



Board of Retirement Regular Meeting

Sacramento County Employees' Retirement System

Agenda Item 3

MEETING DATE: September 16, 2020

SUBJECT: Error Correction Policy

SUBMITTED FOR: ___ Consent X Deliberation and Action ___ Receive and File

RECOMMENDATION

Staff recommends the Board approve an Error Correction Policy (Policy) that sets out a framework for correcting errors in connection with the payment of member benefits and the collection of member contributions. Staff also recommends the Board rescind the Member Contribution Underpayment Collection Policy (Policy No. 009) as superseded by the Policy.

PURPOSE

This item supports the Strategic Management Plan by providing transparent communication to stakeholders regarding roles and responsibilities.

BACKGROUND

In the course of administering the County Employees' Retirement Law, SCERS may on occasion pay benefits in an amount less than or in excess of what was owed to the member under the law. Similarly, SCERS may on occasion collect member contributions in an amount less than or in excess of what the law requires. Such errors may be due to a variety of causes: a mathematical miscalculation; staff's reliance on a misrepresentation by a member or beneficiary; judicial disapproval of a long-time SCERS practice or legal interpretation; a failure to discontinue or decrease payments after some benefits-terminating event (e.g., continued payment of a retirement allowance after the death of a member); and more.

When errors occur, SCERS has a legal duty to take reasonable corrective actions in a timely manner. That duty flows from: (1) the constitutional prohibition against gift of public funds (Cal. Const., Sec. 6, Art. XVI); (2) Government Code section 31539; (3) SCERS' fiduciary duty to its members; (4) SCERS' duty to safeguard fund assets; and (5) SCERS' compliance obligations to the IRS as a tax-qualified retirement plan. Generally, errors must be corrected both prospectively and retroactively – that is, by adjusting benefits and contributions on a going forward basis, and by recouping past over-payments and refunding past over-collections.

Mindful of its legal duties, SCERS has over the years developed various practices and processes for carrying out error correction. The proposed Error Correction Policy captures, and expands upon, those historical practices in a single comprehensive document.

DISCUSSION

There are several advantages to adopting a publicly-available Policy that clearly sets out SCERS' error correction authority and procedures. Foremost, the Policy memorializes best practices for staff and lays out criteria and considerations to guide decision-making. The Policy also educates members about their rights and responsibilities, and about the administrative procedure that governs the error correction process. Finally, the Policy demonstrates SCERS' commitment to compliance with IRS rules pertaining to error correction by a tax-qualified retirement plan.

The Policy addresses the appropriate prospective and retroactive corrections for three categories of errors: (1) overpayment of benefits, (2) over-collection and under-collection of contributions, and (3) the underpayment of benefits. Of these, the first category is the most common and the most challenging to correct. This is particularly true if the recipient of the overpayment does not receive an ongoing stream of benefits from which SCERS can deduct.

Generally, the Policy calls for SCERS to take all reasonable steps to recover 100 percent of the overpayment from the member within some reasonable period of time (e.g., the same period of time over which the overpayment occurred). This is true whether the overpayment was due to member fraud, inadvertent error by SCERS, or inadvertent error by the member. However, the Policy also allows the CEO and/or the Board to approve an agreement of compromise that relieves the member from repaying some or all of the overpayment. In deciding whether to compromise, SCERS should consider factors such as: the amount of the overpayment, whether the member has valid legal defenses, principles of fairness, the applicable statute of limitations, the cost of pursuing repayment versus the likelihood of recovery, and the solvency of the recipient. In unusual circumstances (e.g., a system-wide overpayment due to a disapproved statutory interpretation by SCERS) the Board may authorize staff not to seek any repayment at all. *City of Oakland v. Oakland Police and Fire Retirement System*, 224 Cal.App.4th 210 (2014); *Blaser v. State Teachers' Retirement System*, 37 Cal.App.5th 349 (2019).

SCERS' experience has been it is usually possible to come to terms with a member on a mutually acceptable repayment plan. But when that does not occur, an actionable administrative decision about repayment must be made, and a process provided to the member for voicing objections. The Error Correction Policy includes a robust notice, hearing, and appeals procedure that provides due process to the member and that, at its conclusion, results in an enforceable final administrative decision.

Finally, the Policy gives the Board an important oversight function. Under the Policy, situations involving overpaid benefits of \$50,000 or more must be brought to the Board's attention. In addition, the Chief Executive Officer will annually present a report about the collection status of overpaid benefits and underpaid contributions.

Attachment

- Error Correction Policy

Prepared by:

Reviewed by:

/S/

/S/

Stephen Lau
General Counsel

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Chief Executive Officer



ERROR CORRECTION POLICY

PURPOSE

The purpose of this policy is to establish a framework for correcting errors in connection with the payment of member benefits and the collection of member contributions. In particular, this policy sets out SCERS' authority and procedures for making prospective corrections (i.e., adjusting benefits and contributions on a going forward basis) and retroactive corrections (i.e., recouping past over-payments and refunding past over-collections). In addition, this policy protects SCERS' tax-qualified status by setting out an error correction protocol consistent with the Internal Revenue Service Employer Plans Compliance Resolution System.

POLICY

This policy pertains to three categories of errors caused by the acts and omissions of SCERS and/or SCERS members: (1) overpayment of member benefits; (2) the over-collection or under-collection of member contributions; and (3) the underpayment of member benefits. For the avoidance of doubt, this policy, and the procedures therein, do not apply to errors, under-collections, over-collections, and other correctible events driven by employer operations (e.g., usual and customary employer reporting adjustments for member contributions).

All references to "interest" below refers to the semiannual interest crediting rate for Member Reserves for the period(s) to be corrected.

A. Correcting the Overpayment of Member Benefits

On occasion, SCERS may discover that it has paid a retirement allowance or other benefit to a member or beneficiary (collectively, "member") in excess of what is owed under the law. When that occurs, SCERS shall take steps to make prospective and retroactive corrections as soon as practicable in accordance with this policy. Consistent with SCERS' status as a tax-qualified retirement plan, SCERS will make error corrections using any methods consistent with the IRS' Employee Plans Compliance Resolution System under Revenue Procedure 2019-19 or any subsequent guidance promulgated by the Secretary of the Treasury for correcting qualification errors.

1. Prospective Corrections (Adjusting Benefits Going Forward)

With respect to prospective corrections, SCERS shall adjust the amount of the member's benefit to ensure that, going forward, the member receives a benefit that does not exceed what is owed under the law.

Where there has been a system-wide error affecting a significant number of members, SCERS may encounter practical limitations on its ability to gather the facts necessary to recreate the members' final compensation and achieve perfect prospective corrections. If, in the judgment of the Board, the cost of such fact-gathering and prospective correction exceeds what is administratively prudent under the circumstances, the Board may authorize alternative corrective actions so long as they reasonably protect members' rights and are consistent with the prudent administration of fund assets and IRS correction principles.

2. Retroactive Corrections (Recovery of Overpaid Benefits)

With respect to retroactive corrections, SCERS shall take all reasonable steps to recover and collect overpaid benefits, plus interest, from members in accordance with the following criteria:

- a. Where the overpayment of a benefit was due to fraudulent reports made or caused to be made by the member, or the member caused his or her final compensation to be improperly increased or overstated at the time of retirement, SCERS shall seek recovery of such overpayments from the member. See Gov. Code § 31539. SCERS may use any and all collection methods and legal remedies that, in its judgment, would facilitate a full recovery. SCERS may seek to recover overpayments from the member in a lump sum or by installment plan (which may, but need not be, over the same period of time that the error occurred). SCERS may also offset the amount of overpayment to be recovered against future benefit payments. SCERS may also seek recovery by adjusting the allowance so that the retired member or the retired member and his/her beneficiary will receive the actuarial equivalent of the allowance to which the member is entitled. SCERS may also institute an action against the member for declaratory, legal, and equitable relief.
- b. Where the overpayment of a benefit was due to an act or omission by SCERS, the member, or beneficiary, and the circumstances would not subject SCERS to valid equitable defenses and potential fiduciary claims by the member or beneficiary, SCERS shall seek recovery of such overpayments from the member. SCERS may use any and all collection methods and legal remedies that, in its judgment, will most likely to facilitate a full recovery, including those identified in the preceding paragraph.
- c. Where the overpayment of a benefit was due to inadvertent error by SCERS (including an inadvertent error in statutory or legal interpretation), and such error would (in the judgment of the Board and/or the Chief Executive Officer with consultation with legal counsel) subject SCERS to valid equitable defenses and potential fiduciary claims by the member, SCERS need not seek to recover such overpayments from the member unless ordered to do so by the IRS and/or a final, non-appealable order of a court of competent jurisdiction. *City of Oakland v. Oakland Police and Fire Retirement System*, 224 Cal.App.4th 210 (2014); *Blaser v. State Teachers' Retirement System*, 37 Cal.App.5th 349 (2019).

SCERS shall take actions to recover overpayments in accordance with the notice and hearing procedures set out in Section D below. Although SCERS should strive to commence corrective recovery actions in a timely manner, no limitations period applies to the

administrative actions described in the paragraphs above. See *Krolikowski v. San Diego City Employees' Retirement System*, 24 Cal. App. 5th 537 (2018).

To the extent SCERS is unable to collect any overpayments from members – including under the circumstances in Section A.2.c. above – those overpayments will be reconciled through the Actuarial Accrued Liability as part of the annual actuarial valuation process.

3. Agreements of Compromise in the Collection of Overpaid Benefits

Although SCERS will generally strive to collect 100 percent of overpaid benefits, plus interest, from the overpaid member, SCERS may on occasion encounter legal and practical limitations on its ability to do so. In those situations, SCERS may enter into an agreement whereby the member repays less, or is likely to repay less, than 100 percent of overpaid benefits and interest (“agreements of compromise”). In determining whether to enter into an agreement of compromise, and in determining the extent of compromise, SCERS shall consider the following:

- The total amount of overpaid benefits received by the member;
- The total amount of overpaid benefits that the member would be relieved from returning;
- The cause of the overpayment;
- Whether, in litigation, the member would have equitable or legal defenses against repaying 100 percent of the overpaid benefits;
- Whether litigation to recover 100 percent of the overpaid benefits would be wholly or partially subject to a statute of limitations or other time bar (e.g., Code Civ. Proc. § 338; Gov. Code § 31539);
- The cost of pursuing administrative or litigation action against the member weighed against the amount of overpayment to be collected;
- Whether the member is insolvent or otherwise judgment-proof; and/or
- Any other reasonable factors stemming from SCERS' fiduciary obligations, obligations as a tax-qualified plan, and other public policy considerations.

An agreement of compromise involving overpaid benefits of \$50,000 or more requires the approval of the Board. An agreement of compromise involving overpaid benefits of less than \$50,000 requires approval of the Chief Executive Officer. Any collection shortfall arising from SCERS entering into an agreement of compromise will be reconciled through the Actuarial Accrued Liability as part of the annual actuarial valuation process.

B. Correcting Over-Collection or Under-Collection of Member Contributions

When SCERS has over-collected or under-collected member contributions, SCERS shall take steps to make prospective and retroactive corrections as soon as practicable in accordance with this policy.

In the event an active or deferred member overpaid member contributions, SCERS will refund the full overpayment amount, plus interest, to such member. In the event contributions were overpaid by a member who has since retired, the full amount of overpaid

contributions will be refunded to the member, plus interest, with any offset necessary to recover overpaid benefits, if any.

In the event of an active or deferred member underpaid his or her contributions, the full underpaid amount must be collected, plus interest, in order for the member to be entitled to his or her benefits under the law. In the event of any underpaid contributions by a retired member, the full member contribution underpayment will be recouped, plus interest, to support the continuing payment of ongoing monthly benefits supported by those contributions. SCERS may recoup the contribution underpayment from the retired member by deducting from benefits.

SCERS shall take actions to collect underpaid contributions and refund overpaid contributions in accordance with the notice and hearing procedures set out in Section D below. Although SCERS will strive to commence corrective recovery actions in a timely manner, no limitations period applies to the administrative actions described in the paragraphs above.

To the extent SCERS is unable to recoup any underpaid contributions from members as described above, the shortfall will be reconciled through the Actuarial Accrued Liability as part of the annual actuarial valuation process.

C. Correcting the Underpayment of Member Benefits

When SCERS has underpaid a retirement allowance or other benefit to a member, SCERS shall take steps to make prospective and retroactive corrections as soon as practicable in accordance with this policy.

With respect to prospective corrections, SCERS shall adjust the amount of the member's benefit to ensure that, going forward, the member receives a benefit in the amount owed under the law.

With respect to retroactive corrections, SCERS shall pay the member an amount equal to (1) the member's underpayment prior to the date of the prospective correction described in the preceding sentence, and (2) interest.

D. Error Correction Procedures

1. Notice of Correction and Administrative Appeal

SCERS shall notify members of errors, and provide an opportunity for administrative appeal, in accordance with following procedure:

- a. Upon the discovery of an error concerning the payment of benefits or collection of contributions, SCERS Staff shall conduct an investigation to determine the cause of the error. As soon as practicable, Staff shall form a plan to correct the error prospectively and retroactively in accordance with Sections A.1., A.2., B, and C above. (Staff shall consult with General Counsel, the Chief Benefits Officer, and/or the Chief Executive Officer as appropriate to determine whether Section

A.2.c. applies.) Staff may, in its discretion, decide not to pursue recovery when overpaid benefits are \$100 or less.

- b. Staff shall send a Notice of Correction (Notice) to the member containing information about the nature of the error and a proposed plan for prospective and retroactive corrections. Further requirements for the Notice are set forth in Section D.3 below. The Notice shall be sent via Certified Mail or other method that allows Staff to verify its receipt by the member.
- c. If the member does not object to the Notice of Correction in writing by the date identified in the letter (at least 30 days), the member will be deemed to have agreed and consented to all aspects of the Notice, including the proposed repayment plan. The repayment plan is thereafter deemed final, and SCERS will proceed to implement it. (The preceding is subject to any limiting requirements of the IRS or final, non-appealable, order of a court of competent jurisdiction.)
- d. If the member does not agree with the proposed correction plan in the Notice, or any other aspect of the Notice (e.g., whether SCERS correctly calculated the error), the member must object to the Notice in writing within the approximately 30 day period. In addition, the member may confer with the Chief Benefits Office (CBO) or designee and attempt to negotiate an agreement with alternative terms. Although the CBO or designee may agree to alternative repayment schedules, the CBO or designee is not authorized to enter into any agreements of compromise concerning prospective or retroactive corrections.
- e. If no agreement is reached between the member and Staff, the CBO will make an administrative decision regarding the scope of the error and the plan of correction.
- f. The member may appeal the CBO's decision in accordance with the "Appeal of SCERS' Administrative Decisions Policy." As a part of that appeal process, the Chief Executive Officer and/or the Board may consider an agreement of compromise in accordance with Section A.3. above.
- g. At the conclusion of the administrative appeal process, there should be a final administrative decision about the scope of the error and a plan of correction for SCERS to implement. (For example, if the member was unsuccessful in appealing the CBO's decision, then that will be the final administrative decision.) SCERS shall then take all reasonable steps to implement, administer, and enforce the final administrative decision. The Board may meet in closed session to consider whether to initiate any litigation so that SCERS may obtain and execute on a civil judgment (garnishing wages and attaching property).

2. Modified Procedures for Overpaid Persons Not Receiving Ongoing Benefits

Where SCERS has overpaid an individual that is not receiving ongoing benefits, a modified procedure applies.

After Staff sends a Notice of Correction pursuant to Section D.1.a. and D.1.b. above, Staff shall reach out to the individual and attempt to obtain his or her affirmative agreement to the

proposed repayment plan. The CBO (or designee) and the individual may also negotiate for some alternative repayment plan. If the agreement involves a compromise in the amount owed, the agreement must be reviewed and approved by the Chief Executive Officer and/or the Board (depending on whether the total overpayment exceeds \$50,000). Any such agreement must be in writing and fully executed by both parties.

If the parties come to terms on a plan for repayment, SCERS shall implement the agreed-upon plan. If the individual subsequently breaches the agreement, SCERS may, at its discretion, use any available legal remedy to enforce the agreement, including by obtaining a civil judgment against the individual and executing on the judgment (garnishing wages and attaching property).

If the parties cannot come to terms on a plan for repayment, then Section D.1.e. to D.1.g. will resume. At the end of the administrative appeal process, SCERS may take all reasonable steps to implement, administer, and enforce the final administrative decision, including by obtaining and executing on a civil judgment.

3. Contents of Notice of Correction

The Notice of Correction shall inform members that, if they have objections to any aspect of the Notice, they must contact Staff and/or the Chief Benefits Officer by a certain date. Generally, that date should be no less than 30 days after the member's receipt of the Notice. The Notice shall also inform members that they may submit an administrative appeal in accordance with the "Appeal of SCERS' Administrative Decisions Policy" to dispute the proposed correction plan or any aspect of the Notice.

In the event of an overpayment of a benefit to the member that is not subject to a fiduciary defense determination (Section A.2.a. and A.2.b.), the Notice shall inform the member of the amount of the prospective correction, the total amount previously overpaid to the member, and the amount of any interest charged. In addition, the Notice shall inform the member that the correction shall be made with the next available benefit payment after the Notice has been sent. The Notice shall identify the expected duration of the repayment to recover the overpaid amount plus interest. Finally, the Notice shall note that the proposed corrective plan will become subject to any order by the IRS and/or a final, non-appealable, order of a court of competent jurisdiction to make additional corrections.

With respect to overpayments of a benefit that are subject to a fiduciary defense (Section A.2.c.), the Notice of Correction shall specify the amount of the prospective correction, and that SCERS has decided for fiduciary and equitable reasons not to recover past overpayments from the member, but instead to include it in the Actuarial Accrued Liability, unless ordered to recoup it from the member by the IRS and/or a final, non-appealable, order of a court of competent jurisdiction.

In the event of any under-payment of contributions by the member, the Notice of Correction shall inform the member that the correction will commence, if practicable, with the next available payroll if the member is in active service or otherwise for deferred members, and that full contribution underpayment amount, plus interest on contributions, will need to be recouped to be entitled to the monthly benefits supported by those contributions. Unless

circumstances reasonably warrant otherwise, the correction applicable to underpaid contributions should occur over the same period of time as the error occurred.

4. Reports to the Board

The Chief Executive Officer shall annually report to the Board the amount of overpaid benefits and underpaid contributions in collection status. To protect the privacy rights of members, the report shall contain aggregate information only.

The first report shall be provided to the Board in January 2022 to reflect the prior calendar year activity, and every January thereafter.

RESPONSIBILITIES

Executive Owner: General Counsel

POLICY HISTORY

Date	Description
9-16-2020	Staff to recommend Board approve Policy.