Pension Administration: Problems and Solutions

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Public Pension Funds Need Independent Inspectors General

These massive pools of money are ripe for fraud without oversight by nonpartisan watchdogs.

By Mark Lee Greenblatt

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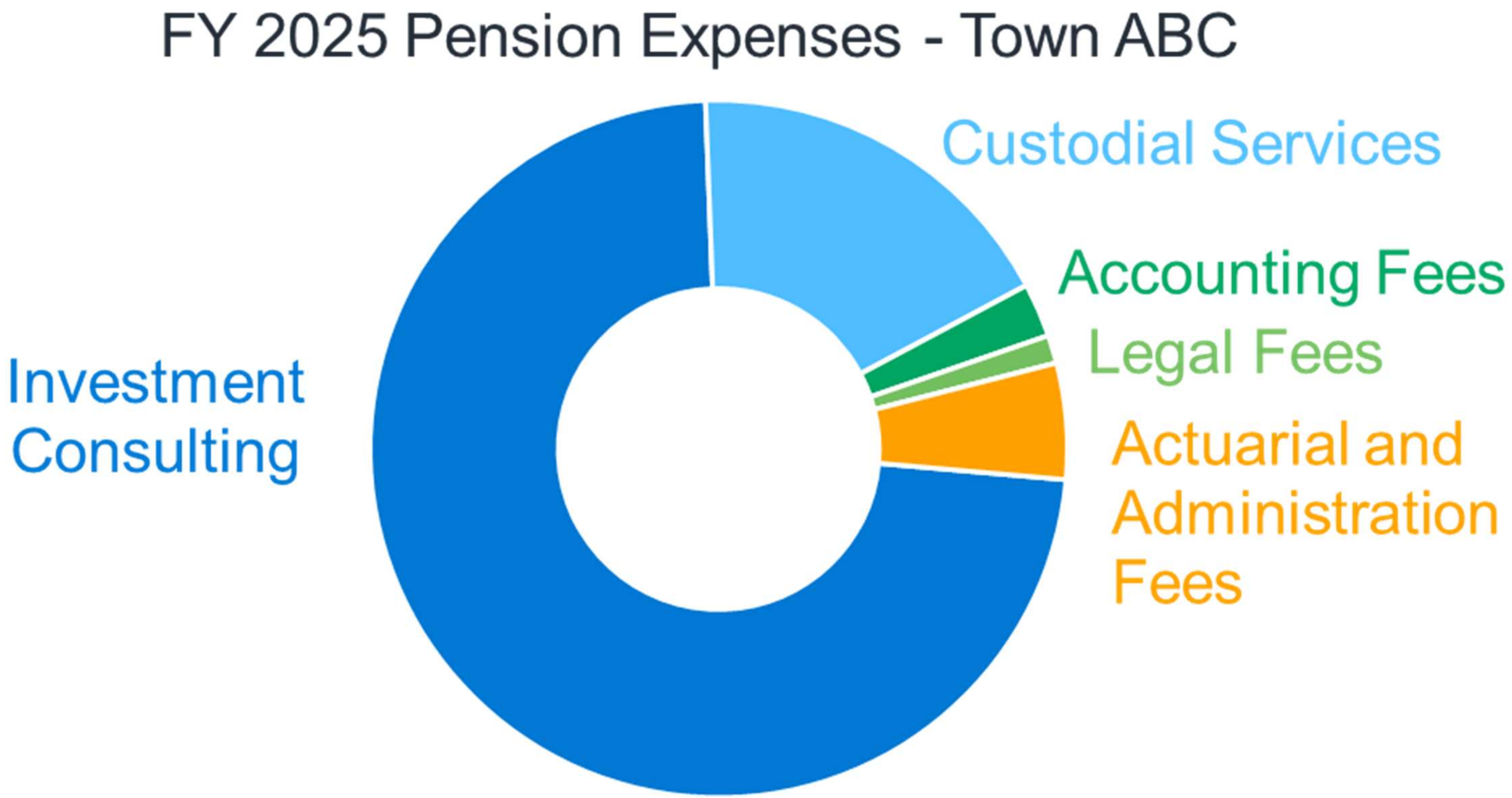
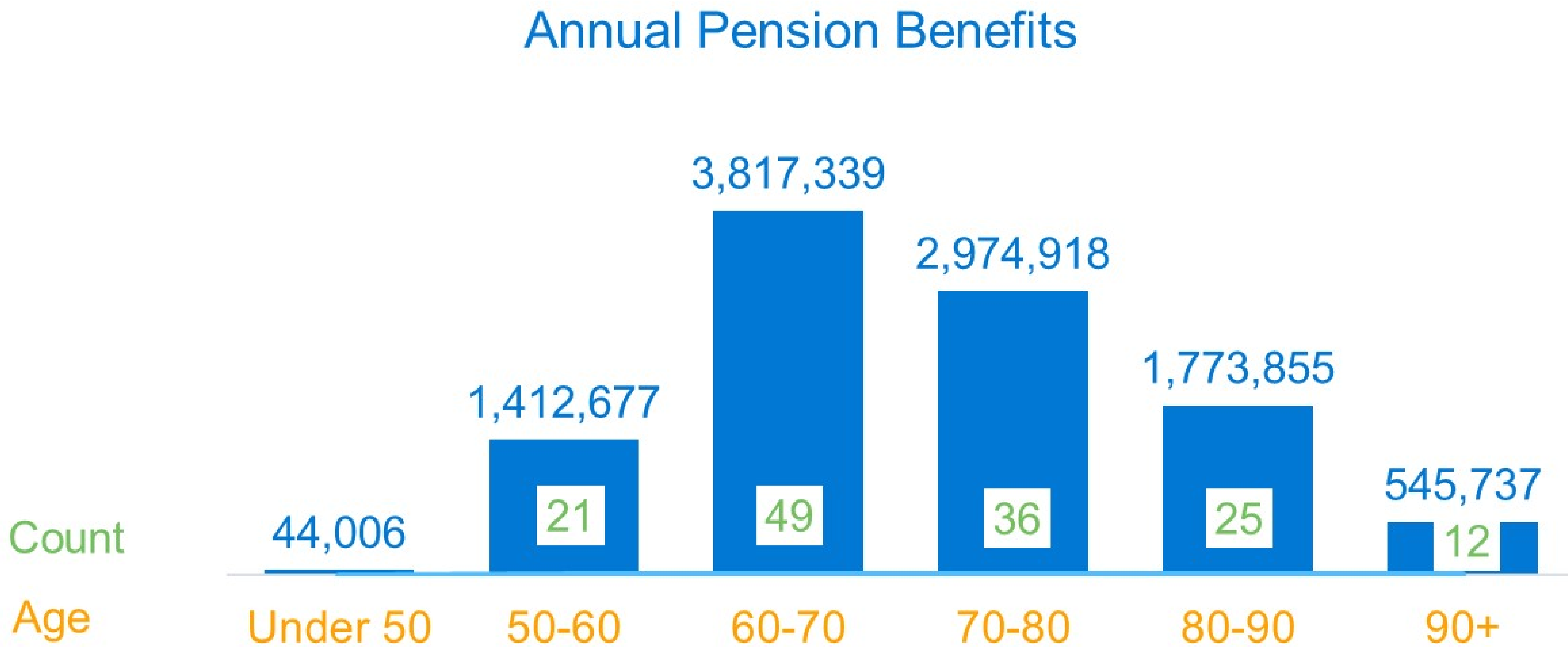
Wherever there's public money, someone is trying steal it. Public pension funds, which manage $6.1 trillion, are no different. Improper disability claims, falsified records and outright fraud have led in recent years to prosecutions and recovered funds. Some larger states and systems have internal audit and ethics offices to investigate waste, fraud and abuse. But smaller states and systems often lack the resources or independence to pursue mistakes and wrongdoing. Every public pension fund needs some form of independent oversight.

What we spend money (and time) on:



What a pension plan is for:



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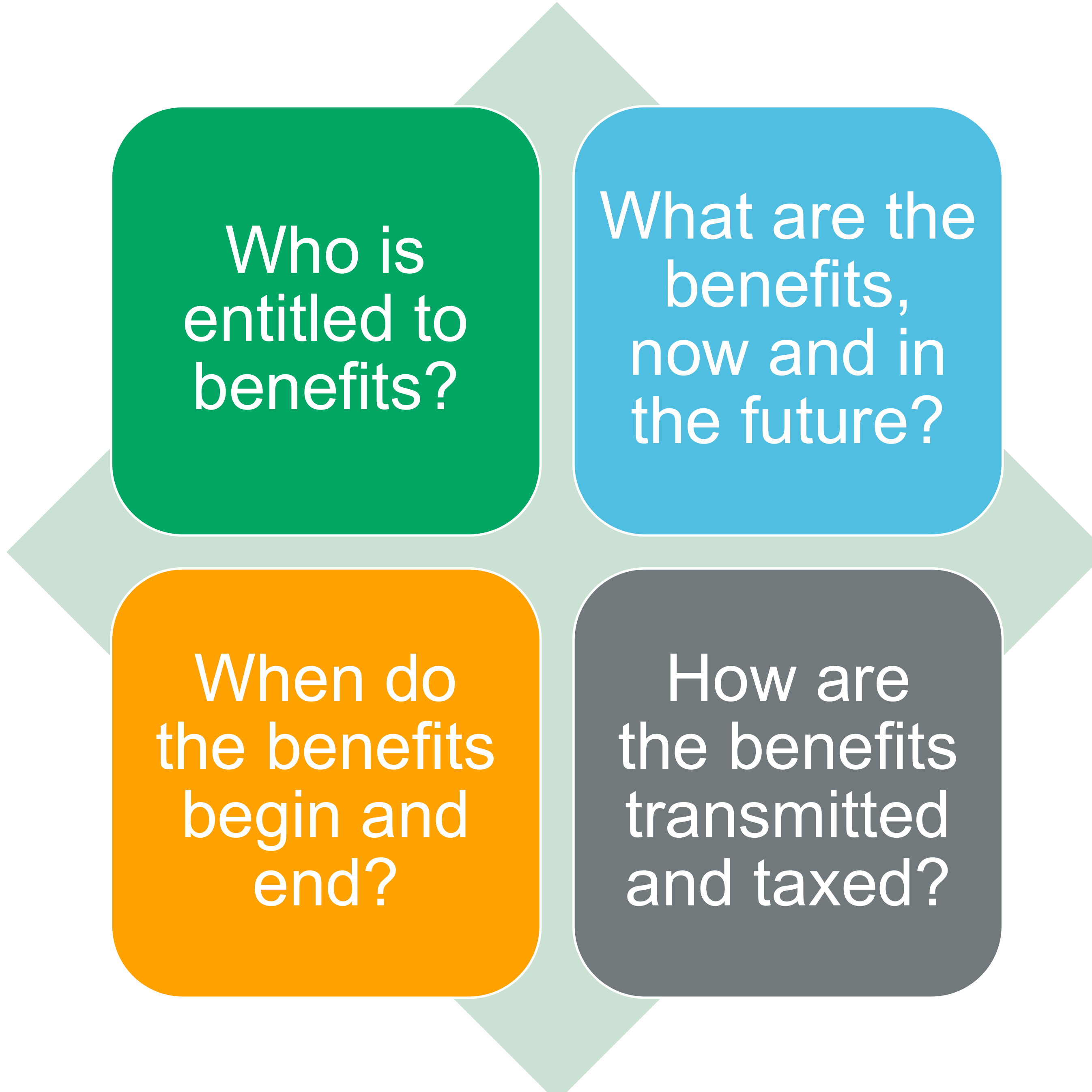
Key pension administration tasks



What can go wrong?

The data used to determine benefits is faulty

- Earnings used do not match the plan's definition of pensionable earnings
- Earnings from the wrong time period are used
- Dates of birth are wrong
- Wrong union / department identification
- Prior period of service is missed
- Service purchase is not reflected
- Employee contribution history is incomplete or incorrect
- Benefits payable to an alternate payee are not reflected

What can go wrong?

The calculations are faulty

- Hand calculations / old spreadsheets / plan factors are wrong
- Manual data entry errors
- Benefits are based on the wrong group / tier
- Benefits are not capped appropriately
- Prior service is for eligibility / benefits is incorrectly included / excluded
- Sick / vacation time is not reflected properly
- Rule of X is not calculated correctly
- Benefits payable to alternate payee are not adjusted to reflect life expectancy
- Statutory restrictions on non-spousal beneficiaries are not followed
- Statutory limits on annual benefits are not applied

What can go wrong?

The administration is faulty

- Benefits do not start or stop when they should
- Employee contributions do not start or stop when they should
- Employee contributions are not done on the proper pre-tax / post-tax basis
- Benefits are not properly taxed
- Refunds are not paid when the member terminates employment
- Accrued benefits are not calculated when the member terminates employment
- The correct optional payment forms are / are not being offered
- Non-level benefits do not change when they should
- COLA increases are not paid at the proper time / in the correct amount
- Disability benefits are not offset by workers comp, Social Security, etc.

What can go wrong?

No one knows what the benefits actually are

- Language is different in ordinances vs. plan documents vs. collective bargaining agreements vs. plan booklets vs. websites, etc.
- The plan document and calculation procedures are not amended when benefit changes are bargained
- Decisions on unclear or unwritten plan provisions are not memorialized in an administration policy document
- The details on data and benefit calculations are in one person's head
- Members in different departments deal with different HR people who may not all have the same understanding of how the plan works
- Members may not receive plain language plan booklets or have access to on-line information about their pension benefits

What can you to do get things right?

Audit the calculation process from beginning to end

- Reread the plan document and all supporting documentation
- Verify all sources of data
- Reengineer the data-gathering process to avoid manual errors
- Check that all calculations are correct
- Review the information and forms that are provided to members when they have a change in status
- Minimize manual data entry required for calculations

What can you to do get things right?

Clean up the plan documentation

- Create workflows that document the processes to follow when there is a change in status (hire, termination, retirement, death, disability, divorce, LOA, job change)
- Restate/amend the plan document
  - → Do this every time a change in benefits is bargained
  - → Make sure to pick up changes in applicable federal or state rules & regulations
- Review and update the plan booklet
- Compile a policy document to memorialize plan administration practices

What can you to do get things right?

Outsource the benefit payment function

- Pension benefits are subject to different taxation and tax withholding rules than employee payroll
- Retirees are often less computer savvy than employees, requiring a different type of customer service
- The pros have the robust infrastructure needed to automatically handle administration complexities such as non-level benefits, COLAs, required minimum distributions, pop-up joint & survivor annuities, cash refunds paid at death, etc.

What can you to do get things right?

Perform continuous death / address / eligibility searches

- Commercial death and address searches are very easy and inexpensive
- The sooner you are aware that a member has died, the sooner payments can be stopped or changed
- Have a process for searching for members approaching plan or retirement eligibility
- Contact terminated members as they approach retirement eligibility to get them into pay status and avoid the potential for paying out large retro amounts

What can you to do get things right?

Other best practices

- Pay refunds to all nonvested terminated members who are due them
- Determine accrued benefits for all vested terminated members
- Compile documentation for all Domestic Relations Orders and calculate benefits where possible
- Have your actuary review unusual or nonstandard calculations
- Engage a third party to conduct annual sampling audits of standard calculations
- Review the process for generating census data for actuarial valuations
  - → Minimize manual processing steps
  - → Standardize reporting across multiple payroll sources
  - → Ensure data codes are correct and being correctly interpreted by the actuary
  - → Check for missing or inconsistent data

What can you to do get things right?

More best practices

- Review compliance with data security and data privacy requirements
- Automate calculations and processes as much as possible
- Prepare annual benefit statements for active members
- Provide more educational opportunities so members have a better understanding of how the plan works
- Provide members with on-line access to plan documents and self-service tools (e.g., changes in address, tax withholding, direct deposit)
- Provide training for plan administration staff
- Consider ways to modify the plan provisions to remove potential administration stumbling blocks

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