

Refunds To Members Who Voluntarily Terminate Service With Less Than 10 Years of Creditable Service

Commonwealth of Massachusetts
Public Employee Retirement Administration Commission
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James Tivnan
Deputy Chief Auditor
August 17, 2010



MEMORANDUM #31, 2010

Commonwealth of Massachusetts | Public Employee Retirement Administration Commission
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Joseph E. Connarton, Executive Director

MEMORANDUM

TO: All Retirement Boards
FROM: Joseph E. Connarton, Executive Director
RE: Refunds to Members Who Voluntarily Terminate Service With Less Than 10 Years of Creditable Service
DATE: July 26, 2010

We have been contacted by several boards and staff expressing concern over the recently enacted FY11 State Budget (Chapter 131 of the Acts of 2010) section that impacts the calculation of interest for persons who became members after January 1, 1984 and request a refund of their contributions to the system. Section 25 provides that effective July 1, 2010, the annual rate of interest that will be paid when a member voluntarily withdraws from service and seeks a return of his or her contributions with less than 120 months (10 years) of creditable service will be 3%. The following is an effort to address these concerns.

This provision applies only to members voluntarily withdrawing from service with less than 10 years of creditable service, so the amount of interest credited to members' accounts before withdrawal remains unchanged at regular interest. The interest is calculated and applied only when the member withdraws his or her funds. Interest payable on the contribution refunds for those involuntarily withdrawing from service or for those with more than 10 years of creditable service will be set at regular interest. The 2 year limitation on the accrual of interest remains unchanged.

This is a fundamental change in the way the interest is calculated for refunds qualifying under this provision. A refund in these circumstances will include interest at a rate of 3% for the entire period, meaning that the interest credited for each year will be 3%. Previously, interest was awarded differently for those voluntarily leaving service with less than 5 or 10 years, and that provision in the law has now been superseded.

We are in the process of updating the PERAC form entitled Application for Withdrawal of Total Accumulated Deductions that was most recently revised September, 2009. This form allows a member to receive a refund of the total accumulated contributions in his or her Annuity Savings (retirement) account. During this interim transitional period, we continue to encourage use of this form. Manual editing is acceptable and encouraged.

The attachment provides specific examples using a manual or application based spreadsheet that Board staff can reference. We anticipate that the vendors and providers will be able to accommodate the changes associated with this change over time. Our examples are based on an inspection of the normal membership file Annuity Savings Record generally available on screen, print or manual records in most systems. You are encouraged to utilize this spreadsheet until the refund portion of the membership module can be adjusted to reflect the changes included in this notice. We do not anticipate any additional accounting tasks relative to this section. Refunds should continue to be disbursed using Refunds to Members #5757. The interest related to these refunds should continue to be applied through the membership module using the transfer process from the Pension Reserve Fund to the Annuity Savings Fund.

Board staff is encouraged to maintain a complete record and the associated documentation pertaining to both the refund as well as the original statutory regular interest applied to member's refunds under this section. These will be an essential reference in the event a member is reemployed with the same or another system subject to Chapter 32 and the provisions of this section.

Boards should carefully counsel members applying for a refund to assure that they are aware of the requirements and benefits of this section. Boards should provide a copy of the requirements of this section to such members. The current rules related to buy-backs are unchanged by this provision. Interested individuals should carefully consider whether a refund is appropriate in their situation.

We trust the foregoing is of assistance. Any questions should be directed to the PERAC audit unit: James.Tivnan@MassMail.State.MA.US.

SAMPLE REFUND CALCULATION AS REQUIRED BY PERAC MEMO #31/2010

Anonymous Member | 9 years creditable service | Decides to voluntarily leave for private sector | Entitled to 3% interest per statute

ASF Card Format	Current View																			
Name	Date of Membership	Unit: Group:	Deduction %	Total Creditable Service	Current Board Creditable Service	Interest	Other	Current Year Accumulated Deductions	Accumulated Deductions											
Year	Statutory Interest Rate	Deductions	Incremental 2% deductions	Transfer In/Make Up	Refund/Transfer Out	Interest	Other	Current Year Accumulated Deductions	Accumulated Deductions											
2002	1.40%	780.00	45.00	-	-	-	-	825.00	825.00											
2003	1.00%	3,148.80	187.20	-	-	8.25	-	3,344.25	4,169.25											
2004	0.60%	3,236.95	209.28	-	-	25.02	-	3,471.25	7,640.50											
2005	0.60%	3,506.08	341.99	-	-	45.84	-	3,893.91	11,534.41											
2006	0.60%	4,075.24	418.81	-	-	69.21	-	4,563.26	16,097.66											
2007	0.60%	4,488.00	522.00	-	-	96.59	-	5,106.59	21,204.25											
2008	0.60%	4,636.20	559.08	-	-	127.23	-	5,322.51	26,526.76											
2009	0.50%	4,905.12	626.28	-	-	132.63	-	5,664.03	32,190.79											
2010	0.30%	2,452.56	313.20	-	-	96.57	-	2,862.33	35,053.12											
		31,228.95	3,222.84	-	-	601.33	-	35,053.12												

ASF Card Format Revised by the provisions of Section 25, Chapter 131 of the acts of 2010

Name	Date of Membership	Unit: Group:	Deduction %	Total Creditable Service	Current Board Creditable Service	Interest	Other	Current Year Accumulated Deductions	Accumulated Deductions											
Year	Revised Statutory Interest Rate	Deductions	Incremental 2% deductions	Transfer In/Make Up	Refund/Transfer Out	Interest	Other	Current Year Accumulated Deductions	Accumulated Deductions											
2002	3.00%	780.00	45.00	-	-	-	-	825.00	825.00											
2003	3.00%	3,148.80	187.20	-	-	24.75	-	3,360.75	4,185.75											
2004	3.00%	3,236.95	209.28	-	-	125.57	-	3,571.80	7,757.55											
2005	3.00%	3,506.08	341.99	-	-	232.73	-	4,080.80	11,838.35											
2006	3.00%	4,075.24	418.81	-	-	355.15	-	4,849.20	16,687.55											
2007	3.00%	4,488.00	522.00	-	-	500.63	-	5,510.63	22,198.18											
2008	3.00%	4,636.20	559.08	-	-	665.95	-	5,861.23	28,059.40											
2009	3.00%	4,905.12	626.28	-	-	841.78	-	6,373.18	34,432.58											
2010	3.00%	2,452.56	313.20	-	-	516.49	-	3,282.25	37,714.83											
		31,228.95	3,222.84	-	-	3,263.04	-	37,714.83												
		Difference in interest to be applied to refund				2,661.71														

(Continued on the next page.)

NOTES PERTAINING TO SPREADSHEET ON PRIOR PAGE.

The deductions, 2% additional and interest in 2010 reflect 6 months of employment.

The current accounting involves adjusting the amount of the refund and the balance of the Annuity Savings account for interest not refunded #4822.

The revised accounting involves recognizing the additional interest to be refunded by increasing the balance of the Annuity Savings account for the additional interest.

In the above example, the additional interest to be refunded would be added to the balance of the Annuity Savings account and reflected in both the Investment Income to be credited to members' accounts as well as the total of Income Required for the Annuity Savings Fund as represented in the membership module.

IMPROVE BENEFITS FOR SHORT-SERVICE WORKERS BY PROVIDING INTEREST EQUAL TO THE ONE-YEAR TREASURY RATE ON ALL WITHDRAWN MEMBER CONTRIBUTIONS.

Rationale: Employees who leave public service with less than five years of service receive a refund of their contributions with no interest. Those who stay between five and ten years receive a small amount of interest, based on 50 percent of the rates paid on individual savings accounts at a sample of at least ten financial institutions. The current rate is 0.6 percent. Providing more

Substantial interest is important because Massachusetts workers are not accumulating any credits under Social Security while they work for the Commonwealth, and their state pension is not portable when moving outside the system.

Impact on cost: < 0.1% of PVB (\$25 million for the State and Teachers Systems)

QUESTIONS AND ANSWERS.

Q: A member had prior creditable service with three other Boards before transferring back to mine. How do I calculate the refund when I do not have a breakdown of the contributions by year?

A: Contact the other Boards for the data pertaining to the periods worked, deductions, 2% additional and interest for those specific periods.

Q: Does the 2 year limitation rule still apply?

A: Yes

Q: Will this 3% rate change from year to year - like the statutory interest rate does?

A: I don't believe the rate of 3% will change annually. The rule states a fixed 3% rate.

Q: What about a situation where a member has less than 10 years of service and decides to refund half and transfer half? Will the transfer portion use the original interest amount and the refund portion use the new interest amount? Or does the interest calculation change apply only to full refunds?

A: Whether a refund or rollover, the new rule applies. Use the 3% to calculate the interest for the total amount; then apply the portion to the rollover or refund in turn. Both portions use the 3% rule.

Q: Does the ten year inactive transfer to the PRF still apply?

A: Yes.

Q: Should we really change the member's prior year balances? Or should we figure out how much total interest to change and then make one adjustment in the current year?

A: The latter.

Q: What happens if a person *involuntarily* withdraws from service?

A: These who involuntarily leave service are in the category of "Any other member entitled to return of his accumulated total deduction shall receive 100 per cent of the rate of regular interest payable." so they get 100% of the regular interest, just like before.

Q: A firefighter had prior service with both another system and the Teachers Retirement System. He started with 8%, then transferred to MTRS for 11%, then back to us with 8%.

A: If the member retires from your system; with 30 + years of creditable service; keep the funds; the normal retirement formula applies. If they retire from your system with less than 30 years; you are supposed to refund the difference between the 11% and the 8 + 2%! If they transfer, transfer it all. PERAC Memo #24 in 2005 is the definitive reference that deals with this issue.

Q: How did the 3% rate become the standard?

A: The 3% rate is a "magic" number in the retirement community. The 3% rate limitation applies to annual COLA increases; and it is applied to annual changes in the Annuity Reserve Fund balances, likely related to the COLA increase.

FIRST PUBLIC JOB

Name	Date of Membership	Unit: Group:	Deduction %	Creditable Service dates	Total Credit-able Service	Current Board Credit-able Service
Jane Doe	5/22/2000	Admin	9+2%	5/22/2000 to 6/22/2001	0.6667	0.6667
Year	Statutory Interest Rate	Deductions	Incremental 2% deductions	Interest	Current Year Accumulated Deductions	Accumulated Deductions
1999	2.20%	-	-		-	-
2000	2.10%	1,001.11	-	-	1,001.11	1,001.11
2001	1.90%	1,190.78	-	19.02	1,209.80	2,210.91
2002	1.40%	-	-	30.95	30.95	2,241.86
2003	1.00%	-	-	22.42	22.42	2,264.28
2004	0.60%	-	-	13.59	13.59	2,277.87
2005	0.60%	-	-	2.28	2.28	2,280.15
2006	0.60%	-	-	-	-	-
2007	0.60%	-	-	-	-	-
2008	0.60%	-	-	-	-	-
2009	0.50%	-	-	-	-	-
2010	0.30%	-	-	-	-	-
		2,191.89	0.00	88.26	2,280.15	

SECOND PUBLIC JOB

Name	Date of Membership	Unit: Group:	Deduction %	Creditable Service dates	Current Board Creditable Service	Total Credit-able Service
Jane Doe	5/22/2000	Admin Group 1	9+2%	8/26/2002 to 6/30/2005	2.8333	3.5000
Year	Statutory Interest Rate	Deductions	Incremental 2% deductions	Interest	Current Year Accumulated Deductions	Accumulated Deductions
1999	2.20%	-	-		-	-
2000	2.10%	-	-	-	-	-
2001	1.90%	-	-	-	-	-
2002	1.40%	702.90	-	-	702.90	702.90
2003	1.00%	2,100.98	-	7.03	2,108.01	2,810.91
2004	0.60%	2,296.65	-	16.87	2,313.52	5,124.42
2005	0.60%	1,579.13	-	30.75	1,609.88	6,734.30
2006	0.60%	-	-	-	-	-
2007	0.60%	-	-	-	-	-
2008	0.60%	-	-	-	-	-
2009	0.50%	-	-	-	-	-
2010	0.30%	-	-	-	-	-
		6,679.66	0.00	54.64	6,734.30	

THIRD PUBLIC JOB

Name	Date of Membership	Unit: Group:	Deduction %	Creditable Service dates	Current Board Creditable Service	Total Creditable Service
Jane Doe	5/22/2000	Admin Group 1	9+2%	8/29/2006 - 2/29/2008	1.5000	5.0000
Year	Statutory Interest Rate	Deductions	Incremental 2% deductions	Interest	Current Year Accumulated Deductions	Accumulated Deductions
1999	2.20%	-	-	-	-	-
2000	2.10%	-	-	-	-	-
2001	1.90%	-	-	-	-	-
2002	1.40%	-	-	-	-	-
2003	1.00%	-	-	-	-	-
2004	0.60%	-	-	-	-	-
2005	0.60%	-	-	-	-	-
2006	0.60%	879.62	15.02	20.41	915.05	915.05
2007	0.60%	2,253.64	37.96	59.78	2,351.38	3,266.43
2008	0.60%	525.90	5.28	18.47	549.65	3,816.08
2009	0.50%	-	-	-	-	-
2010	0.30%	-	-	-	-	-
		3,659.16	58.26	98.66	3,816.08	

FOURTH PUBLIC JOB

Name	Date of Membership	Unit: Group:	Deduction %	Creditable Service dates	Current Board Creditable Service	Total Creditable Service
Jane Doe	5/22/2000	Admin Group 1	9+2%	3/1/2008 - 6/18/2010	2.3	7.3000
Year	Statutory Interest Rate	Deductions	Incremental 2% deductions	Interest	Current Year Accumulated Deductions	Accumulated Deductions
1999	2.20%	-	-	-	-	-
2000	2.10%	-	-	-	-	-
2001	1.90%	-	-	-	-	-
2002	1.40%	-	-	-	-	-
2003	1.00%	-	-	-	-	-
2004	0.60%	-	-	-	-	-
2005	0.60%	-	-	-	-	-
2006	0.60%	-	-	-	-	-
2007	0.60%	-	-	-	-	-
2008	0.60%	1,084.14	-	58.61	1,142.75	1,142.75
2009	0.50%	1,343.24	-	70.04	1,413.28	2,556.03
2010	0.30%	875.97	-	23.13	899.10	3,455.13
		3,303.35	0.00	151.78	3,455.13	

SUMMARY OF MEMBER CONTRIBUTIONS AND INTEREST

Member		Jane Doe				
7.3 years credit-able service			5	2.25	0.05	7.3
decides to voluntarily leave for private sector						
entitled to 3% interest per statute						
ASF Card Format	Current View					
Name	Date of Membership	Unit: Group:	Deduction %	Creditable Service dates	Current Board Creditable Service	Total Creditable Service
Jane Doe	5/22/2000	Admin Group 1	9+2%	5/22/2000 - 6/18/2010	2.3000	7.3000
Year	Statutory Interest Rate	Deductions	Incremental 2% deductions	Interest	Current Year Accumulated Deductions	Accumulated Deductions
1999	2.20%	-	-		-	-
2000	2.10%	1,001.11	-	-	1,001.11	1,001.11
2001	1.90%	1,190.78	-	19.02	1,209.80	2,210.91
2002	1.40%	702.90	-	30.95	733.85	2,944.76
2003	1.00%	2,100.98	-	29.45	2,130.43	5,075.19
2004	0.60%	2,296.65	-	30.46	2,327.11	7,402.30
2005	0.60%	1,579.13	-	33.03	1,612.16	9,014.46
2006	0.60%	879.82	15.02	54.09	948.93	9,963.39
2007	0.60%	2,253.64	37.96	59.78	2,351.38	12,314.77
2008	0.60%	1,610.04	5.28	77.08	1,692.40	14,007.17
2009	0.50%	1,343.24	-	70.04	1,413.28	15,420.45
2010	0.30%	875.97	-	23.13	899.10	16,319.55
		15,834.26	58.26	427.03	16,319.55	

The current accounting involves adjusting the amount of the refund and the balance of the Annuity Savings account for interest not refunded #4822.

REFUND CALCULATION AS REQUIRED BY PERAC MEMO #31/2010

Year	Revised Statutory Interest Rate	Deductions	Incremental 2% deductions	Interest	Current Year Accumulated Deductions	Accumulated Deductions
1999	3.00%	-		-	-	0.00
2000	3.00%	1,001.11		-	1,001.11	1,001.11
2001	3.00%	1,190.78		30.03	1,220.81	2,221.92
2002	3.00%	702.90		66.66	769.56	2,991.48
2003	3.00%	2,100.98		89.74	2,190.72	5,182.21
2004	3.00%	2,296.65		155.47	2,452.12	7,634.32
2005	3.00%	1,579.13		229.03	1,808.16	9,442.48
2006	3.00%	879.82	15.02	283.27	1,178.11	10,620.60
2007	3.00%	2,253.64	37.96	318.62	2,610.22	13,230.81
2008	3.00%	1,610.04	5.28	396.92	2,012.24	15,243.06
2009	3.00%	1,343.24		457.29	1,800.53	17,043.59
2010	3.00%	875.97		255.65	1,131.62	18,175.21
		15,834.26	58.26	2,282.69	18,175.21	
Difference in interest to be applied to refund				1,855.66	1,855.66	

The revised accounting involves recognizing the additional interest to be refunded by increasing the balance of the Annuity Savings account for the additional interest.

In the above example, the additional interest to be refunded would be added to the balance of the Annuity Savings account and reflected in both the Investment Income to be credited to members' accounts as well as the total of Income Required for the Annuity Savings Fund as represented in the membership module.

Retirement Board

Refund Breakdown

Note: 1099R will be mailed at the end of the year

Name

Social Security Number xxx-xx-xxxx

	OLD WAY	NEW WAY
Creditable Service Start Date	05/22/2000	same
Creditable Service End Date	06/18/2010	same
Withdrawal Date		same
Creditable Service	7.30	same
Total Accumulated Deductions	\$16,342.68	\$18,175.21
Refund of Contributions	\$15,892.52	\$15,892.52
Non-Taxable Contributions		
Refund of Interest		\$2,282.69
Non-Taxable Interest		
Interest not Refunded	(\$225.08)	
Taxable Portion of Refund	\$16,117.60	\$18,175.21
Non-Taxable Portion of Refund		
Federal Tax Withheld	(\$3,223.52)	(\$3,635.04)
Total Refund Amount	\$12,894.08	\$14,540.17

Notice

Note: Under IRS tax laws, this lump sum distribution may be rolled into an I.R.A. account within 60 days. If the taxable portion of this refund is not rolled over, we will have to withhold taxes at the rate of 20% and you may be subject to IRS penalties. This Retirement Plan falls under section 414(h)(2) of the IRS codes.

