

SDCERS NAVIGANT REPORT COMMITTEE/ STAKEHOLDER MEETING

February 15, 2006 - Meeting Notes

By Virginia Silverman

INTRODUCTION/PRELIMINARY

The Meeting was called to order by the Chair, Mark Sullivan, who introduced the other SDCERS Board members on the committee: Richard Kipperman, Thomas Hebrank and William Sheffler.

Sullivan asked the stakeholder representatives to stand and come to the front row seats. About five stakeholder representatives were in attendance.

COMMITTEE PURPOSE AND SCOPE/ STAKEHOLDER PARTICIPATION

1) Purpose and Scope:

Sullivan outlined the purpose and scope of the committee as follows: To study the recommendations in the Navigant Report (presented to the full SDCERS Board in January); to determine necessary actions/steps to restore fiscal health and strict independent governance, and to bring these proposals to the full SDCERS Board for approval.

2) Meeting Schedule:

All meetings are open to the public and will be at 1:00 p.m. on the second Wednesday of the month in the SDCERS offices. The meetings will continue at least through July. An agenda will be posted (on the SDCERS website?) 72 hours before the meeting. The meeting schedule and topics are as follows:

February 15, 2006 – IRS Voluntary Compliance Program

March 8, 2006 – Contingency Planning in the Event of City Bureaucracy/Restoring Funding Level and Actuarial Soundness (Gleason and Corbett Settlements, Prop. G/amortization)

April 12, 2006 - Governance and Education/ Restoring Funding Level and Actuarial Soundness (Reduce UAAL, EAN, amortization periods, eliminate waterfall, reserve accounts)

May 10, 2006 - Retiree Health Insurance/Governance and Education

June 14, 2006 – Safeguarding and Maintaining (SDCERS) Independence/Restoring Funding Levels and Actuarial Soundness.

July 12, 2006 – Other reform issues as the Committee deems necessary

REPORT BY TAX COUNSEL ON IRS VOLUNTARY CORRECTION PROGRAM

A lengthy presentation was made on the IRS Voluntary Correction Program (VCP) by attorneys Mary Beth Braitman and Terry Mumford of the Ice Miller law firm, SDCERS Tax Counsel. Under the IRS Voluntary Correction Program (VCP), the IRS works with agencies to correct problems in a non-punitive settlement. The goal of the SDCERS use of the VCP to protect the tax-qualified status of the SDCERS pension system)

The attorneys first reviewed the advantages of a ‘qualified’ tax status: employer

contributions not taxed when made, earnings and income from the trust not taxed until distributions made, and rollover of some distributions.

However, the Navigant report raised several concerns about the qualified tax status of the SDCERS plan, including: the operation of SDCERS in conformance with plan documents; overpayment of benefits from the Corbett settlement and Presidential Leave Benefit (the 13th check also mentioned verbally); payments of retiree health care from pension assets; payment from pension assets to administer the retiree health benefits; and contributions to the Presidential Leave Benefit

In March 2005, ICE Miller presented a road map too the SDCERS Board with the steps necessary for SDCERS to confirm its status with the IRS as a qualified governmental plan. In April, 2005, the SDCERS Board approved the IRS filing and compliance review.

Step 1 – Perform a Document Compliance Review

SDCERS staff identified documents comprising the plan document, including City ordinances and SDCERS Board minutes. In May, 2005 the Board adopted a resolution proposing technical compliance corrections for the City to adopt to bring the plan documents into compliance with IRS requirements. (The City has not yet acted).

Steps 2 and 3 – Prepare IRS submission for Determination Letter and VCP:

In July 2005, Ice Miller submitted an IRS determination letter (Form 5300) to the IRS, along with the initial filing of the Voluntary Correction Program (VCP). Both documents must be submitted together to obtain IRS confirmation of SDCERS qualified governmental plan status, and the ability to self-correct compliance mistakes. The initial filing included the health benefits payment issue, the Presidential Leave Benefit, and the Corbett and Andrews settlements, and advised the IRS that additional filings might be forthcoming as the result of ongoing compliance review efforts.

Step 4 – IRS Review of From 5300 and VCP

Ice Miller has not yet heard from the IRS about the filings from last July (the attorneys indicated it may take up to a year for a response. The attorneys said that IRS will work with Ice Miller and SDCERS and may request additional documents, and additional corrections. Any additional revisions or corrections will be brought back to the Board and/or City for appropriate action.

Step 5- Negotiate and Agree on Compliance Statement with IRS

The attorneys said it would take significant time to reach agreement, and would probably require supplemental filings.

Step 6 – Perform an operational compliance review

Steps will include review of retiree health benefit issues, minimum distribution rules, compensation limits and eligible rollover distributions, benefit and contribution limits, service purchase provisions, replacement benefit arrangements(?), DROP, and structure of plan and trust (Port and Airport issues), taxation and reporting of payments (2006), and the exclusive benefit rule (2006).

In addition to the above efforts, in September 2005, Ice Miller recommended revisions to DROP distributions to comply with Final IRS rules. These rules were implemented by January 1,

2006.

COMMENTS/QUESTIONS

Comment by Bill Farrar, President of the POA. Farrar raised issue of POA presidents serving shorter terms than other union presidents. .

Question (Sheffler): What kind of supplemental filings might there be? Answer (IM) Issues under 401(a) (the plan document; if operations conform to plan document minimum distribution rules, compensation limits, and eligible rollover distributions). It is always better to go to IRS than have them come to you. The goal is to permit equitable settlement without a punitive process.

Question (Sheffler): Does the compliance submission cover prior actions or mistakes(such as calculations for cost of purchase of service). Answer(IM): This was addressed in the initial filing. However, the health benefits issue (401(h) may still need other actions. DROP distributions sand the Port District/Airport issues are still open. Also, the exclusive benefit rule (Presidential Leave) is a prohibited transaction under IRS rules.

Question (Sheffler) : What if the City amends the plan document after the VC settlement? Answer (IM): the IRS works on a cycle; there will be another review in the next cycle and that would be addressed at that time.

Question (Hebrank): Will there be supplemental filings, particularly on health benefits? Answer (IM): IM has planned for supplemental filings if new information discovered in the operations compliance review. Regarding health benefits, IM needs to clarify the issues. Their assessment differed from Navigant's findings and may require a new submission.

Question (Hebrank): Has the City passed the corrective ordinances recommended by SDCERS? Answer (IM): No, there are in the City Attorney's office. SDCERS need to demonstrate that corrective ordinances are being passed.

Question (Prevolos): SDCERS administers two other plans, for the Port District and Airport Authority. The current arrangement (called a Multiple Employer Plan) has significant liabilities. If PD or airport wants to leave, can this be done? For example, could the Port District transfer its assets to another type of plan – 401K or cash balance? Answer (IM): IM recommends that the Board never do that without specific prior approval from the IRS. (They commented that a group trust encompassing three individual trusts would offer more protection than the Multiple Employer Plan).

Question: (Sullivan) Not all benefits are really the same, for example the Presidential Leave Benefit. The IRS ruling will be very slow, so City/SDCERS may have to make a choice – refund money to unions and let individuals contribute? Or?? Answer (IM): SDCERS would have to determine....what?

Comment: Bill Farrar, POA President, asked to speak again at this point, and said that only Ron Saathoff received two salaries. MEA and POA presidents did not receive City salaries

while serving as presidents; they were on approved Leave of Absence from the City. (The Civil Service Commission approves the leaves of absence annually) One past POA president who received the Presidential Leave Benefit has already retired. Farrar said that he signed DROP documents two years ago, but the SDCERS Board has never acted to approve DROP for him, Italiano or another past POA president.

Question (Sullivan): What would be the most conservative approach to the Presidential Leave Benefit? Answer (IM): Back out union contributions and refund the money and continue the process (presumably with the IRS?)

Comment (Fiduciary Counsel, sitting with Board): Presidential Leave raises significant questions under state and federal law. A study is needed to determine if the Presidential Leave Benefits has come to be relied upon in the past. If someone retires 3 months from now, should a (pension) check be cut or not be cut?

Comment (Prevolos): Could SDCERS cut a basic pension benefit for City employment, and set aside the rest in an escrow account until the IRS rules?

Comment (Kipperman): If nothing else, SDCERS should do something in the way of counsel if there is a bankruptcy filing. He thinks there may be a bankruptcy filing, and that it may be sudden, without warning.

ADJOURNMENT

Mark Sullivan asked for questions or comments by the Stakeholder representatives. There were none. Meeting adjourned.