay the omitted deduction amount within six months of notification, or forfeit the payment right, and the employing unit is obligated to pay the omitted employer contributions associated with the deductions, plus interest at an annual compound rate of 8.5 percent. [Minnesota Statutes, Section 353.27, Subdivisions 12, 12a, and 12b]
TRA	No specific provision.
DTRFA	No specific provision.
MTRFA	No specific provision.
SPTRFA	No specific provision.

Plan	Omitted Deduction For Subsequently Terminating Employee
MERF	No specific provision.

Plan	Time Limitation on Correcting Omitted Deductions
MSRS-General	No provision.
PERA-General	PERA not allowed to recover omitted deductions or contributions due for more than three calendar years after the calendar year in which the omission occurred. No payments of omissions may be accepted by PERA unless PERA has begun action to recover, which occurs when PERA mails written correspondence requesting pertinent data to allow for the computation of the omission. [Minnesota Statutes, Section 353.27, Subdivision 12]
TRA	Omitted deductions dating before 7/1/1957 may not be paid. [Minnesota Statutes, Section 354.51, Subdivision 5]
DTRFA	Omitted deductions due for more than three years after the date of the omission are not payable. [Minnesota Statutes, Section 354A12, Subdivision 1a]
MTRFA	Omitted deductions due for more than three years after the date of the omission are not payable. [Minnesota Statutes, Section 354A12, Subdivision 1a]
SPTRFA	Omitted deductions due for more than three years after the date of the omission are not payable. [Minnesota Statutes, Section 354A12, Subdivision 1a]
MERF	No specific provision.

Discussion and Analysis

S.F. 435 (Betzold); H.F. 2114 (Smith) modifies the omitted member deduction recovery provisions of the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General), the Correctional Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Correctional), the State Patrol Retirement Plan, the General Employee Retirement Plan of the Public Employees Retirement Association (PERA-General), the Public Employees Police and Fire Plan (PERA-P&F), the PERA Local Government Correctional Service Retirement Plan (PERA-Correctional), the Teachers Retirement Association (TRA), the first class city teacher retirement fund associations, the Minneapolis Employees Retirement Fund (MERF), and the Uniform Judicial Retirement Plan by making the following changes:

a. Adds Omitted Deduction Recovery Provisions for Four Retirement Plans. Includes in a consistent omitted member contribution recovery provision four retirement plans that lack the provision, the State Patrol Retirement Plan, the Local Government Correctional Retirement Plan, MERF, and the Uniform Judicial Retirement Plan;

b. Standardizes Member Responsibility for Omitted Deductions for Five Retirement Plans. Requires member payment of omitted member deductions during the first 60 days following the omission for TRA, the three first class city teacher retirement fund associations, and MERF;

c. Adds Employer Responsibility for Paying Omitted Deductions for Three Retirement Plans. Requires employer payment of omitted member deductions after the first 60 days following the omission for the State Patrol Retirement Plan, MERF, and the Uniform Judicial Retirement Plan;

d. Standardizes Employer Omitted Deductions Payment Responsibility for Four Retirement Plans. Delays the employer payment of omitted member deductions requirement until after the first 60 days following the omission for TRA and the three first class city teacher retirement fund associations; and

e. Consistent Three-Year Limit on Recovery for Two Retirement Plans. Imposes a three-year limitation on the potential recovery of omitted member deductions for MSRS-General and TRA.

S.F. 435 (Betzold); H.F. 2114 (Smith) raises several pension and related public policy issues that may merit Commission consideration and discussion, as follows:

1. Appropriateness of Adding Omitted Deduction Recovery Provisions to Plans Lacking the Provisions. The policy issue is the appropriateness of adding omitted member contribution deduction recovery provisions to those plans that lack the recovery provisions. Currently, the State Patrol Retirement Plan, MERF, and the Uniform Judicial Retirement Plan lack any provision governing the recovery of omitted member contribution deductions and the Local Government Correctional Retirement Plan lacks some portions of the omitted deduction recovery provisions. The lack of omitted deduction recovery provisions may reflect the absence of any past accounting or payment errors in making member contribution deductions. If so, errors could occur in the future and the addition of an omitted deduction recovery provision may serve as good insurance for the future. If past employer accounting

or payment errors have occurred, but have been handled in a less formal or a less clear manner, the procedures used then may have been deficient and the retirement plan would be better served with a specific statutory process.

2. Appropriateness of Requiring Members to Pay Omitted Deductions Under 61 Days. The policy issue is the appropriateness of mandating retirement plan members to pay omitted member deductions when the omission is no more than 60 days. Currently, four plans with omitted deduction provisions lack any requirement for plan members to pay omitted deductions, with the employer immediately responsible for all omitted deductions in TRA and the three first class city teacher retirement fund associations. If some retirement plans require members to pay omitted deductions for up to 60 days while others immediately shift the burden to employers, some plan members are treated more advantageously than others are and some employers are treated less advantageously than others. If there is a rational basis for that disparate treatment, then the differential treatment is not problematic. However, the differential treatment in this instance does not appear to have any clear policy basis or policy advantage.

3. Appropriateness of Imposing the Employer Payment Requirement for Omitted Deductions. The policy issue is the appropriateness of requiring some employers to newly bear the burden of paying omitted member contribution deductions. Currently, the Department of Public Safety, the Department of Natural Resources, and the Department of Corrections with respect to State Patrol Retirement Plan members, the City of Minneapolis, the Metropolitan Airports Commission, the Metropolitan Council, and the Minnesota State Colleges and Universities System with respect to MERF members, and the Judicial Branch with respect to judges are not required to ever pay an omitted member deduction amount no matter how the error occurred or for how long the error continued. Since plan members have little or no control over the member contribution deduction process, but employers do, it would appear to be appropriate to give employing units a financial incentive to perform the deduction process properly or to correct errors in the process quickly. Also, since all employing units are obligated to pay omitted member contributions for at least some employees (i.e. the Department of Public Safety would owe omitted member deductions for its MSRS-General covered employees even if it does not owe them for state troopers), making employing units obligated for all omitted member deductions is not an unprecedented step and achieves some consistency.

4. Appropriateness of Delaying Some Employer Omitted Member Deduction Payments. The policy issue is the appropriateness of postponing the imposition of the employer obligation to pay omitted member deductions for teacher retirement plans. The four teacher retirement plans currently have immediate requirements for the employer payment of omitted member deductions, but the payment requirement would be delayed to after 60 days of omission, consistent with the other plans. As a general rule, absent some more overriding policy concerns that the Commission staff is unable to identify, consistent treatment for all employing units for all employees seems to be an appropriate course of action in this matter.

5. Appropriateness of Imposing a Three-Year Limitation on the Recovery of Omitted Member Deductions. The policy issue is the appropriateness of imposing a three-year limitation on the recovery of omitted member deductions. Currently, MSRS-General and TRA do not have any limit on the recovery of omitted member deductions, while most other retirement plans have a three-year limitation. Omitted member deduction recoveries constitute a service credit purchase at a reduced (subsidized) contribution rate if the recovery is delayed beyond a limited period of time. Consistency would argue for the imposition of a uniform limit unless there are overriding contrary policy concerns.