



Finance & Administration Committee

California Public Employees' Retirement System

Agenda Item 6b

April 14, 2015

ITEM NAME: Proposed Regulatory Changes – Payment of Interest

PROGRAM: Customer Account Services

ITEM TYPE: Action

RECOMMENDATION

Approve the initiation of the rulemaking process to establish rules and procedures by which interest payments would be made to a defined benefit plan participant when a defined benefit plan has delayed payment in the correct amount owed to a participant beyond a reasonable administrative processing time.

EXECUTIVE SUMMARY

The proposed regulation would (1) define the circumstances under which interest should be included in retroactive payments to participants of a defined benefit plan, (2) establish what interest rate should apply, and (3) establish a fair administrative appeal process for participants to pursue claims that a defined benefit plan has failed to pay interest when required under the regulation.

STRATEGIC PLAN

This agenda item supports Strategic Goal A by making explicit certain processes and procedures for the efficient administration of pension benefits.

BACKGROUND

Under Government Code section 20160(b), "the board shall correct all actions taken as a result of errors or omissions of ... this system." Under section 20160(e), in general, "[c]orrections of errors or omissions ... shall be such that the status, rights, and obligations of all parties ... are adjusted to be the same that they would have been if the act that would have been taken, but for the error or omission, was taken at the proper time ..."

In the vast majority of cases, the defined benefit plans administered by the Board pay benefits in the correct amount within a reasonable administrative processing time (usually far less than 90 days). From time to time, however, benefits are underpaid due to a system delay that might fairly be characterized as unreasonable. In those instances, it may be appropriate to include interest with the retroactive payments owing to the participants. Including interest in such payments is consistent with the

statutory directive that “the status, rights, and obligations of all parties ... are adjusted to be the same that they would have been if the act that would have been taken, but for the error or omission, was taken at the proper time.”

In some situations, statutory law provides clear direction as to when interest should be paid to members and which interest rate should be used (for example refunds of member accounts and payments of death benefits more than 45 days after the system receives all of the information it needs to pay the death benefits). In many situations, however, statutory law does not provide clear direction as to when interest should be paid and at what rate.

ANALYSIS

The proposed regulation is intended to define the circumstances under which interest should be included in retroactive payments to participants of a defined benefit plan by drawing a distinction between ordinary administrative processing time and “wrongfully withheld” payments, as those concepts reasonably apply to the defined benefit plans administered by the Board in particular.

The proposed regulation establishes 90 days as a reasonable administrative processing time. That 90 days would not start running until (1) the right to the payment has accrued, and (2) the defined benefit plan has all of the information it needs to determine the proper amount of the payment. This 90-day processing time is more time than is needed in most circumstances. This regulation will not impact the goal to make all payments owing to participants as quickly as practicable. Most payments to participants from defined benefit plans are made well before any interest would accrue under this regulation. That would continue to be the case if this regulation is adopted by the Board.

The proposed regulation establishes a seven percent per annum simple (non-compounding) interest rate as the appropriate interest rate for delayed payments. This is the default interest rate established by Article XV, Section 1 of the California Constitution.

The proposed regulation specifies a process for participants to pursue claims that a defined benefit plan has failed to pay interest when required by the regulation. This aspect of the proposed regulation is important, because a decision as to whether interest is owed may turn on individualized factual scenarios that can vary substantially from case to case. The regulation makes use of the Board’s existing administrative appeal procedures under Board Regulation 555, *et seq.*, to ensure that there is a fair process available to participants who believe they have been denied interest owing to them.

The proposed regulation delegates authority to the Executive Officer or his or her designee to grant a participant’s claim for interest under this regulation for \$2,000 or

less, if the Executive Officer or his or her designee determines that the claim has merit. This delegation of authority is proposed so that staff need not expend unwarranted resources on administrative appeals under this regulation.

The proposed regulation specifies that a participant must make a claim for interest under this regulation within three years of receiving the payment that the participant claims should have included interest. This provision will help staff avoid expending resources on stale claims.

Additionally, while not addressed in this proposed regulation, staff will be evaluating whether there should be another regulation to address the collection of interest from participants who receive overpayments from funds administered by the board.

BUDGET AND FISCAL IMPACTS

The fiscal impact of the proposed regulation, if adopted, is difficult to quantify, but likely minimal. The proposed regulation would result in interest payments on some payments to participants that would not otherwise be made. The instances in which payments would be subject to the accrual of interest should be rare, however, as the vast majority of all participant payments that would be subject to this regulation are made within the time frames contemplated by the proposed regulation. Further, the additional costs associated with the regulation may be offset by the savings resulting from the efficiency and predictability that the regulation would bring to the defined benefit plans administered by the Board.

BENEFITS/RISKS

The primary benefit of approving the proposed regulation is that it will provide clear and transparent guidelines for staff and participants of defined benefit plans administered by the Board. Further, it should help resolve legal disputes with members and beneficiaries claiming entitlement to interest.

The primary risk of the proposed regulation is that administration of the regulation will consume staff time and resources, but staff believes that this risk can be mitigated through an efficient and reasonable administration of the proposed regulation.

ATTACHMENTS

Attachment 1 – Proposed Regulatory Action by CalPERS

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