

Unreported Employee and Employer Contributions on Employer-Paid Deferred Compensation Amounts



The outstanding issue to be resolved following the Court of Appeals decision on the *Salary Determination Affecting Retired and Active Employees of the City of Duluth* is addressed in Section 2, Article 14 of this year's Omnibus Pension Bill, House File 1951. While the Court and the Administrative Law Judge's findings both directed PERA to collect employee and employer contributions on the City's employer-paid deferred compensation amounts deposited into current and former City employees' accounts from August 2007 through December 31, 2011, there was nothing in our governing statute guiding us on the best approach to doing so.

We want to ensure that everyone understands why we are using an end date of December 31, 2011. We were informed that with contracts which went into effect January 1, 2012, this employer-paid benefit became part of a cafeteria plan arrangement offered to the City of Duluth's employees. Under Minnesota Statutes, Section 353.01, subdivision 10(b)(8), "employer-paid amounts used by an employee toward ..., cafeteria plan, ..." are not salary for PERA reporting purposes. Thus, only the employer deposits into employees' deferred compensation accounts made before January 1, 2012, can be included as salary for PERA benefit and contribution purposes.

The legislation allows individual City employees to choose whether they want to make employee contributions on the deferred compensation deposits made into their individual accounts by the City from August 2007 through December 31, 2011. As staff explained to the Board, requiring everyone for whom the City stopped reporting these amounts as salary to make past contributions seemed unreasonable. The Board agreed that this proposed solution would be the most equitable approach in addressing this issue because it wasn't reasonable to require individuals – or the City -- to make all of the past contributions on amounts that would not be included in some individuals' highest five years of earnings on which pensions would be determined.

PERA moved forward in September 2013 with collecting contributions from individuals already retired from employment with the City with a benefit effective date up to and including July 1, 2013. It was clear that almost all of these individuals wanted the deferred compensation deposits included in the calculation of their benefits and those adjustments made. The City agreed to pay the employer contributions upon receipt of employee payments from that group of benefit recipients. By December 1, 2013, PERA received employee and employer contributions, adjusted benefit payments and made retroactive payments to 156 of 176 eligible benefit recipients. Of the remaining 20 from that group of former employees, staff determined five individuals' benefits would not be adjusted, thus there was no value added to making the contributions. The other 15 will receive notice with the letters going out this June to all current and former employees of the City authorized to make their contributions.

Following is a list of questions and responses we hope will address most questions about PERA's next and final steps in bringing this issue to closure.

Q: Didn't the Court of Appeals require PERA to collect all employee and employer contributions on employer-paid deferred compensation deposits the City made into employees' accounts from August 2007 until the City negotiated these payments as part of a cafeteria plan?

A: The Court's decision was not clearly stated on how to address contributions that had not been made to PERA. The issue regarding "*The Determination Affecting Retired and Active Employees of the City of Duluth*" before the Court of Appeals on which the Court ruled was limited to the period from 1995 through July 2007. Neither the Administrative Law Judge nor the Court of Appeals considered or specifically ruled on whether PERA's policy was longstanding as applied to the period of August 2007 through the recent law change.

There is nothing in current statutes that provides a clear direction on how to deal with the issue of collecting contributions on unreported amounts deposited by the City of Duluth into current and former employees' deferred compensation accounts from August 2007 until recent changes in the collective bargaining agreements. Therefore, PERA sought direction through special legislation that is supported by the City.

Q: You have referred to deferred compensation deposits made from August 2007 through December 31, 2011. Isn't the date of the 2013 law change to PERA's definition of salary the date that should be used?

A: PERA received confirmation from the City that beginning with contracts in effect January 1, 2012 and forward, the amount of money contributed to an employee's deferred compensation account is part of a new cafeteria plan offered by the City and negotiated with the employees' bargaining units. PERA's statute [353.01, subdivision 10 (b)(8)] states that employer paid amounts used by an employee toward ... cafeteria plans, ... are not salary for pension purposes.

Q: Specifically, what does the 2014 Omnibus Pension Bill say about the Duluth salary issue?

A: Any current or former City of Duluth employees who had amounts deposited into their deferred compensation accounts by the City may make contributions on those amounts upon receipt of notice from PERA of the amount due. Specifically, the law directs that:

1. The individuals must make contributions on all deposits made from August 2007 through December 31, 2011, or date of termination of employment, whichever is earlier. Individuals cannot choose to make contributions for only part of this period of time.
2. Upon receipt of the employee payment, PERA must bill the City of Duluth for the employer amount due on behalf of that individual.
3. No interest will be charged to the employee or the employer.

4. Any individuals already receiving benefits – who were not included in the group of recipients whose benefits were adjusted in late 2013 – must have their benefits adjusted and will be paid any retroactive payments to which they may be entitled, upon receipt of the employee and employer contributions.
5. The opportunity to make these payments expires on October 31, 2014.

Q: Why must employees pay contributions on the entire period of past deposits to their deferred compensation accounts?

A: Had PERA not directed the City to stop withholding employee deductions, making employer contributions and reporting these deposits as salary, the individuals would have had deductions taken and these amounts would have been included as salary.

If we allowed them to make employee contributions on only those months of deferred compensation deposits that fall within their high five years' salary determination, we would be allowing the equivalent of "spiking." In other words, we'd allow them the benefit of the higher salary but not require them to make the "total" contribution that would have otherwise been made had we not ordered the City to stop including these amounts as salary.

Q: Why was special legislation needed to address a ruling by the Court of Appeals?

A: We looked at a couple perspectives on this. First of all, the ruling from the Court of Appeals, the memorandum from the Administrative Law Judge and PERA's governing statutes provided no clear direction on how to resolve the unpaid contributions on City-paid deferred compensation deposits. Secondly, since the record before the Court only included discussion of the period 1995 through July 2007, the Court did not have any helpful information on which to provide clear direction beyond that period.

We also considered that making contributions on these employer-paid deferred compensation deposits would not benefit everyone. If we required all employees (and the City) to make contributions on deferred compensation that would not add value to their PERA benefits, it was likely we'd be entangled in yet another legal challenge.

Also, the legislation clarifies that those employees who want the employer-paid deferred compensation deposits included in the salary used by PERA to determine benefits, must make contributions on all amounts deposited into their deferred comp accounts back to August 2007. An individual cannot ask to make contributions only on those deferred compensation deposits that would fall within a person's highest five years' earnings period for calculating the PERA benefit.

Q: How soon can individuals expect to receive information from PERA about what they must pay and how soon can they expect their benefits to be retroactively adjusted?

A: The calculation work is already underway. The letters will be mailed from the PERA office on June 3. For those already receiving benefits, monthly payments will be adjusted the first of the month following receipt of both the employee *and* employer contributions, but no later than December 1, 2014 – that is if an individual waits until the latest date to submit payment, October 31, 2014.

Q: What if the person was already receiving benefits but did not hear from PERA in 2013. Does this still apply?

A: We contacted only those individuals who we knew had retired between August 2007 and July 1, 2013. Individuals will receive a notice from us again and be given the opportunity to make the payment if for some reason the benefit recipient wasn't contacted in 2013, or if contacted, did not choose to make the payment at that time.

Letters will be mailed from our office on June 3 with the amount of employee contributions owed, the new value of their pensions and the amount of the retroactive payment they can expect. Payments must be made by October 31, 2014.

Q: Will PERA be sending all City employees information about this?

A: PERA received from the City all of the information needed to calculate employee and employer contribution amounts for any current or former employees who are eligible to make these payments so the deferred compensation deposits can be included as salary in the determination of the individuals' PERA benefits.

We will be sending letters from our office on June 3. Those letters will include information about the employee deductions to be paid and the amount the City will pay as well as the following:

- For former employees who are receiving benefits, or beneficiaries of former employees who are receiving benefits – the current average salary on which benefits were calculated; the change in average salary on which benefits will be calculated, if payment is made; the current monthly benefit paid; the monthly benefit if the new average salary is used to calculate benefits; and the amount of additional benefits to be paid retroactively due to the adjustment of salary.
- For former employees who terminated employment with the City, are vested, and have not withdrawn their contributions from the plan – the current average salary on which future

benefits will be calculated; the average salary on which benefits will be calculated if payment is made; the current future benefit payable; and the projected future benefit payable using the adjusted average salary.

- For current employees:
 - a. General Plan – if age 50 and over; Police and Fire Plan – if age 45 and over: the person will receive an estimate of the current average salary and the adjusted average salary, if payment is made, and estimates of the benefits payable using the average salary with and without payment of the additional contributions.
 - b. General Plan – if under age 50; Police and Fire Plan – if under age 45: the person will receive an estimate of the current average salary and the adjusted average salary, if payment is made. The letter will advise the person that since they will likely receive salary increases in the future, the adjusted average salary may not be used to calculate their future benefits.

We are scheduling letters to go out June 3.

Q: Should individuals send their pay stubs or tax records so PERA can calculate what they owe in PERA contributions?

A: No, PERA has received from the City the data on deferred compensation deposits made by the City into individuals' accounts. We have used that data to calculate employee and employer contributions owed. Any questions about the data we used should be directed to the City.

Q: If a person receives an estimate, but wants a different retirement date, will PERA staff prepare an estimate and mail it out?

A: Individuals are encouraged to use My PERA to prepare their own "what if" estimates using the average salary information in the letter, or they can call the office and speak to a member of the staff.

Q: If a person doesn't receive an estimate with the letter, will PERA staff prepare an estimate?

A: Individuals are encouraged to use My PERA to prepare their own "what if" estimates using the average salary information in the letter, or a different average salary they estimate they may earn before they retire. They can also call the office and speak to a member of the staff.

Q: How does a person make the payment of contributions owed?

A: The letter sent to everyone will include a Transmittal Form that must be returned with the payment. Payment can be made by directing a rollover of money from the person's deferred compensation (457) plan account or an IRA or Roth IRA account or with a personal check payable to PERA.

Benefit recipients cannot use the increased benefit value to incrementally pay the necessary contributions. Payment must be a one-time, lump sum through a rollover or a check payable to PERA.

Q: Will employees have an opportunity to discuss any of this information with a member of the PERA staff?

A: PERA staff from the Duluth office will conduct three introductory meetings on May 19 and will present at three more meetings on June 11 – after the individual letters have been sent to all affected current and former employees.

Q: Who can employees call at PERA with questions about this?

A: The Communications Center customer service representatives will be kept informed of the progress of completing calculations and the distribution of the letters. Employees can call our general number and speak to any of the customer service representatives about the information contained in the letter. The phone number in the metro area is (651) 296-7460, or you can call toll-free 1 800 652-9026.

Kristen and Bryan in our Duluth office can be reached at (218) 302-6121 or (218) 302-6120.

To access My PERA, go to www.mnpera.org.